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BUSINESS OVERVIEW

We are a PRC-based cigarette packaging paper manufacturer with research and development capabilities to supply customised products to our customers. We supply our products primarily to cigarette package manufacturers which operate in different provinces of the PRC, mainly including Hubei Province and Henan Province. The products sold by us are used in the manufacture of cigarette packages for well-known cigarette brands in the PRC. During the Track Record Period, a majority of our revenue was derived from the sales of cigarette packaging paper products applied for mid-to-high-end cigarettes, and our products were used as cigarette packaging materials for at least nine cigarette brands which were recognised as the “Dual 15 cigarette brands (雙十五煙草品牌)” by the STMA. The “Dual 15 cigarette brands” represent the 15 cigarette brands which derived the highest sales from mid-to-high-end cigarettes in 2020 in the PRC. According to the Industry Report, we were ranked as the largest cigarette packaging paper manufacturer (in terms of sales value) with a market share of approximately 14.9% in Hubei Province in 2020, and the tenth largest cigarette packaging paper manufacturer (in terms of sales value) with a market share of approximately 0.8% in the PRC in 2020.

During the Track Record Period, our revenue was mainly derived from the sale of cigarette packaging paper. Our products are categorised into (i) transfer paper; (ii) laminated paper; and (iii) frame paper. To a much lesser extent, we also provide cigarette packaging paper processing services to cigarette package manufacturers. The following table sets forth a breakdown of (i) our revenue, sales volume and average selling price by type of our cigarette packaging paper; and (ii) revenue generated from the provision of cigarette packaging paper processing services during the Track Record Period:

	FY2019			FY2020			FY2021					
	% of total Revenue	Sales volume	Average selling price	% of total Revenue	Sales volume	Average selling price	% of total Revenue	Sales volume	Average selling price			
	RMB'000	tonnes	RMB per tonne	RMB'000	tonnes	RMB per tonne	RMB'000	tonnes	RMB per tonne			
Sale of cigarette packaging paper												
— Transfer paper	246,017	78.6	16,162	15,200	253,250	79.6	17,326	14,600	312,741	84.5	20,357	15,400
— Laminated paper	61,414	19.6	5,517	11,100	59,616	18.7	5,553	10,700	55,889	15.1	5,137	10,900
— Frame paper	2,328	0.8	312	7,500	1,486	0.4	175	8,500	1,594	0.3	180	8,800
Sub-total	309,759	99.0	21,991	314,352	23,054	98.7	23,054	370,224	25,674	99.9	25,674	
Provision of cigarette packaging paper processing services												
	3,041	1.0		3,994	1.3			87	0.1			
Total	312,800	100.0		318,346	100.0			370,311	100.0			

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During the Track Record Period, we manufactured all our products at our self-owned production facility in Hong’an County, Huanggang, Hubei Province with a gross floor area of approximately 12,000 sq.m.. Geographically, we are in proximity to sizeable regional cigarette manufacturing markets, such as Hubei, Hunan and Henan where a number of cigarette and related packages manufacturers operate. We also have close access to the extensive transportation networks in Wuhan City, Hubei Province which greatly facilitates our logistics and transportation arrangements.

We are committed to investing in our machinery to enhance our production efficiency and ensure our product quality. As at the Latest Practicable Date, we operated a total of seven production lines. Our production lines are commonly applicable to the production of transfer paper, laminated paper and frame paper. Our principal machinery includes laminating machine, crosscutting machine and winding machine. We also possess various testing equipment to conduct measurement on the colour shading, temperature resistance and chemical compositions of our products. Our machinery is well equipped to be used for producing products with different specifications. For further details on our production facility, please refer to the paragraph headed “Production facility and capacity — Production facility” below in this section.

Our Group places emphasis on research and development. For FY2019, FY2020 and FY2021, the expenses incurred by us on research and development amounted to approximately RMB10.7 million, RMB10.4 million and RMB13.1 million, respectively. Our research and development department comprised 18 personnel as at the Latest Practicable Date. Through our research and development, we had continuously enhanced the anti-counterfeit features, appearances and eco-friendliness of our products, improved our production efficiency and expanded our product offerings in terms of texture, durability and colour mixture. In 2018, we have collaborated with a university in Xi’an in the development of new products and fine-tuning of our production process. In 2021, we have further collaborated with the university in the advancement of our technological innovation capacity. For further information, please refer to the paragraph headed “Research and development” below in this section. As at the Latest Practicable Date, our Group had registered 24 patents in the PRC which are, in the opinion of our Directors, material to our business. For further information, please refer to the paragraph headed “Intellectual property” below in this section.

We believe that our understanding of our customers’ needs and our ability to deliver quality and customised products have been crucial to our success in maintaining stable relationship with our existing customers and attracting new customers. Regular communication and interaction with our customers allows us to stay abreast of the latest trend and development of our customers’ product requirements and facilitates us in further enhancing our product and technical development to maintain and improve the market appeal of our products. We have maintained a stable customer base during the Track Record Period. For FY2019, FY2020 and FY2021, we had generated sales from 37, 40 and 34 customers, respectively. For FY2019, FY2020 and FY2021, the percentage of our total revenue attributable to our top five customers combined amounted to approximately 62.7%, 68.6% and 75.4%, respectively. We had established business relationship with Customer E (being one of our top customers during the Track Record Period) for seven years. In addition, some of our top customers are established market players in the cigarette package manufacturing industry. For instance, Hubei Golden Three Gorges is a subsidiary of a company listed on the

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Stock Exchange, whereas Customer Group C are subsidiaries of state-owned enterprises in the PRC. For further details on our top customers, please refer to the paragraph headed “Our customers – Top customers” below in this section.

The principal types of raw materials for our production process include white cardboard, film and other accessory materials such as glue and ink. We source raw materials from various suppliers in the PRC. To ensure our product quality, our raw materials procurement policy is to make procurement from those approved suppliers who have passed our quality control assessment and have a satisfactory record of quality and on-time delivery. As at 31 December 2021, we had more than 120 approved suppliers on our internal list.

We believe that the quality and reliability of our products are critical to our success. We have established quality assurance standards to meet our customers’ requirements. As at the Latest Practicable Date, our quality control department was staffed with 11 personnel to implement our quality management system. Our quality control manager has over 15 years of relevant industry experience. Under our quality management system, we conduct quality control testing at various stages throughout our production process, including (i) incoming quality check on raw materials; (ii) quality control throughout the production process; and (iii) outgoing quality check on finished products. Our quality management system has been certified to be in compliance with ISO 9001 certification. In addition, in recognition of our commitment to work safety and environmental protection, our occupational health and safety management system and environmental management system have been certified to be in compliance with ISO 45001 certification and ISO 14001 certification, respectively. For further details, please refer to the paragraphs headed “Quality control”, “Occupational health and safety” and “Environmental, social and corporate governance matters” below in this section.

Our Directors believe that we have built up reputation as an established cigarette packaging paper manufacturer in the PRC. We were recognised as “High and New Technology Enterprise” (高新技術企業) by the Department of Science and Technology of Hubei Province (湖北省科學技術廳), the Department of Finance of Hubei Province (湖北省財政廳) and the Hubei Provincial Tax Service, State Taxation Administration (國家稅務總局湖北省稅務局) since November 2017 and was awarded “Hong’an County 2015–2017 Outstanding Enterprises in Scientific and Technological Innovation Work” (紅安縣2015–2017年度科技創新工作成果突出企業) by Hong’an County People’s Government (紅安縣人民政府) in December 2018. We were also recognised as “The 2019 (7th) Huanggang City Excellent Enterprise (Golden Eagle Award) (2019年(第七屆)黃岡市優秀企業(金鷹獎))” by the Huanggang City Entrepreneurs Association of Hubei Province* (湖北省黃岡市企業家協會) and Huanggang City Enterprise Confederation* (黃岡市企業聯合會) in May 2019. For further information, please refer to the paragraph headed “Certification and recognitions” below in this section.

According to the Industry Report, the total sales value of cigarette packaging paper in the PRC is forecasted to grow from approximately RMB41,155.9 million in 2022 to RMB44,349.5 million in 2025. The forecasted increase in sales value of cigarette packaging paper manufacturing industry in the PRC is mainly attributable to (i) the continuation of the focus of cigarette industry towards mid-to-high-end cigarettes. Mid-to-high-end cigarettes, which are charged at a higher selling price, generally entail the use of cigarette packaging paper with advanced technical requirements so as to enhance their brand recognition and product appeal; and (ii) the increase in

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purchasing power of PRC citizens will likely result in a growth in demand for mid-to-high-end cigarettes. Driven by the PRC Government’s policy in promoting mid-to-high-end cigarettes such as the “Three qualities strategy (三品戰略)” which emphasises on improving the quality of cigarettes, variety of cigarette products and reputation of cigarette brands and the “136/345 development goals” which represent a series of targets related to the expansion of cigarette brands that the PRC Government is aiming to achieve in the next four to five years, the demand for mid-to-high-end cigarette packaging paper is expected to maintain a steady growth. With our product quality, experienced management team and past track record, our Directors believe that we are well-positioned to capture the growing demand for mid-to-high-end cigarette packaging paper in the PRC. For details on the industry drivers relating to our Group, please refer to the section headed “Industry overview — Industry drivers and opportunities” in this document.

COMPETITIVE STRENGTHS

We believe that we have the following competitive strengths:

We have established stable business relationship with established cigarette package manufacturers which supply cigarette packages for well-known cigarette brands in the PRC

We supply our products primarily to cigarette package manufacturers. The products sold by us are used in the manufacture of cigarette packages for well-known cigarette brands in the PRC. During the Track Record Period, our products were used as cigarette packaging materials for at least nine cigarette brands which were recognised as the “Dual 15 cigarette brands (雙十五煙草品牌)” by the STMA. The “Dual 15 cigarette brands” represent the 15 cigarette brands which derived the highest sales from mid-to-high-end cigarettes in 2020 in the PRC. We believe that being a supplier for established cigarette package manufacturers has enhanced our market position and industry recognition.

Our customers operate in different provinces of the PRC, mainly including Hubei Province and Henan Province. We had established business relationship with Customer E (being one of our top customers during the Track Record Period) for seven years. In addition, some of our top customers are established market players in the cigarette package manufacturing industry. For instance, Hubei Golden Three Gorges is a subsidiary of a company listed on the Stock Exchange, whereas Customer Group C are subsidiaries of state-owned enterprises in the PRC. For further details on our top customers, please refer to the paragraph headed “Our customers – Top customers” below in this section.

According to the Industry Report, cigarette brand companies generally place emphasis on the consistency and standardisation of their cigarette packages as these are crucial to their brand recognition and product appeal. As such, consistency in the supply and quality of cigarette packaging paper is highly regarded by cigarette package manufacturers as well as cigarette manufacturers. Our customers generally engage us through direct negotiation or tender selection process. If our quotation or tender is accepted by our customers, they will typically confirm our engagement by entering into a framework sales agreement with us. If our customers are satisfied with the quality of our products, they would likely renew the framework sales agreement with us upon its expiry under a new unit price for the products with similar terms and conditions. Based on the aforesaid, our Directors consider that we are well-positioned to maintain the relationship with existing customers so long as our products consistently comply with their standards and

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requirements. With the effort of our senior management team, we have established stable business relationship with our existing customers and have maintained a generally stable customer base during the Track Record Period. The length of our relationships with major customers ranged from two years to seven years. Our customer base spans across various provinces in China, which facilitates us to further expand our potential customer base and explore new business opportunities.

Our Group has made consistent effort in geographic expansion and diversifying our customer base. Our sales representatives have engaged in business development and marketing activities in various provinces in the PRC. They are responsible for (i) enhancing our promotion and sales efforts; (ii) actively approaching and liaising with our existing and potential customers; and (iii) collecting feedbacks and handling any queries on our products from customers in those provinces. While our customers are mainly located in Hubei Province and Henan Province, we strive to expand our reach to customers located at different provinces in the PRC. For example, our Group has established business relationship with (i) a cigarette package manufacturer, being a subsidiary of a state-owned enterprise in the PRC, with its headquarters in Shanghai Municipality in FY2019; (ii) a cigarette package manufacturer (being listed on the Shanghai Stock Exchange) with its headquarters in Anhui Province in FY2020; and (iii) a cigarette package manufacturer located in Yunnan Province, which is a subsidiary of a state-owned cigarette manufacturer, in FY2020.

We are an established cigarette packaging paper manufacturer located strategically in Hubei Province with solid production capacity

We have an established market position in the cigarette packaging paper manufacturing industry in Hubei Province. According to the Industry Report, we were ranked as the largest cigarette packaging paper manufacturer (in terms of sales value) in Hubei Province in 2020, with a market share of approximately 14.9% in Hubei Province.

Our production facility is located in Hong'an County, Huanggang, Hubei Province with a gross floor area of approximately 12,000 sq.m.. Geographically, we are in proximity to sizeable regional cigarette manufacturing markets, such as Hubei, Hunan and Henan where a number of cigarette and related packages manufacturers operate. We also have close access to the extensive transportation networks in Wuhan City, Hubei Province which greatly facilitates our logistics and transportation arrangements. Since cigarette packaging paper is generally bulky and heavy, we believe our strategic location in Hubei Province allows us to have better access to our target customers, shorten the delivery time of products and minimise our logistics and transportation costs.

As at the Latest Practicable Date, we operated a total of seven production lines. Our production lines are commonly applicable to the production of transfer paper, laminated paper and frame paper. We are committed to investing in our machinery to enhance our production efficiency and ensure our product quality. Our principal machinery includes laminating machine, crosscutting machine and winding machine. We also possess various testing equipment to conduct measurement on the colour shading, temperature resistance and chemical compositions of our products. Leveraging our solid production capacity, we are able to schedule our production flexibly, promptly respond to our customers' requirements and ensure timely delivery of products at the required volume.

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We possess research and development capabilities to supply customised products to our customers

We constantly strive to differentiate ourselves from our competitors through providing customised products that match with the evolving requirements and specifications of our customers. We believe that our ability to supply customised products has allowed us to build up a stable and sustainable customer base. In addition, through regular communication and interaction with our customers, we are able to stay abreast of the latest trend and development of our customers’ products requirements. Our research and development department comprised 18 personnel as at the Latest Practicable Date and 17 of them have worked with us for over three years. Through our research and development, we had continuously enhanced the anti-counterfeit features, appearances and eco-friendliness of our products, improved our production efficiency and expanded our product offerings in terms of texture, durability and colour mixture. For FY2019, FY2020 and FY2021, the expenses incurred by us on research and development amounted to approximately RMB10.7 million, RMB10.4 million and RMB13.1 million, respectively. In 2018, we have collaborated with a university in Xi’an in the development of new products and fine-tuning of our production process. In 2021, we have further collaborated with the university in the advancement of our technological innovation capacity. As at the Latest Practicable Date, our Group had registered 24 patents in the PRC which are, in the opinion of our Directors, material to our business. For further information, please refer to the paragraph headed “Intellectual property” below in this section. Moreover, as at the Latest Practicable Date, we possessed more than ten sets of equipment for performing testing in the process of research and development.

We were recognised as “High and New Technology Enterprise” (高新技術企業) by the Department of Science and Technology of Hubei Province (湖北省科學技術廳), the Department of Finance of Hubei Province (湖北省財政廳) and the Hubei Provincial Tax Service, State Taxation Administration (國家稅務總局湖北省稅務局) since November 2017 and was awarded “Hong’an County 2015–2017 Outstanding Enterprises in Scientific and Technological Innovation Work” (紅安縣2015–2017年度科技創新工作成果突出企業) by Hong’an County People’s Government (紅安縣人民政府) in December 2018. We believe our commitment to research and development represent our core competitive strength and will continue to play a major role in our business going forward.

We implement stringent quality control management to ensure a high quality standard

We believe that the quality and reliability of our products are critical to our success. We have established quality assurance standards to meet our customers’ requirements. As at the Latest Practicable Date, our quality control department was staffed with 11 personnel to implement our quality management system. Our quality control manager has over 15 years of relevant industry experience. Our quality management system has been certified to be in compliance with ISO 9001 certification. We have incorporated features of Total Productive Maintenance (TPM) to maintain and enhance the performance efficiency of our production facility. In addition, in recognition of our commitment to work safety and environmental protection, our occupational health and safety management system and environmental management system have been certified to be in compliance with ISO 45001 certification and ISO 14001 certification, respectively.

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In order to meet our customers’ requirements on product quality, we have implemented stringent quality control procedures for each stage of our production process, including (i) incoming quality check on raw materials; (ii) quality control throughout the production process; and (iii) outgoing quality check on finished products. To ensure our product quality, our raw materials procurement policy is to make procurement from those approved suppliers who have passed our quality control assessment and have a satisfactory record of quality and on-time delivery. We also monitor our manufacturing processes and conduct series of testing with a view to ensuring that our products have a low defect rate and meet the expectations of our customers. In addition, we communicate regularly with our customers to obtain feedback on the quality standards of our products.

We have an experienced management team

We have an experienced management team. Mr. Chen, our Chairman and an executive Director, has over 25 years of experience in business management in various industries, including the paper industry in the PRC. Mr. Chen is responsible for the overall management and formulation of business strategies of our Group. Mr. Yu, an executive Director and chief executive officer of our Group, has over 25 years of experience in the cigarette industry, including the cigarette packaging industry. Mr. Yu is responsible for the overall management and day-to-day management of the operations of our Group. Our executive Directors are supported by our senior management who possess practical skills and experience. Mr. Bao Zhigang, our chief technology officer, has over 15 years of experience in the paper industry and Mr. Song Zhengmei, our chief product officer, has over 10 years of experience in product quality control. For the biographical details of our Directors and senior management, please refer to the section headed “Directors and senior management” of this document. With the experience of our executive Directors and senior management, we believe that we are able to strengthen our presence in the market we operate.

We believe that the networks of our executive Directors and senior management with the cigarette package manufacturers have enabled them to understand the needs of the cigarette package manufacturers, thereby allowing them to better anticipate and fulfil our customers’ requirements in a timely and responsive manner and adopt better strategies in securing regular and recurring business and explore more new business opportunities which are crucial to the continuous development of our Group. Our Directors also believe that the profound industry knowledge of our management team are critical to the efficiency of our production and overall development of our business.

BUSINESS STRATEGIES

The principal business objective of our Group is to further strengthen our market position, increase our market share and capture the growth in the PRC cigarette packaging paper manufacturing industry. We intend to achieve our business objective mainly by (i) expanding our production capacity, production efficiency and product portfolio; (ii) enhancing our research and development capabilities; (iii) enhancing our enterprise resource planning system and infrastructure systems to improve our operational efficiency; and (iv) increasing our marketing efforts in various provinces in the PRC.

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In this connection, our key business strategies are as follows:

Expanding our production capacity, production efficiency and product portfolio

(I) Increasing demand for mid-to-high-end cigarettes and higher quality cigarette packaging paper in the PRC

According to our PRC Legal Advisers, the PRC Government has issued a series of tobacco control policies or health promotion plans which aim to reduce the smoking population in the PRC. Notwithstanding the tightened regulations on smoking control, it is expected that the demand for tobacco products and the number of smokers in the PRC will remain stable according to the Industry Report, mainly due to (i) the enforcement of smoking control is inherently difficult and often costly, taking into account the government cost to be incurred for deploying officers for patrol, human resources for responding to complaints and reports, as well as expenses in relation to prosecution or other enforcement actions against smokers who are in breach of the regulations; and (ii) the PRC Government has not imposed absolute ban on smoking, nor is there any indication that the PRC Government is inclined to do so in the foreseeable future. Hence, it is expected that the demand for tobacco products will remain stable in the forecast period. The number of smokers in the PRC is expected to remain stable at approximately 300 million and the sales volume of cigarettes is forecasted to increase from approximately 2,410.3 billion sticks in 2022 to 2,466.9 billion sticks in 2025 at a CAGR of approximately 0.8%.

Along with the promotion of tobacco withdrawal, the PRC Government has taken the health promotion initiative to steer the consumption of cigarettes towards mid-to-high-end cigarettes which are generally associated with higher quality and inflict less harmful effect on health. This, in turn, encourages a shift in the focus of cigarette manufacturers on promoting mid-to-high-end cigarettes. According to the Industry Report, the percentage of sales volume of mid-to-high-end cigarettes, as represented by tier 1 to tier 3 cigarettes, over the total sales volume of cigarettes in the PRC increased from approximately 90.8% for FY2019 to approximately 94.3% for FY2020 and further increased to approximately 96.0% for FY2021. Driven by the PRC Government's health promotion initiative in steering the consumption of cigarettes towards mid-to-high-end cigarettes, which are generally charged at a higher selling price, it is forecasted that the sales value of cigarettes will continue to grow from 2022 to 2025 in the PRC.

Mid-to-high-end cigarettes generally entail the use of cigarette packaging paper with higher quality requirements as the quality of cigarette packaging to a large extent reflects the brand premium of the cigarettes contained in it. According to the Industry Report, the sales value of cigarette packaging paper manufacturing industry in the PRC is forecasted to increase from approximately RMB41,155.9 million in 2022 to RMB44,349.5 million in 2025, at a CAGR of approximately 2.5%, which is mainly attributable to (i) the continuous focus of the cigarette industry towards mid-to-high-end cigarettes; and (ii) the expected increase in per capita disposal income in the PRC that will likely result in an increase in purchasing power of PRC citizens and their spending on mid-to-high-end cigarettes. In light of the expected growth in cigarette packaging paper manufacturing industry and the increasingly stringent technical and quality requirements of cigarette packaging paper associated with the increase in demand for mid-to-high-

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end cigarettes in the PRC, our Directors consider that it is imperative for our Group to further expand our production capacity and product portfolio through the acquisition of more advanced production machinery.

(II) Outperformance of our Group as compared to the industry trend during the Track Record Period

According to the Industry Report, the sales volume of cigarettes in the PRC decreased by approximately 0.2% in FY2019 and remained relatively stable in FY2020; whereas the sales volume of cigarettes in Hubei remained relatively stable in FY2019 and decreased by approximately 1.3% in FY2020. Notwithstanding the decrease in the sales volume of cigarettes in the PRC and Hubei during the Track Record Period, our Group was able to achieve an increase in sales volume of cigarette packaging paper by approximately 33.7% in FY2019 and approximately 4.8% in FY2020, which was mainly attributable to the followings:

- (i) *The composition of our product mix:* according to the Industry Report, the overall sales volume and value of mid-to-high-end cigarettes, as represented by tier 1 to tier 3 cigarettes, in the PRC have recorded an increment during the Track Record Period as driven by the PRC Government's policy in promoting mid-to-high-end cigarettes. For FY2019, FY2020 and FY2021, the sales volume of mid-to-high-end cigarettes in the PRC was approximately 2,150.4 billion sticks, 2,233.4 billion sticks and 2,291.1 billion sticks, representing approximately 90.8%, 94.3% and 96.0% of the total sales volume of cigarettes in the PRC, respectively.

During the Track Record Period, a majority of our revenue was derived from the sales of cigarette packaging paper products applied for mid-to-high-end cigarettes. Our revenue generated therefrom increased from approximately RMB292.8 million for FY2019 to approximately RMB358.7 million for FY2021, representing an increase of approximately 22.5%. Our Directors consider that the increase in our revenue derived and sales volume generated from cigarette packaging paper products applied for mid-to-high-end cigarettes was primarily driven by the increase in volume and proportion of mid-to-high end cigarettes sold in the PRC as aforementioned; and

- (ii) *Expansion in our production capacity to cater to orders from existing and new customers:* along with the expansion in our production scale following the addition of three new production lines and replacement of two of our then existing production lines in FY2018, the maximum production capacity of our production facility increased from approximately 19,019 tonnes for FY2018 to approximately 28,028 tonnes for FY2019. For further details, please refer to the paragraph headed "Production Facility and Capacity — Utilisation rate" in this section. Such increase in our maximum production capacity enabled our Group to cater to the increase in demand from some of our existing major customers as well as new customers. In particular, our Group's sales volume to Change Dayang increased from approximately 315 tonnes for FY2018 to approximately 1,293 tonnes for FY2019, while our Group's sales volume to Customer Group C increased from approximately 1,309 tonnes for FY2018 to approximately 2,107 tonnes for FY2019. Besides, attributable to our consistent effort in diversifying our customer

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base to secure new business opportunities, our number of customers increased from 22 for FY2018 to 37 for FY2019 and these new customers in FY2019 contributed sales volume of approximately 4,654 tonnes to our Group in aggregate for FY2019.

While the cigarette packaging paper manufacturing industry in the PRC is forecasted to achieve nominal growth from 2022 to 2025, our Directors consider that, with the successful implementation of our business strategies, we will continue to outperform the industry trend, taking into account our operation history and financial performance during the Track Record Period. Our Group’s revenue and gross profit increased at a CAGR of approximately 8.8% and 11.5%, respectively, from FY2019 to FY2021 which largely outmatched the industry growth of approximately 1.9% in the PRC cigarette packaging paper manufacturing industry in terms of sales value during the corresponding period. Leveraging (i) our production capability and ability in fulfilling the stringent requirements of various cigarette package manufacturers and well-known cigarette brands in the PRC; (ii) our ability in manufacturing quality cigarette packaging paper for the use by mid-to-high-end cigarette brands and our products being used as cigarette packaging materials for at least nine cigarette brands which were recognised as the “Dual 15 cigarette brands (雙十五煙草品牌)” by the STMA. The “Dual 15 cigarette brands” represent the 15 cigarette brands which derived the highest sales from mid-to-high-end cigarettes in 2020 in the PRC; (iii) our ability in providing customised products that match with the evolving requirements and specifications of our customers; and (iv) the increase in the consumption proportion of mid-to-high-end cigarettes in recent years as explained above, our Directors consider that, with the successful implementation of our business strategies, our Group will continue to achieve business expansion and outperform the forecasted industry growth rate in the PRC cigarette packaging paper manufacturing industry.

(III) Continuous diversification of customer base and geographical expansion

Our Group has made consistent effort in diversifying our customer base. Our customers include various cigarette package manufacturers which provide cigarette packages to various well-known cigarette brands in the PRC. In particular, FY2019, FY2020 and FY2021, approximately 64.6%, 78.0% and 76.4% of our revenue derived from the sale of cigarette packaging paper products was attributable to the sale of cigarette packaging paper for the use in the manufacture of cigarette package of nine of the “Dual 15 cigarette brands (雙十五煙草品牌)” recognised by the STMA. For a detailed breakdown of our sales attributable to the “Dual 15 cigarette brands”, please refer to the paragraph headed “Our products and services — Breakdown of our product sales by cigarette brands” below in this section. Our Directors consider that our ability in delivering products which fulfil the stringent quality and technical requirements of various cigarette package manufacturers and well-known cigarette brands, especially those being recognised as the “Dual 15 cigarette brands”, is a recognition of our product quality, technical know-how, industry knowledge and experience which are transferrable by us to serving new potential customers.

According to the Industry Report, Yunnan, Hunan, Henan, Guangdong and Hubei are the top five production bases of cigarettes in the PRC, accounting for approximately 40% of the national production volume in aggregate. During the Track Record Period, a majority of our revenue was

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derived from customers situated in Hubei Province and Henan Province which in aggregate contributed approximately 73.5%, 88.1% and 77.6% of our total revenue for FY2019, FY2020 and FY2021, respectively.

While our major customers are mainly located in Hubei Province and Henan Province, we also strive to expand our reach to customers located in different provinces in the PRC. For example, our Group has successfully developed business relationship with various customers in other provinces, including (i) a cigarette package manufacturer, being a subsidiary of a state-owned enterprise in the PRC, with its headquarters in Shanghai Municipality in FY2019; (ii) a cigarette package manufacturer (being listed on the Shanghai Stock Exchange) with its headquarters in Anhui Province in FY2020; and (iii) a cigarette package manufacturer located in Yunnan Province, which is a subsidiary of a state-owned cigarette manufacturer, in FY2020.

According to the Industry Report, our Group was ranked as the largest cigarette packaging paper manufacturer (in terms of sales value) in Hubei Province in 2020, with a market share of approximately 14.9% in Hubei Province. Having considered our established presence in Hubei Province and the potential business opportunities available in the other geographical regions in the PRC, our Directors believe that it is the appropriate timing for our Group to further expand geographically and enlarge our market share in the PRC. Leveraging our sales network and business relationship with customers located in different provinces, our Directors believe that we are well positioned to penetrate into other geographical markets in the PRC. In this regard, it is part of our business strategies to increase our marketing efforts by strategically establishing sales centres in Shanghai Municipality, Yunnan Province and Henan Province. For further details, please refer to the paragraph headed “Increasing our marketing efforts in various provinces in the PRC” below in this section.

Our Directors believe that our planned geographical expansion and continuous effort in diversifying our customer base will likely result in an increase in demand for our cigarette packaging paper products of different product requirements and specifications. Hence, our Directors believe that we have genuine and imminent need to expand our production capacity, production efficiency and product portfolio.

(IV) Growing emphasis on the anti-counterfeiting and eco-friendliness features of cigarette packaging paper

According to the Industry Report, the PRC Government authorities have placed greater emphasis on cigarette branding, quality, and variety. In 2014, the State Tobacco Monopoly Administration for the PRC Tobacco Industry Standard issued the “*Requirements for Design of Cigarette Package (卷煙包裝設計要求) YC/T 273-2014*” which encouraged cigarette manufacturers to use environmentally friendly cigarette packaging materials. Likewise, cigarette manufacturers have striven to ensure the consistency and standardisation of their cigarette packages as these are crucial to their brand recognition and product appeal. The more stringent requirements for cigarette packages have resulted in an increase in demand for quality cigarette packaging materials which in turn encouraged cigarette packaging paper manufacturers to develop more products with advanced anti-counterfeiting and eco-friendliness features. Cigarette packaging paper manufacturers are therefore committed to improve their know-how and optimise their manufacturing process to develop cigarette packaging paper which aligns with such market trend.

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According to the Industry Report, it is increasingly common for cigarette manufacturers to use platinum positioning paper as cigarette packaging materials owing to its high precision anti-counterfeiting and eco-friendliness features. Platinum positioning paper is a type of cigarette packaging paper mainly used in the packaging of certain tier 1 cigarettes which are generally used for gifting. As compared to the mainstream cigarette packaging material which are being widely used in the market such as transfer paper and laminated paper, the usage and demand of platinum positioning paper is significantly lower. Platinum positioning paper was first launched to the market in 2012 but has yet to become a mainstream packaging material for cigarette packaging in the PRC mainly because (i) the platinum films used in the production of platinum positioning paper were only supplied by a limited number of suppliers as it required unique design and production technology; (ii) the establishment of production lines of platinum positioning paper for cigarette packaging use is capital intensive as it requires specific production equipment and involves high research and development cost; and (iii) the production of platinum positioning paper has higher requirements on precision which require advanced machinery and experienced workers. Owing to the relatively high market entry barriers, there are only a few major players in the production of platinum positioning paper in the PRC.

According to the Industry Report, notwithstanding platinum positioning paper has not become a mainstream cigarette packaging material to date, demand for platinum positioning paper has been on the rise as cigarette brands have unremittingly striven to search for higher quality and better designed cigarette packaging paper in order to enhance their brand and product appeal. Platinum positioning paper is also gaining favour among cigarette package manufacturers owing to its compatibility with different printing methods and printing machinery which enhances their flexibility in fulfilling different product features and designs.

As confirmed by our Directors and Ipsos, the production process of platinum positioning paper is largely similar to that of our existing products. However, our existing production machinery lacks the capability to handle all the production steps of platinum positioning paper. In light of (i) the growing market demand for platinum positioning paper; and (ii) the increase in number of suppliers which possessed the production technology to manufacture platinum films used in the production of platinum positioning paper according to the Industry Report, which would facilitate us in securing the supply of materials used for the production of platinum positioning paper. In particular, our Directors are aware that a number of our suppliers with whom we have established years of business relationship have also developed the capability in supplying the platinum films used in the production of platinum positioning paper; our Directors consider that it is the appropriate timing for our Group to develop the capability of manufacturing platinum positioning paper by acquiring machinery that can be interchangeably used for the production of different cigarette packaging paper with advanced features, which would in turn allow us to expand our production capabilities as well as to capture the market demand for platinum positioning paper.

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In 2021, we entered into non-binding letters of intent with Changge Dayang and a customer in Henan Province (the “**Henan Customer**”), pursuant to which we would develop and supply certain types of cigarette packaging paper to Changge Dayang and the Henan Customer. The table below sets forth the salient terms of the letters of intent:

Estimated date of sales	:	In or before 2023, depending on the progress of developing the products
Products and estimated annual sales volume to Changge Dayang	:	(i) 500 tonnes of holographic laser cigarette packaging paper with anti-counterfeiting and positioning features per year (ii) 500 tonnes of special cigarette packaging paper with anti-counterfeiting features per year (iii) 750 tonnes of imitation aluminum cigarette packaging paper with eco-friendliness features per year
Products and estimated annual sales volume to the Henan Customer	:	500 tonnes of imitation aluminum cigarette packaging paper with eco-friendliness features per year
Product development and sales arrangement	:	Our Group shall develop the cigarette packaging paper in accordance with the specifications prescribed by Changge Dayang and the Henan Customer and submit prototypes for approval. Upon confirming the prototypes, our Group shall negotiate and enter into a framework sales agreement with Changge Dayang and the Henan Customer. Changge Dayang and the Henan Customer shall place purchase orders according to the agreed unit price as stated in the framework sales agreement.

(V) Improving our production capacity and efficiency

We are committed to improving our production efficiency and product quality. We currently operate seven production lines. For FY2019, FY2020 and FY2021, the utilisation rate of our production facility was approximately 83.3%, 97.4% and 95.4%, respectively. For further details, please refer to the paragraph headed “Production facility and capacity — Utilisation rate” below in this section. The overall utilisation rate of our production facility has reached a relatively high level during the Track Record Period. We believe that in order to keep up with the expected growth in our business, especially those periods with higher sales, we have a genuine and imminent need to increase our production capacity.

During the Track Record Period, we had occasionally arranged our workers to work overtime in order to fulfil the volume of purchase orders received by us. As a result of such overtime work arrangement, during the Track Record Period, the utilisation rates of our production facility had occasionally exceeded 100%, especially for the period before Chinese New Year. Further, while

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our workers were willing to perform overtime works on an as-needed basis, there is nonetheless a limitation on the operating hours of our machinery given that (i) excessive usage of machinery may result in more frequent machine malfunctioning or breakdown; and (ii) we have to spare adequate time for performing routine cleaning and maintenance of our machinery to maintain its operating conditions at an optimal level. In view of the business growth achieved by us during the Track Record Period (excluding the one-off impact associated with the outbreak of COVID-19 in early 2020) and the forecasted increase in our sales, our Directors consider that it may not be feasible for our Group to solely rely on overtime work arrangement to fulfil the expected increase in demand for our cigarette packaging paper products in the long run. Given that the utilisation rate of our production facility remained at a relatively high level throughout the Track Record Period and we had to arrange for overtime work from time to time to fulfil our production needs, our Directors consider that our existing production capacity may not be able to support our further business expansion as it may overload our production facility as well as existing staff. Accordingly, it is essential for our Group to expand our production capacity in order to fulfil the continuous increase in demand for our products while maintaining the workload of our staff at an appropriate level at the same time.

Taking into account (i) the expected increase in market demand for cigarette packaging paper; (ii) the limitation in our production capacity; and (iii) the relatively high utilisation rate of our production facility, our Directors consider that it is justified for our Group to further expand our production capacity by replacing an existing production line which dated back to 2014 with a new one and setting up three additional new production lines with more advanced production machinery. The table below sets forth the remaining useful life of our existing production lines:

Production line(s)	Remaining useful life <i>years</i>
#01	2
#02 to #04	6
#05 to #07	7

As the age of our machinery increases, they generally depreciate in value, operational efficiency and cost-effectiveness. As at the Latest Practicable Date, we owned seven production lines, among which one production line is expected to be fully depreciated in two years. By replacing the aged machinery, our Group will benefit from the higher operational efficiency, shorter down time and lower maintenance cost of new machinery. It is crucial for our Group to constantly review the conditions of our machinery and determine if any machinery replacement or upgrade is required for maintaining our competitiveness.

Our new production lines will possess more advanced functions which enable us to further strengthen our capability in developing cigarette packaging paper that match with the evolving requirements and specifications of our customers.

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(VI) Increase in our production capacity to accommodate the increase in demand for our products

In FY2018, our Group underwent expansion in terms of our production scale following the addition of three new production lines and replacement of two of our then existing production lines. The aforesaid expansion was mainly implemented during the second half of FY2018 and thereafter, our Group spent months on the installation, adjustment and testing of the newly acquired machinery and arranged trainings for our staff on the safe operation of the newly acquired machinery. Therefore, the increase in production capacity arising from the acquisition of machinery in FY2018 was only fully reflected in FY2019, resulting in the substantial increase in maximum production capacity of our production facility from approximately 19,019 tonnes for FY2018 to approximately 28,028 tonnes for FY2019, representing an increase of approximately 47.4%.

The increase in our maximum production capacity in FY2019 enabled our Group to cater to the increase in demand from some of our existing major customers. For instance, our revenue derived from Changge Dayang increased from approximately RMB4.6 million for FY2018 to approximately RMB26.2 million for FY2019 as our sales volume to Changge Dayang increased from approximately 315 tonnes for FY2018 to approximately 1,293 tonnes for FY2019, whereas our revenue derived from Customer Group C increased from approximately RMB19.2 million for FY2018 to approximately RMB30.4 million for FY2019 as our sales volume to Customer Group C increased from approximately 1,309 tonnes for FY2018 to approximately 2,107 tonnes for FY2019.

Besides, the increase in our maximum production capacity in FY2019 also allowed us to cater to potential demand for our products from new customers which in turn enlarged our customer base. The number of customers which generated sales to our Group increased from 22 for FY2018 to 37 for FY2019. These additional customers in FY2019 contributed revenue of approximately RMB56.7 million, representing approximately 18.1% of our total revenue for FY2019.

As a result of the aforesaid, our Group achieved substantial business growth from FY2018 to FY2019 which can be demonstrated by the substantial increase in our revenue from approximately RMB233.9 million for FY2018 to approximately RMB312.8 million for FY2019, representing an increase of approximately 33.7%. Leveraging our ability in securing additional purchase orders to utilise the increase in production capacity resulting from our expansion in production scale in FY2018, the utilisation rate of our production facility increased from approximately 77.9% for FY2018 to approximately 83.3% for FY2019.

In FY2020, our business operations were suspended for approximately two months between late-January 2020 to late-March 2020 due to the outbreak of COVID-19. Subsequent to our resumption of business operations, our production facility was operated at a high utilisation level to fulfill the purchase orders in the remaining period of the year. For FY2021, the utilisation rate of our production facility maintained at a relatively high level of approximately 95.4% which was primarily due to the increase in purchase orders placed by our major customers during the period.

Based on the above, our Directors are of the view that our existing production capacity has been substantially utilised to fulfil the demand from our existing customers and our future business growth is largely limited by the existing production capacity of our production facility.

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Accordingly, our Directors believe that the continuous expansion in our production capacity is conducive and precarious to our business growth as it helps to strengthen our capability in satisfying demand for our products from existing and potential customers.

(VII) Technical improvement of our production lines

Currently, our Group mainly relies on manual inspection on identifying defective products. Our new production lines will be equipped with automatic control system that could perform automatic identification and elimination of defective products. Also, the automatic control system would alert our production staff about the detection of defective products on a real-time basis. Likewise, we also plan to install the automatic control system on our existing production lines. It is expected that the automatic control system will enhance our production efficiency and stability as well as strengthen our quality control.

In addition, the new production lines are expected to substantially increase our overall production efficiency as they will involve less idle time for replenishment of raw materials during the production process. By using more advanced machinery, our new production lines could also reduce the wear-and-tear to our raw materials, namely white cardboard, during replenishment.

Comparison between our existing laminating machines and the advanced laminating machines

The table below sets forth a comparison between the specifications and functions of our existing laminating machines and the advanced laminating machines that we intend to purchase:

Specifications and functions	Existing laminating machines	Advanced laminating machines
Useful life (<i>years</i>)	10	10
Maximum production capacity (<i>tonnes per year</i>)	4,004	4,605
Automatic paper loader ^(Note 1)	No	Yes
Positioning function ^(Note 2)	No	Yes
Automatic control system ^(Note 3)	No	Yes

Notes:

1. The automatic paper loader will enable us to replenish white cardboard while the machine is in operation, which can reduce waste materials and idle time.
2. The positioning function will enable us to produce a wider range of cigarette packaging paper, such as platinum positioning paper.
3. The automatic control system will alert our production staff about the detection of defective products on a real-time basis.

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Features of products to be manufactured by the new production lines

We intend to acquire four sets of advanced laminating machine to facilitate the replacement of an existing production line and set up three new production lines. The advanced laminating machines will allow us to manufacture a wider range of cigarette packaging paper products and achieve higher operational efficiency than our existing models. For instance, according to the Industry Report, it is increasingly common for cigarette manufacturers to use platinum positioning paper as cigarette packaging materials owing to its high precision anti-counterfeiting and eco-friendliness features.

Besides, the use of advanced laminating machines in our new production lines would facilitate us in enhancing the features of our products. The following table sets forth a comparison of the features of cigarette packaging paper that could be manufactured by each of our existing and new production lines:

	Existing production lines	New production lines
Anti-counterfeiting features	Basic anti-counterfeiting features such as holographic and laser effects.	Enhanced anti-counterfeiting features such as positioning pattern, watermarks and special symbols.
Eco-friendliness features	Basic eco-friendliness features such as glass-imitation characteristics. <small>(Note)</small>	Enhanced eco-friendliness features such as aluminum foil-imitation characteristics. <small>(Note)</small>
Technical features	Basic technical features such as aluminised and high gloss effects.	Advanced technical features such as double-sided lamination, hollowing, extra low weight and extra thin characteristics.

Note:

At the lamination stage, the white cardboard and film are bonded together by pressing between the rollers under pressure conditions to form a laminated sheet.

Our existing production lines are equipped with heating tubes which would heat up the white cardboard and film at the lamination stage and is capable of producing a glass-imitation or mirror-like feature. The cigarette packaging paper produced by us are eco-friendly in terms of high recyclability and decomposability.

Our new production lines will be equipped with ultraviolet-fixed point heating technology (the “**UV Heating Technology**”), which provides more cost-efficient and more environmental-friendly manufacturing solutions. UV Heating Technology enables the bond between the white cardboard and film to form more naturally and is capable of producing an aluminum foil-imitation effect. Our existing production lines are only capable of manufacturing aluminum foiled cigarette packaging paper with a thicker metallic layer and are in general more costly. In contrast, the UV Heating Technology enables us to use film with metallic layer of less than one-fifth of the thickness of the metallic film used in our existing production lines, which is therefore more cost-efficient and more bio-degradable. In addition, the UV Heating Technology enables more efficient heat transfer which contributes to reduced heat loss and lower utilities costs.

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(VIII) Breakeven and investment payback periods

Breakeven period refers to the length of time required for our new production lines to generate sufficient monthly revenue to cover their monthly operating expenses incurred for the relevant month, taking into account the non-cash items such as depreciation expenses. Based on our historical record, the breakeven period for the five production lines established by our Group in FY2018 was approximately six months after they came into operation. Our Directors estimated that the breakeven period for the production lines to be established by our Group under our business expansion plan will follow a similar pattern to that of our existing production lines, i.e. approximately six months after they come into operation.

Investment payback period refers to the length of time required for our new production lines to generate sufficient accumulated cash inflows to recover the initial investment costs. The investment payback period for the five production lines established by our Group in FY2018 was approximately 3.5 years after they came into operation. Our Directors expect that the investment payback period for the production lines to be established by our Group under our business expansion plan will be approximately three years after they come into operation.

In making the aforesaid estimation on the breakeven period and investment payback period of our new production lines, our Directors have taken into account the following assumptions: (i) the historical breakeven period and investment payback period for our existing production lines; (ii) the estimated annual maximum production capacity of approximately 4,605 tonnes of each of the new production line; (iii) each of the new production line is expected to have an estimated useful life of ten years; (iv) the new production lines will achieve a utilisation rate of approximately 92.0%, being the average utilisation rate of our existing production lines for the Track Record Period, upon completion of the installation, adjustment and testing process of the machinery; (v) the operating costs and expenses of production machinery mainly including maintenance costs, utilities and depreciation expenses; (vi) the cost structure in relation to the operation of our new production line will remain the same as our existing ones; (vii) the forecasted growth in demand for cigarette packaging paper in the PRC from 2022 to 2025 according to the Industry Report; (viii) the newly acquired machinery will enhance our production capability and allow us to produce a wider range of cigarette packaging paper products with advanced features; and (ix) the forecasted demand for cigarette packaging paper with new product features with reference to, among others, the letter of intent provided by our customer, details of which are set forth in the table under the paragraph headed “(IV) Growing emphasis on the anti-counterfeiting and eco-friendliness features of cigarette packaging paper” above.

(IX) Enhancing our production facility

Our Group owns a parcel of land in Hong’an County, Huanggang, Hubei Province with an aggregate site area of approximately 35,243 sq.m. Our production facility consists of five factory buildings with an aggregate gross floor area of approximately 12,000 sq.m. The five factory buildings are mainly designated for production workshops and warehouse use.

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As mentioned above, we currently plan to set up additional production lines to increase our production capacity and efficiency. As at the Latest Practicable Date, our production facility had already been substantially occupied. Our office, production lines, warehouses and area designated for conducting research and development activities had occupied over 90% of our existing production facility, with only less than 100 sq.m. of vacant space available. Cigarette packaging paper is generally bulky and require a controlled environment with specified humidity and temperature levels during production. Also, we would have to secure enough space to maintain the required level of air ventilation such that the conditions of our paper products and materials could be preserved in our desired conditions. Further, we believe that it is important to provide sufficient operating space for our employees to ensure a safe and congenial work environment.

Based on the number and size of the machinery to be acquired by us under our business expansion plan, our Directors estimated that it would require a total gross floor area of at least 6,000 sq.m. to set up our additional production lines. Given our production facility had already been substantially occupied, it is infeasible for us to allocate adequate space for setting up the additional production lines. In view of the aforesaid, our Directors believe that we have the operational need to enhance our production facility by constructing a two-storey factory building with a gross floor area of approximately 8,200 sq.m. at the vacant portion of land owned by us in Hong'an County, Huanggang (the "**New Factory Building**"). We intend to house the machinery to be acquired by us in the New Factory Building which will occupy approximately 73.2% of its total gross floor area. In addition, under the assumptions that each of the three new production lines will achieve (i) a utilisation rate of approximately 92.0% with reference to the average utilisation rate of our existing production lines for the three years ended 31 December 2021; and (ii) an annual estimated maximum production capacity of approximately 4,605 tonnes for each new production line, it is expected that the three new production lines will contribute to an increase in our annual actual production volume by approximately 12,710 tonnes in aggregate. The expected increase in our actual production volume will likely result in an increase in our need for storage space in relation to our raw materials, finished goods and packaging materials to support our production activities. Accordingly, our Directors consider that it is essential for us to allocate space in the New Factory Building for storage purpose.

In order to create an optimal working environment for our employees and to maintain the conditions of our production workshops, the New Factory Building will be equipped with advanced humidity and temperature control systems as well as a dust-free environment. Based on our management's best estimation and past experience, it will take approximately 12 to 18 months to complete the construction of the New Factory Building.

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Enhancing our research and development capabilities

(I) Acquiring more advanced research and development equipment

We constantly strive to differentiate ourselves from our competitors through providing customised products that match with the evolving requirements and specifications of our customers. Our research and development department comprised 18 personnel as at the Latest Practicable Date. Through our research and development, we had continuously enhanced the anti-counterfeit features, appearances and eco-friendliness of our products, improved our production efficiency and expanded our product offerings in terms of texture, durability and colour mixture. For FY2019, FY2020 and FY2021, the expenses incurred by us on research and development amounted to approximately RMB10.7 million, RMB10.4 million and RMB13.1 million, respectively.

According to the Industry Report, the forecasted increase in sales value of cigarette packaging paper manufacturing industry in the PRC is primarily attributable to consumer preference and industrial focus towards mid-to-high-end cigarettes. Further, driven by the PRC Government's policy on the promotion of mid-to-high-end cigarettes, cigarette packaging paper manufacturers have increased their investment on the research and development for more products with advanced anti-counterfeiting and eco-friendliness features which are critical in boosting cigarette brand recognition and product appeal. Based on the Industry Report, anti-counterfeit technology has been continually evolving and developing to combat illicit cigarettes in the PRC. The production of cigarette packaging paper with anti-counterfeiting features is a relatively sophisticated production process which requires high technical know-how. Some of those new cigarette packaging paper manufacturers may not be capable of producing cigarette packaging paper with the latest anti-counterfeiting features due to limited technical capability.

Taking into consideration the expected increase in demand and government policies on the promotion of mid-to-high-end cigarettes as well as the increasing awareness of anti-counterfeiting and eco-friendliness in the cigarette industry, our Directors consider that it is imperative for our Group to further enhance our research and development capabilities, especially on anti-counterfeiting features, in order to strengthen our capability in developing products which fulfil the evolving requirements and specifications of our customers and to maintain our market competitiveness. One of our strategies in enhancing our research and development capabilities is to acquire more advanced research and development equipment to assist us in the design, development and production of new products.

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The table below sets forth the primary function(s) of (i) our existing principal research and development equipment and testing equipment; and (ii) the advanced research and development equipment and testing equipment to be acquired by us:

Type of equipment	Principal functions
(I) Existing equipment	
Ultraviolet curing machine	Curing of materials at high speed
Quantitative sampler	Extraction of a fixed amount of material for testing
Automatic headspace sampler	Conduct residual solvent testing
Surface absorption tester	Conduct surface absorption testing
Gas chromatography instrument	Measurement of chemical compositions
Spectrometer	Measurement of colour shading
Heat seal tester	Measurement of temperature resistance
Thickness tester	Measurement of thickness of our products
(II) Advanced equipment	
Printing roller engraving machine	Precision engraving of pattern for paper and film application
Positioning crosscutting machine (Double helix blade)	Precision cutting of paper and reduce material waste
Programmable logic controller high speed winding machine	Automatic winding of paper with enhanced precision
Gas chromatography-mass spectrometry instrument	Measurement of chemical compositions with enhanced accuracy
Liquid chromatography instrument	Measurement of chemical compositions of less volatile compounds
Stiffness tester	Measurement of stiffness
Rapid moisture analyser	Measurement of moisture content

According to the Industry Report, cigarette brands generally search for higher quality and better designed cigarette packaging paper in order to enhance their brand and product appeal. Hence, cigarette packaging paper manufacturers have to invest in their research and development capability so as to improve their design and manufacturing quality to attract more business opportunities.

Our Directors consider that the need for acquiring more advanced research and development equipment is complementary to our plan to expand our production capacity and capability. Upon the establishment of the new production lines which consist more advanced production machinery as aforementioned, our Group will be able to manufacture a wider range of cigarette packaging paper products with more diversified and advanced features. In light of the planned expansion in our product offerings, our Directors consider that there are operational needs for us to strengthen our research and development capabilities by acquiring more advanced research and development equipment and testing equipment which possess higher degree of precision and proficiency.

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Based on the aforesaid, we intend to acquire the advanced research and development equipment and testing equipment as set forth in the table above to strengthen our capability in (i) developing a wider range of products with enhanced product features; and (ii) conducting a wider range of testing on our products with higher degree of precision to ensure our products quality. For instance, the chemical components of cigarette packaging paper products are subject to various national and industrial standards. To ensure the chemical components of our cigarette packaging paper products fall within the permissible limit under applicable national and industrial standards, we intend to acquire gas chromatography-mass spectrometry instrument and liquid chromatography instrument, which are capable of measuring chemical compositions with enhanced accuracy. Further, according to the Industry Report, it is increasingly common for cigarette manufacturers to use platinum positioning paper as cigarette packaging materials owing to its high precision anti-counterfeiting and eco-friendliness features and increased compatibility with different printing methods. Platinum positioning paper requires a high level of precision and automation. In light of the growing market demand for platinum positioning paper, our Directors consider that it is imperative for our Group to strengthen our research and development capability in developing platinum positioning paper by acquiring positioning crosscutting machine and programmable logic controller high speed winding machine, which are crucial in the development of platinum positioning paper tailored to our customers' needs.

(II) Expanding our research and development department

As at the Latest Practicable Date, our research and development activities were carried out at a designated area in our production facility with no more than 1,000 sq.m.. We owned more than ten sets of research and development equipment and testing equipment as at the Latest Practicable Date, which were all housed at the designated area in our existing production facility. The designated area for research and development activities has been fully occupied with our existing equipment as well as research and development staff.

As aforementioned, it is part of our business expansion plan to acquire additional research and development equipment to enhance our research and development capabilities. We currently intend to apply a portion of the net [REDACTED] from the [REDACTED] to acquire a total of 10 additional sets of advanced research and development equipment and testing equipment. For further details, please refer to the paragraph headed "Future plans and use of [REDACTED] — Use of [REDACTED]" in this document. Along with the acquisition of additional advanced research and development equipment, our Group intends to recruit four additional research and development staff members. Based on the number and size of the additional equipment to be acquired by us, our Directors estimated that we will require an additional floor area of approximately 1,700 sq.m..

In light of the space required for housing our additional research and development equipment and our additional research and development staff, our Directors currently plan to construct a research and development centre with a gross floor area of approximately 3,200 sq.m. (the "**R&D Centre**") at the vacant portion of land owned by us and relocate our research and development department to the R&D Centre. It is estimated that approximately 84.4% of the gross floor area of the R&D Centre will be occupied with our existing as well as additional research and development equipment and staff, with the remaining area to be reserved for ancillary use. Based on our management's best estimation and past experience, it will take approximately 12 to 18 months to complete the construction of the R&D Centre.

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(III) Strengthening our quality control systems

Our Group places significant emphasis on product quality and safety by implementing stringent and comprehensive quality control measures covering all stages of our operations. We are committed to achieving a low product defect rate and ensuring our products meet the requirements and specifications of our customers. As at the Latest Practicable Date, our quality control department comprises 11 staff members who are primarily responsible for conducting various quality control measures throughout the production process including sample-testing on our goods based on their size, appearance, colour shading, temperature resistance and chemical compositions with the use of our testing equipment.

The production of cigarette packaging paper is subject to various national and industrial standards including the Tobacco Industry Standard for Printed Cigarette Carton and Packet Packaging Papers of the PRC (《中華人民共和國煙草行業標準卷煙條與盒包裝紙印刷品》) (YC/T 330-2014 Standard), the Requirements for Design of Cigarette Package (《卷煙包裝設計要求》) (YC/T 273-2014 Standard) and the Tolerance Values of Volatile Organic Compounds in Cigarette Carton and Packet Packaging Papers (《卷煙條與盒包裝紙中揮發性有機化合物的限量》) (YC 263-2008 Standard). These national and industrial standards impose various requirements on the design, safety and physiochemical and hygienic properties of cigarette packaging paper.

It is our standard operating procedure to conduct various testing on our new products to ensure their compliance with applicable laws, regulations, national and industrial standards and customers' requirements and specifications before launching them in the market. In light of the increasingly stringent quality requirements of cigarette packaging paper, our Directors consider that it is vital for our Group to acquire additional testing equipment to assist us in conducting a wider range of testing on our products based on different aspects in our research and development process. Based on the aforesaid, our Group currently intends to acquire testing equipment which assist us in (i) testing the chemical components of our products to ensure their compliance with applicable national and industrial standards; and (ii) testing the moisture content of our products to prevent product quality issues such as deformation and warpage.

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(IV) Research and development projects to be undertaken

Following the acquisition of the additional research and development equipment and testing equipment and the construction of the R&D Centre, we intend to implement a range of research and development projects to strengthen our product features, enhance our product offerings and increase our production efficiency. Such research and development projects will be financed with our own internal resources. The table below sets forth details of the research and development projects we intend to undertake:

Projects	Expected timeframe Year	Estimated cost RMB'000
Research on recycling of plastic transparent layer of transfer film	2	1,500
Research on application of transfer paper as an eco-friendly substitute for aluminum foil	2	1,000
Research on the anti-counterfeiting feature of cigarette boxes for one of the “Dual 15 cigarette brands”	2	1,000
Research on the wettability of lightweight thin paper	2	1,600
Research and development of cigarette packaging paper with positioning features	2	1,500

Our Directors consider that it is essential for us to acquire advanced research and development equipment and testing equipment to conduct the aforementioned research and development projects. For instance, the positioning crosscutting machine and programmable logic controller high speed winding machine are vital in developing cigarette packaging paper with positioning features and anti-counterfeiting features as it requires a high level of precision and automation. Testing equipment such as the gas chromatography-mass spectrometry instrument and liquid chromatography instrument are essential in testing the chemical compositions of our products to enhance their recyclability and eco-friendliness, while rapid moisture analyser and stiffness tester are crucial in analysing the physical properties of our cigarette packaging paper products, such as wettability.

Enhancing our enterprise resource planning (“ERP”) system and infrastructure systems to improve our operational efficiency

We believe that an advanced ERP system is essential to support our business growth and internal controls. We plan to establish a centralised ERP system to support and manage our business expansion and improve our operational efficiency. The centralised ERP system will be able to manage various aspects of our business operations which include (i) supply chain management; (ii) inventory management; (iii) operation flow management; (iv) production management; and (v) quality control management. The centralised ERP system will be equipped with an online portal which allows us to monitor our procurement, production, sales and inventory data on a real-time basis, which in turn facilitates our production planning, procurement decision-making, inventory analysis, and sale and logistics analysis.

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We will also authorise our approved customers and suppliers access to the online portal. We will share with our approved suppliers the specifications and requirements for raw materials provided by our customers on the online portal so as to streamline our procurement process and facilitate our management of the quality of raw materials procured by us. Likewise, we will also authorise our approved customers access to the online portal so that they can monitor the production and delivery status of their purchase orders on a real-time basis.

In addition, we also plan to upgrade our infrastructure systems, including air-conditioning and mechanical ventilation system, electrical system, lightning protection system, programmable logic controller system and fire alarm system.

Increasing our marketing efforts in various provinces in the PRC

Our Group has made consistent effort in geographic expansion and diversifying our customer base. During the Track Record Period, our sales representatives have engaged in business development and marketing activities in various provinces in the PRC. They are responsible for (i) enhancing our promotion and sales efforts; (ii) actively approaching and liaising with our existing and potential customers; and (iii) collecting feedbacks and handling any queries on our products from customers in those provinces.

In order to strengthen our business relationship with existing customers and broaden our customer base, we intend to increase our marketing efforts by strategically establishing sales centres in certain target regions for our business expansion, namely Shanghai Municipality, Yunnan Province and Henan Province (collectively, the "**Target Regions**"). We also plan to recruit additional marketing staff who will be stationed at our sales centres in the respective Target Regions.

Reasons for establishing sales centres in the Target Regions

In the course of selecting the regions for establishing our sales centres, our Directors have considered, among other factors, the geographical location of our existing customers, market size and growth of the cigarette packaging paper manufacturing industry in different geographical regions, number and scale of potential customers available and transportation networks in the regions. Our marketing department has conducted research on the principal place of business of our existing and potential customers in the Target Regions. Based on the research results, we have strategically decided to establish sales centres in those locations which are in proximity to the principal place of business of our existing as well as potential customers in the Target Regions so as to increase our accessibility to them. Our Directors consider that the establishment of sales centres is conducive to our geographical expansion as they will considerably strengthen our market presence in the Target Regions. Set forth below is a detailed analysis of the reasons for establishing sales centres in the respective Target Regions:

(1) Shanghai Municipality

According to the Industry Report, the cigarette packaging paper manufacturing industry in Shanghai Municipality is relatively concentrated, with around 10 cigarette packaging paper manufacturers in the industry. In FY2019, our Group established business relationship with a cigarette package manufacturer, being a state-owned enterprise, with its headquarters in Shanghai

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Municipality (the “**Shanghai New Customer**”). The Shanghai New Customer is owned as to 60% by a cigarette manufacturer based in Shanghai Municipality (the “**Shanghai New Customer Holdco**”) and 40% by a PRC investment company. Both of the holding companies of the Shanghai New Customer are wholly owned by a state-owned enterprise, which controls cigarette manufacturing and sales in the PRC and is ranked as the largest cigarette manufacturer in the world. The Shanghai New Customer Holdco is a cigarette manufacturer which has launched over 10 cigarette brands in the PRC, including at least two of the “Dual 15 cigarette brands (雙十五煙草品牌)” recognised by the STMA. The Shanghai New Customer is principally engaged in cigarette package manufacturing. The Shanghai New Customer was ranked as one of the top thirty printing and packaging manufacturers in the PRC in 2020 and is renowned for the production of cigarette packages for mid-to-high-end cigarettes. According to the Industry Report, cigarette manufacturers (e.g. the Shanghai New Customer Holdco) generally prefer to engage their fellow group members, being cigarette package manufacturers (e.g. the Shanghai New Customer), to supply cigarette packages.

We have established stable business relationship with the Shanghai New Customer since FY2019. Part of the cigarette packaging paper products supplied by us to the Shanghai New Customer was used as cigarette packaging materials for one of the “Dual 15 cigarette brands”. Our revenue generated from the Shanghai New Customer increased from approximately RMB5.7 million for FY2019 to approximately RMB8.4 million for FY2020, and further increased to approximately RMB17.5 million for FY2021. Our Directors consider that the stable increase in our revenue generated from the Shanghai New Customer is a recognition of our ability in supplying cigarette packaging paper products which fulfill the quality standards of the Shanghai New Customer as well as its customers.

Taking into consideration (i) the scale and market standing of the Shanghai New Customer in the Shanghai cigarette package manufacturing industry; (ii) the constant demand for cigarette packaging paper from the Shanghai New Customer given it is a preferred cigarette packaging manufacturer of its holding company (i.e. a cigarette manufacturer); (iii) our growing business relationship with the Shanghai New Customer as demonstrated by the continuous increase in revenue derived from it; and (iv) the prospect, potential business opportunities and positive effect on our Group’s reputation resulting from strengthening our business relationship with the Shanghai New Customer, our Directors consider it is essential for us to ensure sufficient resources to cater to any requests or enquiries from the Shanghai New Customer on a timely basis. By stationing marketing staff and establishing sales centre in Shanghai Municipality, our Directors believe that we will be able to attend to the Shanghai New Customer more swiftly and efficiently and thereby further strengthening our business relationship with them.

Further, our Group intends to use our sales centre to be established in Shanghai Municipality as a stepping stone to further strengthen our presence and increase our market share in East China. Our Group recorded a significant increase in the amount of revenue contributed by customers from East China, which includes Shanghai Municipality, from approximately RMB11.3 million for FY2019 to approximately RMB33.3 million for FY2021. Our Group strives to strengthen our presence in East China and establish business relationship with more cigarette package manufacturers located in Shanghai Municipality. According to the Industry Report, there are around five cigarette package manufacturers in Shanghai Municipality. As at the Latest Practicable Date, our Group had established business relationship with two of these five cigarette package

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manufacturers in Shanghai Municipality. Our Directors intend to explore for potential business opportunities from those cigarette package manufacturers who had no prior business engagements or connections with us. Our marketing department has conducted research on the principal place of business of these cigarette package manufacturers and tentatively decided that our sales centre shall be established in proximity to their principal place of business so as to increase our accessibility to them and strengthen our market presence in Shanghai Municipality. Under our tentative plan, the sales centre in Shanghai Municipality will be located in Jiading District. Upon the establishment of our sales centre in Shanghai Municipality, our marketing staff stationed in the region will be able to approach those cigarette package manufacturers with whom we had no prior business engagements and promote our corporate profile and product portfolio to them in a more organised and effective manner.

(II) Yunnan Province

According to the Industry Report, Yunnan Province is one of the largest production bases of cigarettes in the PRC. The cigarette packaging paper manufacturing industry in Yunnan Province is relatively concentrated with over 20 cigarette packaging paper manufacturers in the industry. In FY2020, our Group commenced business relationship with a new customer located in Yunnan Province (the "**Yunnan New Customer**"), which is a subsidiary of a state-owned cigarette manufacturer. Our Group had submitted tender to the Yunnan New Customer in November 2020 and became its approved supplier of cigarette packaging paper products. As at the Latest Practicable Date, we had submitted a prototype to the Yunnan New Customer for its approval. The Yunnan New Customer is principally engaged in printing and packaging manufacturing which includes manufacturing of cigarette packages for mid-to-high-end cigarettes. The Yunnan New Customer is wholly owned by a cigarette manufacturer based in Yunnan (the "**Yunnan New Customer Holdco**"). The Yunnan New Customer Holdco is a cigarette manufacturer which focuses on manufacturing four cigarette brands in the PRC, including three of the "Dual 15 cigarette brands (雙十五煙草品牌)" recognised by the STMA. The Yunnan New Customer Holdco is ultimately owned by a state-owned enterprise which controls cigarette manufacturing and sales in the PRC and is ranked as the largest cigarette manufacturer in the world. According to the Industry Report, cigarette manufacturers (e.g. the Yunnan New Customer Holdco) generally prefer to engage their fellow group members, being cigarette package manufacturers (e.g. the Yunnan New Customer), to supply cigarette packages.

Our Directors consider that our success in obtaining tender from the Yunnan New Customer is conducive to enhancing our market presence in and expansion to Yunnan Province. Given we had no previous business engagements with the Yunnan New Customer, our Directors consider that it is vital for us to work closely with it in order to familiarise ourselves with its product quality requirements and specifications. By establishing sales centre and stationing marketing staff in Yunnan Province, we can conduct more frequent site visits to the production facility of the Yunnan New Customer so as to better understand its production needs and address its product requests or enquiries more expediently.

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According to the Industry Report, there are around 20 cigarette package manufacturers in Yunnan Province. As at the Latest Practicable Date, our Group had established business relationship with three of these cigarette package manufacturers in Yunnan Province. In view of the large potential customer base in Yunnan Province, our Directors consider that we could increase our market presence and further expand our market share by establishing a sales centre in Yunnan Province. Under our tentative plan, the sales centre in Yunnan Province will be located in Kunming City.

(III) Henan Province

According to the Industry Report, Henan Province is one of the largest production bases of cigarettes in the PRC. The cigarette packaging paper manufacturing industry in Henan Province is relatively fragmented, with over 30 cigarette packaging paper manufacturers in the industry. There are at least 15 cigarette package manufacturers in Henan Province. As at the Latest Practicable Date, our Group had established business relationship with nine cigarette package manufacturers in Henan Province. In terms of geographical location of our customers, Henan Province was our second largest market in terms of revenue during the Track Record Period. Our Group recorded a significant increase in the amount of revenue contributed by customers from Henan Province from approximately RMB63.9 million for FY2019 to approximately RMB121.2 million for FY2021.

Our Directors consider that our Group was able to compete successfully in the fragmented market in Henan Province due to the following factors: (i) Henan Province is located in close geographical proximity to Hubei Province in which our Group is headquartered, thereby facilitating us in effectively conducting marketing activities and building up business relationship with customers in Henan Province. In recent years, we have continued placing our business focus on Hubei Province and Henan Province while enhancing our market presence in North-east China, East China and South China. We have been actively approaching leading players in the cigarette packaging manufacturing industry which included state-owned enterprises and listed companies. Leveraging our long-standing and stable business relationship with Customer E (being one of our top customers during the Track Record Period and a renowned cigarette package manufacturer headquartered in Henan Province), we have further penetrated into the Henan market by establishing business relationship with Changge Dayang in 2018. In 2021, our Group commenced business relationship with a new customer in Henan Province, which is a subsidiary of a state-owned cigarette manufacturer. During the Track Record Period, three of our marketing staff, including two marketing directors and one marketing manager, were assigned to travel constantly to Henan Province for the purpose of (a) promoting our corporate profile and product portfolio to our existing and potential customers; (b) liaising with our customers for potential business opportunities and new product development; and (c) collecting feedbacks from and providing after-sales services to our customers, which we believed have contributed to the close working relationships between us and our customers based in Henan Province; (ii) the extensive transportation networks of Henan Province and Hubei Province has lowered the transportation costs and facilitated the delivery efficiency of our products to customers in Henan Province; (iii) our marketing staff monitors tender notices published by cigarette package manufacturers from

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different provinces in the PRC on various tendering platforms on a regular basis. This has in turn enabled us to promptly identify available market opportunities from potential customers whenever they arise. Out of our nine cigarette package manufacturer customers located in Henan Province as at the Latest Practicable Date, our Group had established business relationship with four of them through tender selection process; (iv) we place strong emphasis on research and development to cater to the evolving demand of our customers. In 2021, we entered into non-binding letters of intent with Change Dayang and a customer in Henan Province, pursuant to which we would develop and supply certain types of cigarette packaging paper to them. Our Directors consider that our commitments to develop cigarette packaging paper tailored to our customers’ needs are fundamental to our success in solidifying our market position in Henan Province; and (v) our customers in Henan Province are cigarette package manufacturers which generally supply cigarette packaging materials to cigarette manufacturers which manufacture mid-to-high-end cigarettes. In particular, all of our customers from Henan Province have supplied cigarette packaging materials to the “Dual 15 cigarette brands”. According to the Industry Report, during the supplier selection process, cigarette package manufacturers generally place more emphasis on the research and development capability of the cigarette packaging paper manufacturers and their ability in fulfilling the quality standards and technical requirements over the geographical location of their production bases. Therefore, our Directors believe that our Group’s established track record, experience and technical know-how in fulfilling the stringent quality and technical requirements of various cigarette package manufacturers and well-known cigarette brands, especially the “Dual 15 cigarette brands (雙十五煙草品牌)”, are recognised by and readily transferrable to serving those customers in Henan Province.

In light of (i) our growing presence in Henan Province as demonstrated by the continuous increase in amount of our revenue derived therefrom; (ii) our number of customers located in Henan Province; (iii) Henan Province being our second largest market in terms of revenue during the Track Record Period; and (iv) the needs for conducting regular marketing and customer relationship management activities including site visits to our customers in Henan Province, our Directors consider that it is commercially justifiable for us to establish a sales centre and station marketing staff in Henan Province. Under our tentative plan, the sales centre in Henan Province will be located in Zhengzhou City.

Functions of the sales centres

We currently intend to set up a showroom in each of the sales centre where we will display and showcase samples of our products. We will prepare product brochure which sets forth the features, functions, size and colour of all products offered by us for customers’ selection. We will also present corporate video to our customers to demonstrate our production facility, production process and quality control measures, with the aid of projection equipment and virtual reality headsets. With the aim of maintaining regular communication with our customers and keeping ourselves abreast of the latest industry trend, our marketing staff stationed at the sales centres will invite cigarette package manufacturers and cigarette manufacturers in the Target Regions to attend customer relationship management events held at our sales centre on a regular basis.

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Further, we plan to expand our marketing department by recruiting six additional staff members. Some of the new staff will be stationed at our sales centres to conduct marketing activities including (i) promotion of our products; (ii) maintaining regular communication with our customers on product development and enhancement in our production process; (iii) providing after-sales services and technical support to our customers; (iv) collecting feedbacks from our customers on our products; and (v) maintaining regular communication and interaction with our customers so as to stay abreast of the latest trend and development of our customers’ products requirements. The marketing staff who will be stationed at our sales centres will be recruited locally and preferably with past working experience in the cigarette packaging paper manufacturing industry so as to ensure their familiarity with the local industry and proficiency in local dialect.

During the Track Record Period, our marketing staff conducted site visits to the production facility of our customers regularly for the purpose of (i) better understanding their production needs so as to facilitate us in making suitable recommendations or making necessary adjustment or modifications to our products so as to enhance their compatibility with our customers’ cigarette package production; and (ii) providing technical support and assistance to our customers regarding problems they may encounter during application of our products in their production. Given our Group had not stationed any staff in regions beyond Hubei Province during the Track Record Period, our marketing staff had to travel constantly from region to region to conduct visit to our customers. Our Directors consider that by establishing sales centres and stationing marketing staff in the Target Regions, we will be able to save time spent on travelling and attend to our customers’ enquiries more efficiently and expediently.

As at the Latest Practicable Date, our Group owned a motor vehicle for transporting our marketing staff to conduct regular visit to our customers. As we plan to further strengthen our marketing activities in various provinces in the PRC, we intend to purchase three additional motor vehicles to facilitate the travelling of our marketing staff in their respective regions.

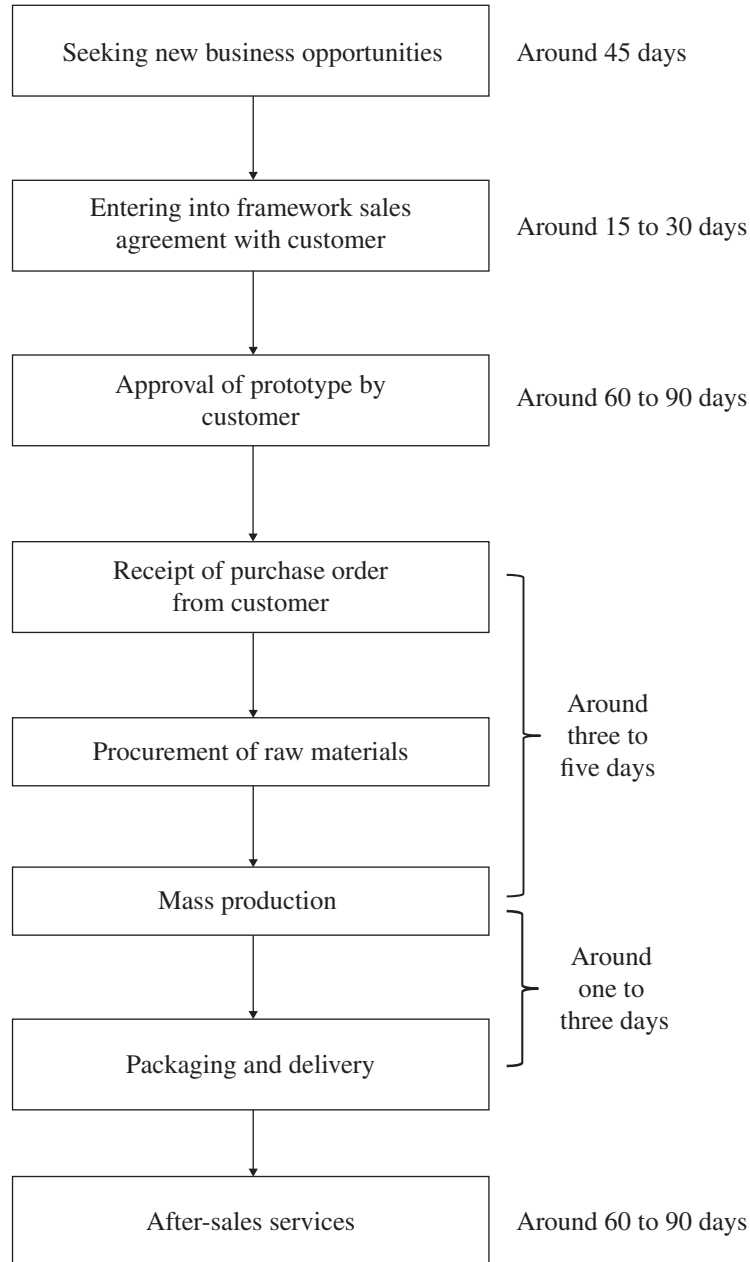
Implementation of business strategies

For further details on the implementation of the abovementioned business strategies, please refer to the section headed “Future plans and use of [REDACTED]” in this document.

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OPERATION FLOW

Set out below is a flowchart summarising the principal steps of our workflow for the manufacture of cigarette packaging paper and the typical time frame for such steps:



Note: The timeframe is calculated on an approximate basis and may vary depending on the volume of products purchased, our available production capacity and our customers' request on the delivery date.

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Seeking new business opportunities

Our Group seeks new business opportunities mainly through (i) incoming enquiries from new and existing customers; (ii) referrals from existing customers; (iii) identification of tender opportunities by regularly monitoring tender notices published by cigarette package manufacturers on various tendering platforms; and (iv) marketing and promotion activities carried out by our marketing department. For further information, please refer to the paragraph headed “Marketing” below in this section.

In general, our customers will provide us the requirements and specifications of the products, such as size, colour, materials, texture and cuttings. Our marketing department, together with our production department, will work closely with our customers to familiarise themselves with the product requirements and specifications and evaluate the scope, technical requirements, complexity and feasibility of production.

If we decide to pursue a potential engagement after our assessment, we will prepare an internal production cost plan and a bill of material detailing the raw materials to be used. We will then submit to our customer a quotation or tender, which sets out, among others, the types and specifications of the products to be sold by us, the unit price for each product, our corporate profile and track record.

Entering into framework sales agreement with customer

If our quotation or tender is accepted by our customer, our customer will typically confirm our engagement by entering into a framework sales agreement with us. For further details, please refer to the paragraph headed “Our customers — Principal terms of engagement” below in this section.

Approval of prototype by customer

After confirming the major specifications of the product with our customer, our production department will produce prototypes for the product according to the specifications and submit to our customers for approval.

Receipt of purchase order from customer

Once we receive a purchase order from our customer, our production department will assess the production requirements and delivery time and plan for our production schedule. The required quantity and the arrangement of delivery may vary from order to order. Our marketing department will then confirm the purchase order with the customer.

Procurement of raw materials

Our procurement department will procure the required raw materials from our approved suppliers based on our production needs and inventory level. For further details, please refer to the paragraph headed “Our suppliers” below in this section.

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Mass production

After ensuring our production schedule and required raw materials are in order, we will proceed to mass production. For details of our production process, please refer to the paragraph headed “Production facility and capacity — Production process” below in this section.

Throughout the entire production process, we have implemented quality control measures to ensure that our product meets the requirements and specifications of our customers. For details of our quality control procedures, please refer to the paragraph headed “Quality control” below in this section.

Packaging and delivery

Our finished products will be packaged carefully to avoid wear and tear during delivery. After inspection and packaging, the finished products are stored in our warehouse and we will engage third party logistics service providers to deliver our finished products to the destinations specified by our customers.

After-sales services

We strive to provide quality and effective after-sales services and technical support to our customers and collect feedbacks on the quality of our products for future improvement. In the event that a defect is identified, our customers may request for product return within a prescribed time under our product return policy. For details of our product return policy, please refer to the paragraph headed “Our customers — Principal terms of engagement” below in this section.

OUR PRODUCTS AND SERVICES

We manufacture cigarette packaging paper as our principal products. We supply our products primarily to cigarette package manufacturers which operate in different provinces of the PRC, mainly including Hubei Province and Henan Province. The products sold by us are used in the manufacture of cigarette packages for well-known cigarette brands in the PRC. Our products are customised in accordance with the specifications prescribed by our customers.

To a much lesser extent, we also provide cigarette packaging paper processing services to cigarette package manufacturers, of which the work flow and process are largely similar to the production of our cigarette packaging paper. In respect of our cigarette packaging paper processing services, our customers are responsible for the procurement of raw materials which they will provide us for further processing. In general, our customers provide us the requirements and specifications of the cigarette packaging paper processing services required, which primarily involve enhancing the eco-friendliness, elasticity, smoothness and abrasion resistance of the cigarette packaging paper.

During the Track Record Period, our revenue was mainly derived from the sales of cigarette packaging paper. Our products are categorised into (i) transfer paper; (ii) laminated paper; and (iii) frame paper. To a much lesser extent, we also provide cigarette packaging paper processing services to cigarette package manufacturers. The following table sets forth a breakdown of (i) our

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revenue, sales volume and average selling price by type of our cigarette packaging paper products; and (ii) revenue generated from the provision of cigarette packaging paper processing services during the Track Record Period:

	FY2019				FY2020				FY2021			
	Revenue	% of	Sales	Average	Revenue	% of	Sales	Average	Revenue	% of	Sales	Average
		total	volume	selling		total	volume	selling		total	volume	selling
	revenue	revenue	price	price	revenue	revenue	price	price	revenue	revenue	price	price
RMB'000		tonnes	RMB per tonne	RMB'000		tonnes	RMB per tonne	RMB'000		tonnes	RMB per tonne	
Sale of cigarette packaging paper												
— Transfer paper	246,017	78.6	16,162	15,200	253,250	79.6	17,326	14,600	312,741	84.5	20,357	15,400
— Laminated paper	61,414	19.6	5,517	11,100	59,616	18.7	5,553	10,700	55,889	15.1	5,137	10,900
— Frame paper	2,328	0.8	312	7,500	1,486	0.4	175	8,500	1,594	0.3	180	8,800
Sub-total	309,759	99.0	21,991		314,352	98.7	23,054		370,224	99.9	25,674	
Provision of cigarette packaging paper processing services												
	3,041	1.0			3,994	1.3			87	0.1		
Total	312,800	100.0			318,346	100.0			370,311	100.0		

Our revenue generated from the sales of transfer paper increased from approximately RMB253.3 million for FY2020 to approximately RMB312.7 million for FY2021 mainly due to the increase in sales volume of transfer paper. The sales volume of transfer paper increased from approximately 17,326 tonnes for FY2020 to approximately 20,357 tonnes for FY2021. Such increase was mainly attributable to the increase in demand for transfer paper from some of our existing customers. In particular, (i) the sales volume of transfer paper attributable to Harbin Shixiang increased from approximately 1,010 tonnes for FY2020 to 2,717 tonnes for FY2021, mainly due to the increase in sales of a transfer paper product newly developed by our Group in FY2021; (ii) the sales volume of transfer paper attributable to Customer E increased from approximately 1,677 tonnes for FY2020 to 2,970 tonnes, mainly due to the increase in sales volume of three new transfer paper products newly developed in late-2020 for the use in the manufacture of cigarette packages for a “Dual 15 cigarette brand (雙十五煙草品牌)””; and (iii) the sales volume of transfer paper attributable to Changge Dayang increased from approximately 2,248 tonnes to 2,882 tonnes mainly due to the award of tender to Changge Dayang for the supply of cigarette packages for a “Dual 15 cigarette brand (雙十五煙草品牌)”, which resulted in Changge Dayang’s increase in demand for our Group’s transfer paper products which is to be used in the production of cigarette packages for such “Dual 15 cigarette brand (雙十五煙草品牌)”.

Our revenue generated from the sales of laminated paper decreased from approximately RMB59.6 million for FY2020 to RMB55.9 million for FY2021 mainly due to the decrease in sales volume of laminated paper. The sales volume of laminated paper decreased from approximately 5,553 tonnes for FY2020 to 5,137 tonnes for FY2021. Such decrease was mainly due to the decrease in demand for laminated paper from some of our existing customers. In particular, the sales volume of laminated paper attributable to Hubei Golden Three Gorges decreased from

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approximately 534 tonnes for FY2020 to 242 tonnes for FY2021, mainly due to the loss of tender of Hubei Golden Three Gorges in the supply of cigarette packages for a cigarette brand. The loss of tender of Hubei Golden Three Gorges resulted in a decrease in demand for our laminated paper which was to be used by Hubei Golden Three Gorges in the production of cigarette packages for the cigarette brand.

Our revenue generated from the sales of frame paper decreased from approximately RMB2.3 million for FY2019 to approximately RMB1.5 million for FY2020 mainly due to the decrease in sales volume of frame paper. The sales volume of frame paper decreased from approximately 312 tonnes for FY2019 to approximately 175 tonnes for FY2020. Such decrease was mainly because of our strategy in allocating more of our production capacity for transfer paper and laminated paper, which are our major types of products, in light of the constraint in our production facility as evidenced by our utilisation rate of 97.4% in FY2020.

The average selling price of transfer paper decreased slightly from approximately RMB15,200 per tonne in FY2019 to RMB14,600 per tonne in FY2020. Such decrease was mainly attributable to the increase in sales volume of two types of transfer paper products that we sold to Changge Dayang for one of the "Dual 15 cigarette brands". In particular, (i) the sales volume of one of the aforesaid products, with an average selling price of approximately RMB13,100 per tonne, increased from approximately 255 tonnes in FY2019 to approximately 862 tonnes in FY2020; and (ii) the sales volume of the other product, with an average selling price of approximately RMB13,900 per tonne, increased from approximately 373 tonnes in FY2019 to approximately 843 tonnes in FY2020.

The average selling price of transfer paper increased slightly from approximately RMB14,600 per tonne in FY2020 to approximately RMB15,400 per tonne in FY2021. Such increase was mainly attributable to the sales of a number of new transfer paper products that we sold to Hubei Golden Three Gorges in FY2021, which contributed a sales volume of approximately 939 tonnes. The average selling price of these new products was approximately RMB20,300 per tonne in FY2021.

The average selling price of laminated paper decreased slightly from approximately RMB11,100 per tonne in FY2019 to RMB10,700 per tonne in FY2020. Such decrease was mainly attributable to the sales of two types of new laminated paper products that we sold to Hubei Xinjiarui in FY2020, which contributed a sales volume of approximately 712 tonnes. The average selling price of these two types of products was approximately RMB10,200 per tonne in FY2020.

The average selling price of frame paper increased from approximately RMB7,500 per tonne in FY2019 to approximately RMB8,500 per tonne in FY2020, and further increased to approximately RMB8,800 per tonne in FY2021. Such increase was mainly because of change of product mix with more frame paper of higher price.

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Breakdown of our product sales by the categories of cigarettes

During the Track Record Period, a majority of our revenue was derived from the sales of cigarette packaging paper products applied for mid-to-high-end cigarettes. The table below sets forth a breakdown of our revenue of our sales of cigarette packaging paper products by the categories of cigarettes during the Track Record Period:

	FY2019		FY2020		FY2021	
	<i>RMB'000</i>	%	<i>RMB'000</i>	%	<i>RMB'000</i>	%
Mid-to-high-end cigarettes ^(Note 2)						
Tier 1 cigarettes	74,746	24.1	57,100	18.2	47,659	12.9
Tier 2 cigarettes	67,846	21.9	67,958	21.6	72,657	19.6
Tier 3 cigarettes	<u>150,195</u>	<u>48.5</u>	<u>171,823</u>	<u>54.6</u>	<u>238,336</u>	<u>64.4</u>
	292,787	94.5	296,881	94.4	358,652	96.9
Low-end cigarettes ^(Note 3)						
Tier 4 cigarettes	16,972	5.5	17,471	5.6	11,572	3.1
Tier 5 cigarettes	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
	<u>16,972</u>	<u>5.5</u>	<u>17,471</u>	<u>5.6</u>	<u>11,572</u>	<u>3.1</u>
Total	<u><u>309,759</u></u>	<u><u>100.0</u></u>	<u><u>314,352</u></u>	<u><u>100.0</u></u>	<u><u>370,224</u></u>	<u><u>100.0</u></u>

Notes:

1. The classification of our products by the tiers of cigarettes that our products were applied for was compiled based on information provided by our customers and Ipsos, and the product description set out in the framework sales agreements and/or purchase orders.
2. Mid-to-high-end cigarettes represent tier 1 to tier 3 cigarettes, with retail price at or above RMB6 per box.
3. Low-end cigarettes represent tier 4 to tier 5 cigarettes, with retail price below RMB6 per box.

Our revenue generated from the sales of cigarette packaging paper products which were used for the manufacture of tier 1 cigarette packages decreased by approximately 23.6%, from approximately RMB74.7 million for FY2019 to approximately RMB57.1 million for FY2020 and further decreased by approximately 16.5% to approximately RMB47.7 million for FY2021, which was mainly attributable to the decrease in sales of cigarette packaging paper to certain major customers for the use in the manufacture of cigarette packages for several tier 1 cigarettes due to, amongst others, (i) the loss of tender and decrease in demand of our major customers in the supply of cigarette packages for several tier 1 cigarettes; and (ii) changes to the package design of a tier 1 cigarette, resulting in a decrease in demand for our cigarette packaging paper products.

Our Directors consider that the decrease in demand or loss of tender by our major customers for the supply of tier 1 cigarette packages were one-off in nature. Notwithstanding the decrease in our revenue generated from the sales of cigarette packaging paper used for the manufacture of tier 1 cigarette packages due to the reasons aforesaid, our Group was able to achieve a growth in our

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revenue and gross profit and maintain our gross profit margin during the Track Record Period. Based on the aforesaid, our Directors consider that the decrease in demand or loss of tender by our major customers for the supply of tier 1 cigarette packages did not result in any material adverse impact on our Group’s business and financial performance.

Our revenue generated from the sales of cigarette packaging paper products which were used for the manufacture of tier 2 cigarette packages remained stable at approximately RMB67.8 million and RMB68.0 million for FY2019 and FY2020, respectively, and subsequently increased to approximately RMB72.7 million for FY2021.

Our revenue generated from the sales of cigarette packaging paper products which were used for the manufacture of tier 3 cigarette packages increased by approximately 14.4%, from approximately RMB150.2 million for FY2019 to approximately RMB171.8 million for FY2020 and further increased by approximately 38.7%, to approximately RMB238.3 million for FY2021, which was mainly attributable to the increase in sales of cigarette packaging paper to certain major customers for the use in the manufacture of cigarette packages for several tier 3 cigarettes due to, amongst others, (i) the increase in tender amount awarded to a major customer for the supply of cigarette packages for certain tier 3 cigarettes; (ii) the award of tenders to a number of our major customers for the supply of cigarette packages for various tier 3 cigarettes; and (iii) the increase in sales of cigarette packaging paper used for newly developed cigarette package for a tier 3 cigarette.

Breakdown of our product sales by cigarette brands

During the Track Record Period, our products were used as cigarette packaging materials for at least nine cigarette brands which were recognised as the “Dual 15 cigarette brands (雙十五煙草品牌)” by the STMA. The “Dual 15 cigarette brands” represent the 15 cigarette brands which

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derived the highest sales from mid-to-high-end cigarettes in 2020 in the PRC. The table below sets forth a breakdown of our revenue by the cigarette brands that our products were applied for during the Track Record Period:

	FY2019		FY2020		FY2021	
	RMB'000	%	RMB'000	%	RMB'000	%
Dual 15 cigarette brands						
—Brand A <i>(Note 2)</i>	71,635	23.1	100,834	32.1	157,085	42.4
—Brand B <i>(Note 3)</i>	62,891	20.3	77,718	24.7	57,260	15.5
—Brand C <i>(Note 4)</i>	39,321	12.7	38,707	12.3	29,523	8.0
—Brand D <i>(Note 5)</i>	16,798	5.4	3,351	1.1	61	Negligible
—Brand E <i>(Note 6)</i>	152	0.1	171	0.1	97	Negligible
—Brand F <i>(Note 7)</i>	4,201	1.4	1,474	0.5	2,133	0.6
—Brand G <i>(Note 8)</i>	—	—	1,351	0.4	31,073	8.4
—Brand H <i>(Note 9)</i>	4,131	1.3	20,506	6.5	5,486	1.5
—Brand I <i>(Note 10)</i>	935	0.3	867	0.3	—	—
Sub-total	<u>200,064</u>	<u>64.6</u>	<u>244,979</u>	<u>78.0</u>	<u>282,718</u>	<u>76.4</u>
Other brands	<u>109,695</u>	<u>35.4</u>	<u>69,373</u>	<u>22.0</u>	<u>87,506</u>	<u>23.6</u>
Total	<u><u>309,759</u></u>	<u><u>100.0</u></u>	<u><u>314,352</u></u>	<u><u>100.0</u></u>	<u><u>370,224</u></u>	<u><u>100.0</u></u>

Notes:

1. The classification of our products by the cigarette brands that our products were applied for was compiled based on information provided by our customers and Ipsos and the product description set out in the framework sales agreements and/or purchase orders.
2. Brand A is a cigarette brand based in Henan Province and was first manufactured in the 1950s. Brand A was recognised as one of the top ten best-selling brands by the National Bureau of Statistics of China in 1999 and was recognised as one of China’s well-known trademarks (中國馳名商標) in 2006. According to the Industry Report, the sales value of Brand A cigarettes was approximately RMB63.5 billion, RMB69.6 billion and RMB77.4 billion for FY2019, FY2020 and FY2021, respectively, while the average selling price of Brand A cigarettes was approximately RMB12.8 per box for the three years ended 31 December 2021.
3. Brand B is a cigarette brand based in Hubei Province and was first manufactured in the 1930s. According to the Industry Report, the sales value of Brand B cigarettes was approximately RMB103.2 billion, RMB107.5 billion and RMB117.2 billion for FY2019, FY2020 and FY2021, respectively, while the average selling price of Brand B cigarettes was approximately RMB20.1 per box for the three years ended 31 December 2021.
4. Brand C is a cigarette brand based in Yunnan Province and was first manufactured in the 1950s. Brand C was included in the Hurun Most Valuable China Brands 2020 (2020胡潤品牌榜) published by Hurun Report (胡潤百富) in 2021. According to the Industry Report, the sales value of Brand C cigarettes was approximately RMB111.0 billion, RMB114.2 billion and RMB118.7 billion for FY2019, FY2020 and FY2021, respectively, while the average selling price of Brand C cigarettes was approximately RMB13.0 per box for the three years ended 31 December 2021.

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5. Brand D is a cigarette brand based in Yunnan Province and was first manufactured in the 1950s. According to the Industry Report, the sales value of Brand D cigarettes was approximately RMB75.5 billion, RMB73.7 billion and RMB77.0 billion for FY2019, FY2020 and FY2021, respectively, while the average selling price of Brand D cigarettes was approximately RMB20.9 per box for the three years ended 31 December 2021.
6. Brand E is a cigarette brand based in Guangdong Province and was first manufactured in the 1900s. Brand E was recognised as one of China famous brand products (中國名牌產品) by the General Administration of Quality Supervision, Inspection and Quarantine of the PRC in 2005 and was recognised as one of China’s well-known trademarks (中國馳名商標) in 2008. According to the Industry Report, the sales value of Brand E cigarettes was approximately RMB66.1 billion, RMB64.5 billion and RMB66.9 billion for FY2019, FY2020 and FY2021, respectively, while the average selling price of Brand E cigarettes was approximately RMB11.0 per box for the three years ended 31 December 2021.
7. Brand F is a cigarette brand based in Hunan Province and was first manufactured in the 1970s. According to the Industry Report, the sales value of Brand F cigarettes was approximately RMB56.8 billion, RMB56.5 billion and RMB56.7 billion for FY2019, FY2020 and FY2021, respectively, while the average selling price of Brand F cigarettes was approximately RMB11.6 per box for the three years ended 31 December 2021.
8. Brand G is a cigarette brand based in Jiangsu Province and was first manufactured in the 1950s. Brand G was recognised as a major cigarette brand in the PRC (全國性捲煙重點骨幹品牌) in 2008. According to the Industry Report, the sales value of Brand G cigarettes was approximately RMB91.5 billion, RMB95.3 billion and RMB102.4 billion for FY2019, FY2020 and FY2021, respectively, while the average selling price of Brand G cigarettes was approximately RMB16.2 per box for the three years ended 31 December 2021.
9. Brand H is a cigarette brand based in Yunnan Province and was first manufactured in the 1950s. Brand H was recognised as one of China’s well-known trademarks (中國馳名商標) in 1997 and was recognised as one of China’s 500 Most Valuable Brands (中國品牌500強) published by World Brand Lab in 2010. According to the Industry Report, the sales value of Brand H cigarettes was approximately RMB48.0 billion, RMB48.7 billion and RMB47.7 billion for FY2019, FY2020 and FY2021, respectively, while the average selling price of Brand H cigarettes was approximately RMB7.6 per box for the three years ended 31 December 2021.
10. Brand I is a cigarette brand based in Hunan and was first manufactured in the 1950s. Brand I was recognised as one of the best-selling brands in the PRC (全國暢銷品牌) by the STMA in 1996. According to the Industry Report, the sales value of Brand I cigarettes was approximately RMB107.7 billion, RMB109.7 billion and RMB114.1 billion for FY2019, FY2020 and FY2021, respectively, while the average selling price of Brand I cigarettes was approximately RMB22.6 per box for the three years ended 31 December 2021.

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During the Track Record Period, our revenue generated from the sales of cigarette packaging paper for the use in the manufacture of Brand A cigarette packages was mainly attributable to Hubei Golden Three Gorges, Harbin Shixiang, Customer E, Changge Dayang and 13 other customers. Our revenue generated from the sales of cigarette packaging paper for the use in the manufacture of Brand A cigarette packages increased from approximately RMB71.6 million for FY2019 to approximately RMB100.8 million for FY2020 and further to approximately RMB157.1 million for FY2021. Such increase was mainly driven by (i) the increase in sales value of Brand A cigarettes. According to the Industry Report, the sales value of Brand A cigarettes increased from approximately RMB60.9 billion for FY2018 to approximately RMB63.5 billion for FY2019 and further to approximately RMB69.6 billion for FY2020; (ii) the increase in our revenue derived from the sales of cigarette packaging paper for the use in the manufacture of Brand A cigarette packages to Customer E from approximately RMB19.8 million in FY2019 to approximately RMB32.1 million in FY2020 and further to approximately RMB55.6 million for FY2021; and (iii) the increase in our revenue derived from the sales of cigarette packaging paper for the use in the manufacture of Brand A cigarette packages to Changge Dayang from approximately RMB12.2 million in FY2019 to approximately RMB34.3 million in FY2020 and further to approximately RMB50.4 million for FY2021.

During the Track Record Period, our revenue generated from the sales of cigarette packaging paper for the use in the manufacture of Brand B cigarette packages was mainly attributable to Hubei Golden Three Gorges, Customer Group C and 11 other customers. Our revenue generated from the sales of cigarette packaging paper for the use in the manufacture of Brand B cigarettes increased from approximately RMB62.9 million for FY2019 to approximately RMB77.7 million for FY2020. Such increase was mainly driven by (i) the increase in sales value of Brand B cigarettes. According to the Industry Report, the sales value of Brand B cigarettes increased from approximately RMB100.3 billion for FY2018 to approximately RMB103.2 billion for FY2019 and further to approximately RMB107.5 billion for FY2020; (ii) the increase in our revenue derived from the sales of cigarette packaging paper for the use in the manufacture of Brand B cigarette packages to Customer Group C from approximately RMB30.4 million for FY2019 to approximately RMB42.8 million for FY2020; and (iii) the increase in our revenue derived from the sales of cigarette packaging paper for the use in the manufacture of Brand B cigarette packages to a cigarette packager manufacturer, being a subsidiary of a state-owned enterprise in the PRC with its headquarters in Shanghai Municipality, from approximately RMB5.7 million in FY2019 to approximately RMB8.4 million in FY2020.

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During the Track Record Period, our revenue generated from the sales of cigarette packaging paper for the use in the manufacture of Brand G cigarette packages was mainly attributable to Harbin Shixiang and three other customers. Our revenue generated from the sales of cigarette packaging paper for the use in the manufacture of Brand G cigarette packages increased from approximately RMB1.4 million for FY2020 to approximately RMB31.1 million for FY2021. Such increase was mainly driven by the increase in our revenue derived from Harbin Shixiang from the sales of cigarette packaging paper for the use in the manufacture of Brand G cigarette packages from nil for FY2020 to approximately RMB29.3 million for FY2021.

Movement in the volume of our cigarette packaging paper products

The table below sets forth the movement in the volume of our cigarette packaging paper products produced and used/sold during the Track Record Period:

	FY2019	FY2020	FY2021
	<i>tonnes</i>	<i>tonnes</i>	<i>tonnes</i>
Inventory of finished goods as at the beginning of the year (by volume)	1,437	2,666	2,201
Add: Actual production volume during the year	23,352	22,749	26,733
Less: Sales volume during the year	(21,991)	(23,054) ^(Note)	(25,674)
Less: Finished goods used for research and development during the year	(132)	(160)	(274)
 Inventory of finished goods to be carried forward to the next year (by volume)	 2,666	 2,201	 2,986

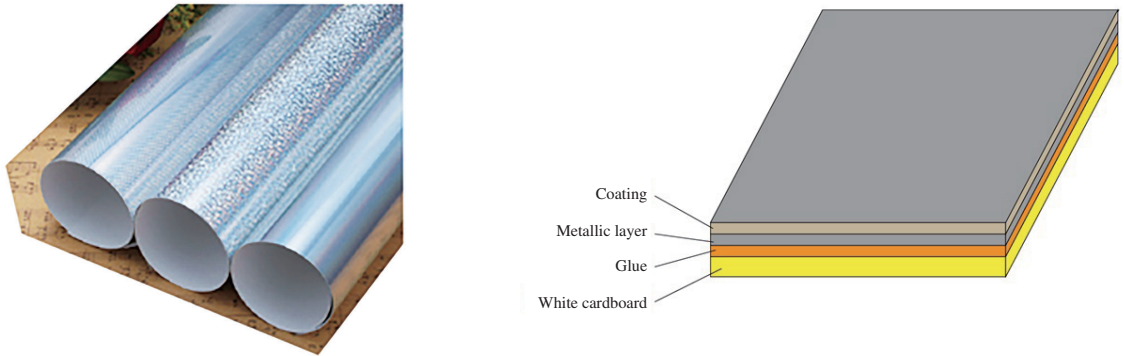
Note: As we plan for our production during FY2020, our management had taken into account the forecasted demand for our cigarette packaging paper products as well as the inventory of finished goods carried forward from FY2019, resulting in the sales volume for FY2020 exceeding our actual production volume for the corresponding year.

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Transfer paper

Transfer paper is packaging paper which is glossy and shiny and has a laser effect. By using various processing techniques including curing, a transfer film is first laminated onto a white cardboard. Upon lamination, the plastic transparent layer of the transfer film is then stripped from the laminated sheet, leaving only the metallic layer on the white cardboard. Therefore the metallic layer is transferred from the transfer film onto the white cardboard to form transfer paper.

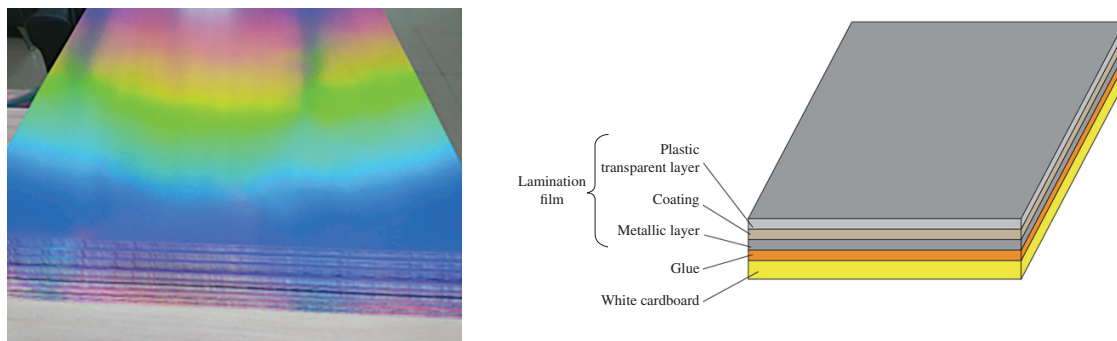
Transfer paper is more eco-friendly compared to laminated paper as the plastic transparent layer of the transfer film is removed after lamination. Transfer paper is therefore bio-degradable and recyclable.



Transfer paper

Laminated paper

Laminated paper possess similar appearance as transfer paper. It also uses similar processing techniques to laminate a lamination film onto a white cardboard. However, unlike transfer paper, the entire lamination film stays on the laminated sheet to form laminated paper without removing any layer of the lamination film. Laminated paper therefore consists of a plastic transparent layer in its final product.



Laminated paper

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Both transfer paper and laminated paper are used as external packaging paper in the manufacture of cigarette packages and boxes. According to our customers' requests, our packaging paper may be printed with the names and logos of cigarette brands in the PRC for the purpose of identification. The surface of our packaging paper is waterproof and non-absorbent and may carry anti-counterfeit features.

Frame paper

Our frame paper is used as the paper which forms part of the hard box for packing and carrying of cigarettes. The purpose of including the frame paper in the cigarette box is to prevent the cigarette box from collapsing.

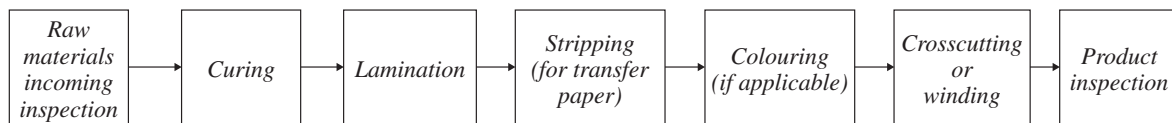


Frame paper

PRODUCTION FACILITY AND CAPACITY

Production process

The following chart illustrates the major production process of our cigarette packaging paper:



Step 1 — Raw materials incoming inspection

The raw materials used in our production process mainly include white cardboard, film, ink and glue. If any defects are detected, the raw materials will be returned to suppliers.

Step 2 — Curing

During the curing process, the white cardboard is back coated, stabilised and hardened.

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Step 3 — Lamination

At the lamination stage, the white cardboard and film are bonded together by pressing between the rollers under pressure conditions to form a laminated sheet.

Step 4 — Stripping (for transfer paper)

For transfer paper, the plastic transparent layer of the transfer film is then separated and removed from the laminated sheet. This stripping process results in leaving only the metallic layer of the transfer film attached to the white cardboard.

Step 5 — Colouring (if applicable)

Depending on the product specification, colours may be added to the laminated sheet after the lamination stage.

Step 6 — Crosscutting or winding

Depending on the requirements of the customer, the processed sheet is crosscut into flat sheets or wound into rollers.

Step 7 — Product inspection

After inspection by various departments including the production department and quality control department, the final product is packaged and stored in the warehouse for delivery.

Production facility

Our self-owned production base, which includes our production facility and office, is located in Hong'an County, Huanggang, Hubei Province, with a gross floor area of approximately 12,000 sq.m.. As at the Latest Practicable Date, we operated a total of seven production lines. Our production lines are commonly applicable to the production of transfer paper, laminated paper and frame paper. Our production workshops are equipped with basic humidity and temperature control systems.

We are committed to investing in our machinery to enhance our production efficiency and ensure our product quality. Our principal machinery includes laminating machine, crosscutting machine and winding machine. We also possess various testing equipment to conduct measurement on the colour shading, temperature resistance and chemical compositions of our products. Our machinery is well-equipped to be used for producing products with different specifications. For FY2019, FY2020 and FY2021, our capital expenditure on acquiring production machinery amounted to approximately RMB0.1 million, RMB25,000 and RMB1.2 million, respectively. We purchase our machinery principally from local machinery vendors in the PRC. Our production department liaise with the machinery vendors to ensure the relevant production machinery fulfils our production requirements. Our production department is responsible for overseeing the installation of our production lines with a view to optimising our entire production process.

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As at the Latest Practicable Date, the principal machinery that was owned and used by our Group at our production facility are set out below:

Type of machinery	Principal functions	Number of unit(s)
 <p><i>Laminating machine</i></p>	<p>Laminating machines are mainly used for (i) back coating, stabilising, hardening and gluing of white cardboard; and (ii) bonding the white cardboard and film together</p>	7
 <p><i>Crosscutting machine</i></p>	<p>Crosscutting machines are mainly used for (i) stripping the plastic transparent layer of transfer film; and (ii) crosscutting the processed sheets according to the requirements of the customer</p>	4
 <p><i>Winding machine</i></p>	<p>Winding machines are mainly used for (i) stripping the plastic transparent layer of transfer film; and (ii) winding the processed sheets into rollers</p>	4

In line with our strategy to expand our production capacity, we plan to acquire four sets of laminating machine to facilitate the replacement of an existing production line and set up three new production lines. For further information, please refer to the paragraph headed “Business strategies” above in this section and the paragraph headed “Future plans and use of [REDACTED] — Use of [REDACTED]” in this document.

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Utilisation rate

The table below sets forth the maximum production capacity, actual production volume and utilisation rate of our production facility during the Track Record Period:

	FY2019	FY2020	FY2021
Maximum production capacity (tonnes) <i>(Notes 1 and 2)</i>	28,028	23,357 ^(Note 3)	28,028
Actual production volume (tonnes)	23,352	22,749	26,733
Utilisation rate (%) <i>(Note 4)</i>	83.3	97.4	95.4

Notes:

1. Maximum production capacity is determined and calculated by multiplying the daily capacity of the machine with the applicable number of days of operation and the number of machine during the year.
2. We assume the daily operating hours for our machinery to be 14 hours, operating 260 days per year (except for FY2020), taking into account staff holidays, public holidays and seasonal factors.
3. We assume that our machinery operated for 217 days for FY2020, taken into account the suspension of our business operations for approximately two months between late-January 2020 to late-March 2020 when the PRC Government imposed a lockdown in Huanggang, Hubei Province due to the outbreak of COVID-19, staff holidays, public holidays and seasonal factors.
4. Utilisation rate is calculated by dividing actual production volume by maximum production capacity for the relevant year.

Our Directors consider that the utilisation rates of our production facility are affected by a number of factors including the volume of purchase orders, product type, technical requirements and specifications, status of repair and maintenance of our machinery and production schedule.

The maximum production capacity of our production facility increased from approximately 19,019 tonnes for FY2018 to approximately 28,028 tonnes for FY2019. The substantial increase in our maximum production capacity from FY2018 to FY2019 was mainly attributable to the expansion in our production scale following the addition of three new production lines and replacement of two of our then existing production lines in FY2018. The aforesaid expansion was mainly implemented during the second half of FY2018 and thereafter, our Group spent months on the installation, adjustment and testing of the newly acquired machinery and arranged trainings for our staff on the safe operation of the newly acquired machinery. Therefore, the increase in production capacity arising from the acquisition of machinery in FY2018 was only fully reflected in FY2019, resulting in the substantial increase in maximum production capacity of our production facility from FY2018 to FY2019.

In FY2020, our maximum production volume experienced a decrease due to the ad-hoc scenario that our business operations were suspended for approximately two months between late-January 2020 to late-March 2020 when the PRC Government imposed a lockdown in Huanggang, Hubei Province due to the outbreak of COVID-19. Meanwhile, the purchase orders that we

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received during FY2020 remained relatively stable as compared to FY2019. As such, our production facility was operated at a high utilisation level to fulfill the purchase orders in the remaining period of the year after the lockdown.

The utilisation rate of our production facility remained at a relatively high level for FY2021 primarily due to the increase in purchase orders placed by our major customers during the period.

Repair and maintenance

We have implemented a maintenance system for our machinery, which includes regular inspection and regular repair and maintenance of machinery. This allows us to operate our production lines at optimal levels. We carry out routine cleaning and maintenance of our machinery to enhance its useful life. We also conduct major annual maintenance work and engage external mechanics to carry out repair and maintenance on our machinery on an as-needed basis. Our maintenance system aims to maintain operational efficiency and high-quality control standards. For FY2019, FY2020 FY2021, we incurred repair and maintenance expenses of approximately RMB1.0 million, RMB0.7 million and RMB0.4 million, respectively. We did not experience any material or prolonged interruptions to our production process due to machinery failure or breakdown during the Track Record Period and up to the Latest Practicable Date.

Production department

We devote significant resources to improve the capacity and capability of our production department. As at the Latest Practicable Date, we employed a total of 47 personnel under our production department. We provide induction training and on-going technical training to the production staff on, among others, safe operation and maintenance of machinery. Moreover, we provide training to our production staff from time to time in order to update them on production techniques. We also regularly update our production staff on any quality issues arising from our inspection during the production process and feedback from our customers.

MARKETING

Our Group seeks new business opportunities mainly through (i) incoming enquiries from new and existing customers; (ii) referrals from existing customers; (iii) identification of tender opportunities by regularly monitoring tender notices published by cigarette package manufacturers on various tendering platforms; and (iv) marketing and promotion activities carried out by our marketing department. Our Directors are of the view that our success is largely attributable to our reputation and stable relationship with our customers. As at the Latest Practicable Date, our marketing department consisted a total of 14 staff members. Our marketing staff make regular visit to our customers across China in order to be able to attend to customers' queries as soon as possible. As our products are customised to customers' product specifications, we seek to maintain close contacts with our customers to understand their business and production needs, while at the same time keep them informed of our latest product offerings and development activities. Moreover, through regular visits to our customers and obtaining feedback from them, we can stay abreast of the latest trend and development of our customers' products requirements and to ensure that our products fulfil their production schedule and expectations.

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Our sales representatives have engaged in business development and marketing activities in various provinces in the PRC. They are responsible for (i) enhancing our promotion and sales efforts; (ii) actively approaching and liaising with our existing and potential customers; and (iii) collecting feedbacks and handling any queries on our products from customers in those provinces.

We believe our strategy enables us to promptly respond to market developments and provide customised products to our customers. When customers require new product development, our marketing department and production department will strive to ascertain their needs promptly. Our marketing department reports customers' feedback to our management team and also conducts internal market analysis from time to time on latest industry trends.

Supplier selection process of our customers

According to the Industry Report, cigarette package manufacturers generally select new suppliers through (i) direct negotiations with potential suppliers; or (ii) inviting potential suppliers to participate in tenders for sales of cigarette packaging paper.

Direct negotiation

We have secured the engagements with the majority of our customers through direct negotiations with them. We made acquaintances with these customers mainly through (i) their incoming enquiries; (ii) referrals from existing customers; and (iii) marketing and promotion activities carried out by our marketing department. If a customer accepts our quotation, it will generally enter into a framework sales agreement with us.

Tender selection process

Our marketing department regularly monitors tender notices published by cigarette package manufacturers on various online tendering platforms for potential new business opportunities. We also receive customers' invitations from time to time to submit tenders. The tender documents provided by potential customers generally contain the eligibility of the tenderers, description of the products required, documentary requirements on tender submissions and timeframe for submitting tenders. If our tender submission is successful, the customer will enter into a framework sales agreement with us.

Pricing strategy

We determine our pricing on a case-by-case basis by adopting a cost-plus pricing approach. After estimating our production costs, which mainly include (i) the estimated material costs; (ii) our direct labour cost; and (iii) our other production costs, our management team will proceed to determine the additional profit margin, taking into account factors including (i) the technical requirements and specifications; (ii) the relationship with the customers; (iii) the market standing and position of the customers; and (iv) the credit history and financial track record of the customers. For customers which engage suppliers through tender selection process, the tender documents will generally specify the maximum tender unit price for the products to be supplied and potential suppliers (including our Group) are required to submit a unit price at or below the specified maximum price in the tender submissions. There is no such restriction on our pricing for those customers who engaged us through direct negotiations.

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The purchase orders placed by the customers are charged according to the pre-agreed unit price as stated in the framework sales agreements, which are generally valid for one year to two years. Upon renewal of the framework sales agreements, we will review and adjust the unit price for our products if necessary.

Seasonality and potential market development of cigarette packaging in the PRC

Our business is in the upstream sector within the cigarette industry value chain where cigarette sales to consumers are at the end of the value chain. For further information, please refer to the paragraph headed “Industry overview — Overview of the cigarette packaging paper manufacturing industry in the PRC, Hubei and other regions” in this document for the overview of our industry’s value chain. Our sales largely correspond to the fluctuations in the sales of the cigarette industry in the PRC. Demand for cigarettes in the PRC is generally higher during Chinese New Year as the practice of gifting cigarettes is common in Chinese culture. Some of our customers may place more purchase orders with us prior to the Chinese New Year to cope with their production schedule. We may therefore record higher sales before Chinese New Year.

According to the Industry Report, “plain packaging” is a way of cigarette packaging without any branding, colour, imagery, corporate logo, or trademark. “Plain packaging” could only include the brand name of the cigarette in a specified size, font, and place on the cigarette pack, in addition to health warnings and any other legally mandated information such as toxic constituents and tax-paid stamps. There are around 15 overseas countries adopting “plain packaging” in their cigarette industries until 2021.

According to our PRC Legal Advisers, the State Tobacco Monopoly Administration has enacted various cigarette labeling laws, rules, and regulations that set forth specific requirements on the text, size, colour, and background of cigarette packaging in the PRC. Warnings in relation to the potentially harmful effects of smoking on health must be printed in Chinese and cover at least 35 percent of the front side of the cigarette package. Changes to these regulations may further hamper the growth of the cigarette packaging paper manufacturing industry in the PRC. As at the Latest Practicable Date, no laws, rules or regulations that require plain packaging on cigarette in effective or to be effective.

According to the State Tobacco Monopoly Administration, the current cigarette packaging regulations in the PRC have complied with the requirements of the Framework Convention on Tobacco Control (《煙草控制框架公約》) issued by the World Health Organization, and the health warnings on the cigarette packages are effective to the consumers. According to the Industry Report, in the future, the State Tobacco Monopoly Administration will continue to focus on the research of strengthening the health warnings on cigarette packages, and there is no indication that the PRC Government intends to adopt “plain packaging” on cigarette as a measure of tobacco control.

There is no guarantee that the PRC Government will not adopt “plain packaging” on cigarette as a measure of tobacco control in the future. Should “plain packaging” be adopted by the PRC Government and depending on the scope of restrictions which may be implemented thereunder, cigarette packaging paper manufacturers, such as our Group, will be adversely affected. Taking into consideration (i) as advised by our PRC Legal Advisers, as at the Latest Practicable Date, no laws, rules or regulations that require plain packaging on cigarette in effective

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or to be effective; and (ii) according to the Industry Report, there is no indication that the PRC Government intends to adopt “plain packaging” on cigarette as a measure of tobacco control, our Directors do not foresee any material adverse impact arising from “plain packaging” on our Group’s business and financial performance in the near future.

OUR CUSTOMERS

Characteristics of our customers

For FY2019, FY2020 and FY2021, we had generated sales from 37, 40 and 34^(Note) customers, respectively. We supply our products primarily to cigarette package manufacturers which operate in different provinces of the PRC. For FY2019, FY2020 and FY2021, our direct sales to cigarette package manufacturers contributed approximately 87.1%, 89.6% and 85.6% of our total revenue, respectively. To a much lesser extent, some of our customers are trading companies in the PRC which on-sell our products to cigarette package manufacturers. Leveraging the distribution channels and sales network of these trading companies, our Directors consider that we can further diversify our customer base and expand our reach to different cigarette package manufacturers. For FY2019, FY2020 and FY2021, our sales to trading companies contributed approximately 12.9%, 10.4% and 14.4% of our total revenue, respectively. The table below sets forth a breakdown of our revenue by customer types during the Track Record Period:

	FY2019		FY2020		FY2021	
	<i>RMB'000</i>	%	<i>RMB'000</i>	%	<i>RMB'000</i>	%
Cigarette package manufacturers	272,368	87.1	285,152	89.6	316,931	85.6
Trading companies	<u>40,432</u>	<u>12.9</u>	<u>33,194</u>	<u>10.4</u>	<u>53,380</u>	<u>14.4</u>
Total	<u><u>312,800</u></u>	<u><u>100.0</u></u>	<u><u>318,346</u></u>	<u><u>100.0</u></u>	<u><u>370,311</u></u>	<u><u>100.0</u></u>

Note: Our Group allocated a significant amount of resources in fulfilling the purchase orders placed by our top five customers for FY2021 which in aggregate generated revenue of approximately RMB279.1 million to our Group for FY2021, representing approximately 75.4% of our total revenue for the corresponding year. Our Group is committed to accommodate the demand from our major customers to the extent our resources allow. Being limited by our then production capacity, our Group had placed more focus and allocated a substantial portion of our production capacity on serving our top five customers for FY2021.

Cigarette package manufacturers

During the Track Record Period, a majority of our revenue was derived from cigarette package manufacturers in the PRC. For FY2019, FY2020 and FY2021, we derived revenue of approximately RMB272.4 million, RMB285.2 million and RMB316.9 million from cigarette package manufacturers, representing approximately 87.1%, 89.6% and 85.6% of our total revenue, respectively. The products sold by us to cigarette package manufacturers are used in the manufacture of cigarette packages for various cigarette brands in the PRC.

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Some of our top customers are established market players in the cigarette package manufacturing industry. For instance, Hubei Golden Three Gorges is a subsidiary of a company listed on the Stock Exchange, whereas Customer Group C are subsidiaries of state-owned enterprises in the PRC. For further details on our top customers, please refer to the paragraph headed “Top customers” below in this section.

Trading companies

To a much lesser extent, we also sell our products to trading companies in the PRC which on-sell our products to cigarette package manufacturers. According to the Industry Report, it is not uncommon for cigarette package manufacturers in the PRC to purchase packaging materials through trading companies in view of their network in sourcing quality products from various packaging materials manufacturers. Leveraging the distribution channels and sales network of these trading companies, our Directors consider that we can further diversify our customer base and expand our reach to different cigarette package manufacturers. For FY2019, FY2020 and FY2021, we derived revenue of approximately RMB40.4 million, RMB33.2 million and RMB53.4 million from trading company customers, representing approximately 12.9%, 10.4% and 14.4% of our total revenue, respectively. During the Track Record Period, we had a total of three trading company customers including Harbin Shixiang and two other trading companies, namely “**Trading Co. A**” and “**Trading Co. B**”. The table below sets forth a breakdown of our revenue derived from trading company customers during the Track Record Period:

	FY2019		FY2020		FY2021	
	<i>RMB'000</i>	%	<i>RMB'000</i>	%	<i>RMB'000</i>	%
Harbin Shixiang	34,910	86.3	15,264	46.0	42,821	80.2
Trading Co. A	5,522	13.7	8,488	25.6	5,133	9.6
Trading Co. B	—	—	9,442	28.4	5,426	10.2
Total	<u>40,432</u>	<u>100.0</u>	<u>33,194</u>	<u>100.0</u>	<u>53,380</u>	<u>100.0</u>

Background of our trading company customers

Harbin Shixiang is a limited liability company established in the Heilongjiang Province in the PRC on 2 April 2007. Harbin Shixiang is principally engaged in the distribution of paper and other products. According to publicly available information, Harbin Shixiang is owned equally by two independent third parties.

Trading Co. A is a limited liability company established in Henan Province in the PRC on 17 January 2014. Trading Co. A is principally engaged in the distribution of paper products and packaging materials. According to publicly available information, Trading Co. A is owned by two independent third parties as to 60% and 40%.

Trading Co. B is a limited liability company established in Hubei Province in the PRC on 25 November 2009. Trading Co. B is principally engaged in the distribution of paper products and packaging materials. According to publicly available information, Trading Co. B is owned equally by two independent third parties.

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Commercial arrangements with our trading company customers

Our relationship with trading company customers, being independent third parties, is a seller/buyer relationship. We do not set sales or expansion target or minimum purchase commitment for our trading company customers. We also do not impose any control over the pricing policy of our trading company customers on our products. Similar to our other customers, we generally enter into a framework sales agreement with our trading company customers. The principal terms of the framework sales agreement with our trading company customers are similar to those with our cigarette package manufacturer customers. For further details, please refer to the paragraph headed “Our customers — Principal terms of engagement” below in this section. During the contract term of the framework sales agreement, our trading company customers are entitled to place purchase orders with us. Save as the principal terms set forth in the framework sales agreement, we do not exert any other specific control on our trading company customers.

(i) Product returns arrangement

We do not accept any product return from our customers, including trading company customers, except due to product defects caused by us. We did not experience any material product return during the Track Record Period. For details of our product return policy, please refer to the paragraph headed “Our customers — Principal terms of engagement” in this section.

(ii) No geographical exclusivity

We do not impose any geographical exclusivity to our customers, including trading company customers. Our Directors believe that the risk of cannibalisation, if any, among our trading company customers is low taking into consideration (i) our Group only had three trading company customers during the Track Record Period, each of which is located in a different regions in the PRC; (ii) save and except for Harbin Shixiang, our revenue derived from other trading company customers, namely Trading Co. A and Trading Co. B, accounted for a small portion of our total revenue during the Track Record Period. For FY2019, FY2020 and FY2021, our revenue derived from Trading Co. A accounted for approximately 1.8%, 2.7% and 1.4% of our total revenue, respectively; whereas our Group only derived revenue from Trading Co. B in FY2020 and FY2021 which accounted for approximately 3.0% and 1.5% of our total revenue in the corresponding year, respectively; and (iii) similar to our other customers, our trading company customers place purchase orders with us on a case-by-case basis. Given we do not accept return or exchange of obsolete products from our customers, our Directors consider that our trading company customers are likely to place purchase orders with us only after they have ascertained the demand for our products from downstream customers.

Based on our internal records and information provided by our trading company customers, Trading Co. A and Trading Co. B did not on sell our products to any of our direct customers or their affiliates during the Track Record Period; whereas Harbin Shixiang had on sold our products to one of our direct customers (the “**Direct Customer**”), being a cigarette package manufacturer in the PRC, during the Track Record Period. For FY2019, FY2020 and FY2021, our Group generated revenue of approximately RMB9,000, RMB86,000 and nil from the Direct Customer, respectively.

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According to the Industry Report, cigarette package manufacturers generally select new suppliers through (i) direct negotiations with potential suppliers; or (ii) inviting potential suppliers to participate in tenders for sales of cigarette packaging paper. In this regard, our trading company customer confirmed with us that they have been awarded with the tender of certain cigarette package manufacturers which had no prior business relationship with our Group for the supply of cigarette packaging paper products. Given our Group has not established business relationship with or obtained tender from these cigarette package manufacturers, we could not supply cigarette packaging paper products directly to them. In this regard, our trading company customer had procured cigarette packaging paper products from us and on sold to these cigarette package manufacturers. In addition, our trading company customers also confirmed that the Direct Customer purchased our Group’s products through them partly because they were able to offer more favourable credit terms, which allowed financing flexibility to the Direct Customer.

(iii) Internal control measures to monitor inventory risks

We do not accept any product return from our customers, including trading company customers, except due to product defects caused by us. For details of our product return policy, please refer to the paragraph headed “Our customers — Principal terms of engagement” in this section. We believe that the risk of inventory accumulation by our customers is insignificant as (i) we do not retain the risk of ownership of our products once the legal title of our products has been passed to them; (ii) our customers do not have a legal right to return products to us except for product defects caused by us; (iii) we are not contractually required to repurchase our products if they remain unsold by the trading companies; and (iv) we do not guarantee a minimum resale value of our products.

Sales by geographical locations of our customers

Our customers are all situated in China, and a majority of them are situated in Hubei Province and Henan Province. The following table sets forth a breakdown of our revenue by geographical locations of our customers during the Track Record Period:

	FY2019		FY2020		FY2021	
	RMB'000	%	RMB'000	%	RMB'000	%
Hubei Province	166,038	53.1	186,063	58.4	166,162	44.9
Henan Province	63,883	20.4	94,500	29.7	121,230	32.7
North-east China ^(Note 1)	34,910	11.2	16,959	5.3	44,165	11.9
East China ^(Note 2)	11,280	3.6	13,138	4.1	33,266	9.0
Others ^(Note 3)	36,689	11.7	7,686	2.5	5,488	1.5
Total	312,800	100.0	318,346	100.0	370,311	100.0

Notes:

1. North-east China mainly include Liaoning Province, Jilin Province and Heilongjiang Province.
2. East China mainly include Shanghai Municipality, Jiangsu Province, Zhejiang Province, Anhui Province, Fujian Province, Jiangxi Province and Shandong Province.
3. Others mainly include Guangdong Province, Shaanxi Province and Chongqing Municipality.

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Our revenue generated from Henan Province increased substantially from approximately RMB63.9 million for FY2019 to approximately RMB94.5 million for FY2020 and further increased to approximately RMB121.2 million for FY2021, which was mainly attributable to the increase in revenue generated from two customers, namely Customer E and Changge Dayang, which are located in Henan Province. Our revenue generated from Customer E increased from approximately RMB19.8 million for FY2019 to RMB32.1 million for FY2020 and further increased to approximately RMB55.6 million for FY2021; whereas our revenue generated from Changge Dayang increased from approximately RMB26.2 million for FY2019 to approximately RMB34.2 million for FY2020 and further increased to approximately RMB50.7 million for FY2021.

Our revenue generated from North-east China decreased from approximately RMB34.9 million for FY2019 to approximately RMB17.0 million for FY2020, which was mainly attributable to the decrease in our revenue generated from Harbin Shixiang, which is located in Heilongjiang Province, from approximately RMB34.9 million for FY2019 to approximately RMB15.3 million for FY2020, representing a decrease of approximately 56.2%. Such decrease was mainly attributable to (i) changes to the package design of two cigarette brands in 2020, which substituted the use of transfer paper with white cardboard and hence resulted in a decrease in revenue of approximately RMB13.3 million; and (ii) loss of sales opportunities due to suspension of business operations from late-January 2020 to late-March 2020 due to the outbreak of COVID-19. Our revenue generated from North-east China increased from approximately RMB17.0 million for FY2020 to approximately RMB44.2 million for FY2021, which was mainly attributable to the increase in our revenue generated from Harbin Shixiang from approximately RMB15.3 million for FY2020 to RMB42.8 million for FY2021. Such increase was mainly attributable to the increase in sales of cigarette packaging paper to Harbin Shixiang for the use in the manufacture of cigarette packages for two “Dual 15 cigarette brands” namely, Brand A and Brand G. For further details, please refer to the paragraph headed “Our products and services — Breakdown of our product sales by cigarette brands” in this section.

Our revenue generated from East China increased from approximately RMB13.1 million for FY2020 to approximately RMB33.3 million for FY2021, which was mainly attributable to (i) the increase in our revenue generated from a state-owned enterprise with its headquarters in Shanghai from approximately RMB8.4 million for FY2020 to approximately RMB17.5 million for FY2021; and (ii) the revenue generated from a new cigarette package manufacturer customer based in Anhui Province, being a subsidiary of a company listed on the Stock Exchange, of approximately RMB12.8 million for FY2021.

Our revenue generated from other regions in the PRC decreased from approximately RMB36.7 million for FY2019 to approximately RMB7.7 million for FY2020 which was mainly attributable to the decrease in number of our customers from other regions from 14 for FY2019 to nine for FY2020.

Top customers

For FY2019, FY2020 and FY2021, the percentage of our total revenue attributable to our top customer amounted to approximately 27.1%, 28.8% and 25.4%, respectively, while the percentage of our total revenue attributable to our top five customers combined amounted to approximately 62.7%, 68.6% and 75.4%, respectively.

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The following tables set out information of our top five customers during the Track Record Period:

FY2019

Rank	Customer	Principal business activities	Type of product(s)/ service provided to our customers	Year of commencement of business relationship	Typical credit terms and payment method	Revenue derived from the customer	
						RMB'000	%
1	Hubei Golden Three Gorges <i>(Note 1)</i>	A subsidiary of a company listed on the Stock Exchange principally engaged in manufacture of cigarette package with its headquarters in Hubei Province	Transfer paper, laminated paper and provision of cigarette packaging paper processing services	Since 2017	90 days; by bank acceptance bills	84,918	27.1
2	Harbin Shixiang <i>(Note 2)</i>	A limited company principally engaged in distribution of paper and other products with its headquarters in Heilongjiang Province	Transfer paper and frame paper	Since 2017	60 days; by bank acceptance bills	34,910	11.2
3	Customer Group C <i>(Note 3)</i>	A group of companies owned by a state-owned enterprise principally engaged in manufacture of cigarette package with its headquarters in Hubei Province	Transfer paper	Since 2018	60 days; by bank transfer	30,377	9.7
4	Changge Dayang <i>(Notes 4 and 5)</i>	A limited company principally engaged in manufacture of cigarette package with its headquarters in Henan Province	Transfer paper and laminated paper	Since 2018	60 days; by bank acceptance bills	26,161	8.4
5	Customer E <i>(Note 6)</i>	A collectively-owned enterprise principally engaged in manufacture of cigarette package with its headquarters in Henan Province	Transfer paper and laminated paper	Since 2014	120 days; by bank acceptance bills	19,847	6.3
Total five customers combined						196,213	62.7
All other customers						116,587	37.3
Total revenue						<u>312,800</u>	<u>100.0</u>

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FY2020

Rank	Customer	Principal business activities	Type of product(s)/ service provided to our customers	Year of commencement of business relationship	Typical credit terms and payment method	Revenue derived from the customer	
						RMB'000	%
1	Hubei Golden Three Gorges <i>(Note 1)</i>	A subsidiary of a company listed on the Stock Exchange principally engaged in manufacture of cigarette package with its headquarters in Hubei Province	Transfer paper, laminated paper and provision of cigarette packaging paper processing services	Since 2017	90 days; by bank acceptance bills	91,766	28.8
2	Customer Group C <i>(Note 3)</i>	A group of companies owned by a state-owned enterprise principally engaged in manufacture of cigarette package with its headquarters in Hubei Province	Transfer paper	Since 2018	60 days; by bank transfer	42,780	13.4
3	Change Dayang <i>(Note 4)</i>	A limited company principally engaged in manufacture of cigarette package with its headquarters in Henan Province	Transfer paper and laminated paper	Since 2018	60 to 90 days; by bank acceptance bills	34,162	10.7
4	Customer E <i>(Note 6)</i>	A collectively-owned enterprise principally engaged in manufacture of cigarette package with its headquarters in Henan Province	Transfer paper and laminated paper	Since 2014	120 days; by bank acceptance bills	32,092	10.1
5	Hubei Xinjiarui <i>(Note 7)</i>	A limited company principally engaged in manufacture of cigarette package with its headquarters in Hubei Province	Transfer paper and laminated paper	Since 2019	60 days; by bank transfer	17,845	5.6
Total five customers combined						218,645	68.6
All other customers						<u>99,701</u>	<u>31.4</u>
Total revenue						<u><u>318,346</u></u>	<u><u>100.0</u></u>

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FY2021

Rank	Customer	Principal business activities	Type of product(s)/ service provided to our customers	Year of commencement of business relationship	Typical credit terms and payment method	Revenue derived from the customer	
						RMB'000	%
1	Hubei Golden Three Gorges <i>(Note 1)</i>	A subsidiary of a company listed on the Stock Exchange principally engaged in manufacture of cigarette package with its headquarters in Hubei Province	Transfer paper and laminated paper	Since 2017	90 days; by bank acceptance bills	94,173	25.4
2	Customer E <i>(Note 6)</i>	A collectively-owned enterprise principally engaged in manufacture of cigarette package with its headquarters in Henan Province	Transfer paper and laminated paper	Since 2014	120 to 180 days; by bank acceptance bills	55,617	15.0
3	Change Dayang <i>(Note 4)</i>	A limited company principally engaged in manufacture of cigarette package with its headquarters in Henan Province	Transfer paper and laminated paper	Since 2018	60 to 120 days; by bank acceptance bills	50,659	13.7
4	Harbin Shixiang <i>(Note 2)</i>	A limited company principally engaged in distribution of paper and other products with its headquarters in Heilongjiang Province	Transfer paper and frame paper	Since 2017	120 days; by bank acceptance bills	42,821	11.6
5	Customer Group C <i>(Note 3)</i>	A group of companies owned by a state-owned enterprise principally engaged in manufacture of cigarette package with its headquarters in Hubei Province	Transfer paper	Since 2018	60 days; by bank transfer	35,809	9.7
Total five customers combined						279,079	75.4
All other customers						<u>91,232</u>	<u>24.6</u>
Total revenue						<u><u>370,311</u></u>	<u><u>100.0</u></u>

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Notes:

1. Hubei Golden Three Gorges was established in 1992. Hubei Golden Three Gorges is a subsidiary of Jia Yao Holdings Limited (stock code: 1626), a company listed on the Main Board of the Stock Exchange. Based on the latest annual report of Jia Yao Holdings Limited, its revenue amounted to over RMB570 million for the year ended 31 December 2020.
2. Harbin Shixiang was established in 2007. Harbin Shixiang has a registered capital of RMB1 million.
3. Customer Group C consists of two companies which were established in 1992 and 1994, respectively. Customer Group C has a total registered capital of approximately RMB300 million.
4. Changge Dayang was established in 2003. Changge Dayang has a registered capital of RMB80 million.
5. In FY2019, our Group generated revenue of approximately RMB26.2 million from the sales of 1,293 tonnes of cigarette packaging paper to Changge Dayang. The average selling price of our cigarette packaging paper products sold to Changge Dayang in FY2019 was approximately RMB20,200 per tonne, which was generally higher than the range of average selling price of all our product types ranging from approximately RMB7,500 to RMB15,200 per tonne. The relatively higher average selling price of our cigarette packaging paper products sold to Changge Dayang in FY2019 was mainly attributable to the sales of approximately 351 tonnes of low grammage transfer paper (the “**Low Grammage Transfer Paper**”) with an average selling price of approximately RMB39,500 per tonne, which generated revenue of approximately RMB13.9 million to our Group for FY2019, representing approximately 53.1% of our total revenue generated from Changge Dayang for the corresponding year. During the Track Record Period, our Group only sold the Low Grammage Transfer Paper to Changge Dayang. According to the Industry Report, grammage is a measurement that describes the area density of a paper product, which is expressed in terms of grams per square meter regardless of its thickness. With lower grammage, the total surface area of a paper product per tonne will be higher. The Low Grammage Transfer Paper sold to Changge Dayang represents the lowest grammage product manufactured by our Group during the Track Record Period. The larger surface area of the Low Grammage Transfer Paper per tonne generally involves higher production cost due to the (i) increase in raw materials such as film, ink and glue used for production; (ii) increase in utilities and labour costs owing to increased processing time; and (iii) higher technical difficulties and meticulous craftsmanship required for the Low Grammage Transfer Paper.

According to the Industry Report, low grammage transfer paper is normally used for mid-to-high-end cigarettes packaging, and the price generally ranged from approximately RMB28,000 per tonne to approximately RMB80,000 per tonne. Such price range could be attributed to various factors such as (i) different transfer paper types (e.g. laser beam transfer paper, gold/silver card transfer paper, cross-grained light column transfer paper, laser holographic transfer paper, platinum embossed transfer paper, etc.) involve different levels of complications in production and product designs, as well as raw materials used; (ii) different specifications might be customised per order depending on the customer’s requirement in terms of product color, design, production complexity and product application, etc.; and (iii) different source of raw materials, e.g. the regions and sourcing. According to the Industry Report, the average selling price of the Low Grammage Transfer Paper of approximately RMB39,500 per tonne sold by our Group to Changge Dayang is generally in line with the market price of low grammage transfer paper.

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For illustrative purpose, the following table sets forth a breakdown of the average selling price of our transfer paper, laminated paper and frame paper by grammage during the Track Record Period:

Grammage	FY2019 Average selling price <i>RMB per tonne</i>	FY2020 Average selling price <i>RMB per tonne</i>	FY2021 Average selling price <i>RMB per tonne</i>
Transfer paper			
— Low grammage	39,500 <i>(Note d)</i>	25,400	25,000
— Medium grammage	20,500	15,900	17,400
— High grammage	14,500	14,600	15,200
Laminated paper			
— Medium grammage	14,700	14,200	15,100
— High grammage	11,100	10,700	10,900
Frame paper			
— Medium grammage	8,400	—	—
— High grammage	7,400	8,500	8,800

Notes:

- a. Low grammage refers to products with grammage under 100 gram per square meter.
 - b. Medium grammage refers to products with grammage between 100 gram and 200 gram per square meter.
 - c. High grammage refers to products with grammage above 200 gram per square meter.
 - d. The relatively higher average selling price of our low grammage transfer paper of approximately RMB39,500 per tonne for FY2019 was mainly attributable to the sales of approximately 351 tonnes of the Low Grammage Transfer Paper, which represented the lowest grammage product manufactured by our Group during the Track Record Period, to Change Dayang as aforementioned.
6. Customer E was established in 1995. Customer E has a registered capital of RMB10 million.
 7. Hubei Xinjarui was established in 2019. Hubei Xinjarui has a registered capital of RMB6 million.

None of our Directors, their close associates or any Shareholders who owned more than 5% of the number of issued shares of our Company as at the Latest Practicable Date had any interest in any of our top five customers during the Track Record Period.

Customer concentration

For FY2019, FY2020 and FY2021, the percentage of our total revenue attributable to our top customer amounted to approximately 27.1%, 28.8% and 25.4%, respectively, while the percentage of our total revenue attributable to our top five customers combined amounted to approximately 62.7%, 68.6% and 75.4%, respectively. In particular, a significant portion of our revenue during the Track Record Period was derived from Hubei Golden Three Gorges, Customer Group C,

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Change Dayang and Customer E, which have been our top five customers throughout the Track Record Period. Our Directors consider that our Group’s business model is sustainable despite such customer concentration due to the following factors:

Established relationship with major customers

- As at the Latest Practicable Date, our Group has established business relationship for seven years with one of our major customers during the Track Record Period (Customer E, as referred to in the paragraph headed “Our customers — Top customers” above in this section). Therefore, we will endeavor to accommodate their demand for our products to the extent our resources allow, resulting in them being our top customers. We also communicate regularly with our customers to obtain feedback on the quality standards of our products.

Mutual and complementary reliance

- Leveraging our business relationship with our major customers, we have developed a mutual and complementary business relationship with our major customers. We place significant emphasis on customer relationship management. Our marketing staff conducts regular visits to our customers to stay abreast of the latest trend and development of our customers’ products requirements and to ensure that our products fulfil their production schedule and expectations.
- According to the Industry Report, cigarette brand companies generally place emphasis on the consistency and standardisation of their cigarette packages as these are crucial to their brand recognition and product appeal. As such, consistency in the supply and quality of cigarette packaging papers is highly regarded by cigarette package manufacturers as well as cigarette manufacturers. Our Directors consider that our ability to consistently comply with applicable national and industrial standards has assisted our customers in fulfilling the cigarette packaging requirements and specifications of their customers (i.e. cigarette manufacturers), thereby resulting in the establishment of mutual and complementary reliance between our Group and our major customers.
- Our solid production capacity and research and development capabilities allow us to schedule our production flexibly, promptly respond to our customers’ requirements, ensure timely delivery of products at the required volume and supply customised products to our customers.

Industry landscape

- According to the Industry Report, cigarette manufacturers generally source cigarette packaging from a limited number of cigarette package manufacturers. Hence, it is not uncommon for cigarette packaging paper manufacturers to rely and focus on serving a limited number of cigarette package manufacturers. The established relationship between cigarette packaging paper manufacturers and cigarette package manufacturers have become a barrier for new entrants to capture shares in the cigarette packaging paper manufacturing industry. Based on the industry experience of our executive Directors, and having made reference to comparable company in similar industry, our Directors consider that it is an industry norm for cigarette packaging paper manufacturers to place reliance on a limited number of customers and the risk of reliance is not specific to our Group.

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- Our Directors believe that we have established significant market presence in the PRC cigarette packaging paper manufacturing industry. According to the Industry Report, we were ranked as the largest cigarette packaging paper manufacturer (in terms of sales value) in Hubei Province in 2020, with a market share of approximately 14.9% in Hubei Province.
- According to the Industry Report, the total sales value of cigarette packaging paper in the PRC is forecasted to grow from approximately RMB41,155.9 million in 2022 to RMB44,349.5 million in 2025 at a CAGR of approximately 2.5%. The forecasted increase in sales value of cigarette packaging paper manufacturing industry in the PRC is mainly attributable to (i) the continuation of the focus of cigarette industry towards mid-to-high-end cigarettes. Mid-to-high-end cigarettes, which are charged at a higher selling price, generally entail the use of cigarette packaging paper with advanced technical requirements so as to enhance their brand recognition and product appeal; and (ii) the increase in purchasing power of PRC citizens will likely result in a growth in demand for mid-to-high-end cigarettes. Driven by the PRC Government’s policy in promoting mid-to-high-end cigarettes such as the “Three qualities strategy (三品戰略)” which emphasises on improving the quality of cigarettes, variety of cigarette products and reputation of cigarette brands and the “136/345 development goals” which represent a series of targets related to the expansion of cigarette brands that the PRC Government is aiming to achieve in the next four to five years, the demand for mid-to-high-end cigarette packaging paper is expected to maintain a steady growth. With our product quality, experienced management team and past track record, our Directors believe that we are well-positioned to capture the growing demand for mid-to-high-end cigarette packaging paper in the PRC. For details on the industry drivers relating to our Group, please refer to the section headed “Industry overview” in this document.

Diversification of customer base

- Our Group has made consistent effort in geographic expansion and diversifying our customer base. For instance, the percentage of revenue derived by our Group from regions other than Hubei Province (i.e. Henan Province, North-east China, East China and other regions), has increased from approximately 46.9% for FY2019 to 55.1% for FY2021. Further, our Group has demonstrated a reduction in our reliance on Hubei Golden Three Gorges during the Track Record Period, as evidenced by the decrease in percentage of our revenue attributable to Hubei Golden Three Gorges from approximately 27.1% for FY2019 to approximately 25.4% for FY2021.
- Our sales representatives have engaged in business development and marketing activities in various provinces in the PRC. They are responsible for (i) enhancing our promotion and sales efforts; (ii) actively approaching and liaising with our existing and potential customers; and (iii) collecting feedbacks and handling any queries on our products from customers, in those provinces.
- While our customers are mainly located in Hubei Province and Henan Province, we strive to expand our reach to customers located at different provinces in the PRC. For example, our Group has established business relationship with (i) a cigarette package manufacturer, being a subsidiary of a state-owned enterprise in the PRC, with its headquarters in Shanghai Municipality in FY2019; (ii) a cigarette package manufacturer (being listed on the Shanghai

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Stock Exchange) with its headquarters in Anhui Province in FY2020; and (iii) a cigarette package manufacturer located in Yunnan Province, which is a subsidiary of a state-owned cigarette manufacturer, in FY2020.

Transferrable skills in broadening our customer base

- During the Track Record Period, our products were used as cigarette packaging materials for at least nine cigarette brands which were recognised as the “Dual 15 cigarette brands (雙十五煙草品牌)” by the STMA. The “Dual 15 cigarette brands (雙十五煙草品牌)” represent the 15 cigarette brands which derived the highest sales from mid-to-high-end cigarettes in 2020 in the PRC. Our Directors believe that our manufacturing capability and ability in fulfilling the stringent requirements of various cigarette package manufacturers and well-known cigarette brands in the PRC can be readily transferred to serve new customers.

No material adverse change in business relationship with major customers

- Our customers generally enter into framework sales agreements with us for a term ranging from one year to two years. During the contract term, the customers are entitled to place purchase orders with us based on the unit price as stated in the framework sales agreements. As at the Latest Practicable Date, our Group had entered into framework sales agreement with all our major customers.
- Out of the 40 customers which generated revenue to our Group in FY2020, 27 customers, which contributed revenue of approximately RMB305.4 million, representing approximately 95.9% of our total revenue for FY2020, had continued to place purchase orders with us in FY2021.
- Based on preliminary enquiries with our major customers, our Directors understand that our major customers were in general satisfied with the products and services supplied by our Group and such customers do not foresee any material reduction in the amount of purchase from our Group in the foreseeable future.

Based on the factors aforementioned, in particular taking into consideration the followings, the Directors consider that the likelihood of termination of business relationship between our Group and our major customers is relatively low and the Sponsor is not aware of any material circumstances which would result in material adverse change or termination of relationship between our Group and our major customers:

- (i) our customers generally engage us through direct negotiation or tender selection process. If our quotation or tender is accepted by our customers, they will typically confirm our engagement by entering into a framework sales agreement with us. If our customers are satisfied with the quality of our products, they would likely renew the framework sales agreement with us upon its expiry under a new unit price for the products with similar terms and conditions. Our Group had entered into framework sales agreement with each of our major customers for each financial year during the Track Record Period which serves as an indication of our Group’s capability in fulfilling the

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product quality requirements and specifications of our major customers. Further, based on preliminary enquiries with the major customers, the Sponsor understands that our Group has been one of the approved and major suppliers of our Group's major customers and there had not been any instance of early termination of framework sales agreements with our major customers during the Track Record Period and up to the Latest Practicable Date;

- (ii) each of our major customers had made purchases from our Group in each financial year during the Track Record Period. In particular, each of Hubei Golden Three Gorges, Customer Group C, Changge Dayang and Customer E, had been our top five customers throughout the Track Record Period. Each of our major customers has continued to place purchase orders with our Group subsequent to the Track Record Period and up to the Latest Practicable Date;
- (iii) based on preliminary enquiries with our Group's major customers, the Sponsor understands that (i) our major customers had not experienced any material quality issues, product return or delay in delivery in relation to the products supplied by our Group; (ii) our major customers are in general satisfied with the products and services supplied by our Group; and (iii) there has not been any material dispute, claim or litigation between our Group and our major customers;
- (iv) as confirmed by our Directors, our Group had not received any material claims or complaints from our major customers in relation to the quality of our products during the Track Record Period and up to the Latest Practicable Date. According to the Industry Report, cigarette brand companies generally place emphasis on the consistency and standardisation of their cigarette packages as these are crucial to their brand recognition and product appeal. As such, consistency in the supply and quality of cigarette packaging papers is highly regarded by cigarette package manufacturers as well as cigarette manufacturers. Our Directors consider that our ability to consistently comply with applicable national and industrial standards has assisted our customers in fulfilling the cigarette packaging requirements and specifications of their customers (i.e. cigarette manufacturers), thereby resulting in the establishment of mutual and complementary reliance between our Group and our major customers;
- (v) the majority of our major customers are principally engaged in the manufacture of cigarette package with established operating history of over 15 years. In particular, some of our major cigarette package manufacturer customers are subsidiaries of cigarette manufacturing group in the PRC. According to the Industry Report, cigarette manufacturers generally prefer to engage their fellow group members, being cigarette package manufacturers, to supply cigarette packages. In light of the established business operation and market position of our major customers in the cigarette package industry, it is believed that our major customers will continue to have a stable demand for our cigarette packaging paper products which are to be used in their manufacture of cigarette packages; and

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(vi) to the best of our Directors’ knowledge, each of our major cigarette package manufacturer customers is engaged in the manufacture of cigarette packages for the “Dual 15 cigarette brands (雙十五煙草品牌)”. During the Track Record Period, our products were used as cigarette packaging materials for at least nine cigarette brands which were recognised as the “Dual 15 cigarette brands (雙十五煙草品牌)”. It is believed that our Group’s established track record, experience and technical know-how in fulfilling the stringent quality and technical requirements of various cigarette package manufacturers and well-known cigarette brands, especially the “Dual 15 cigarette brands (雙十五煙草品牌)” are readily transferrable to serving our major customers.

Overlapping customers and suppliers

During the Track Record Period, we occasionally made purchases of certain types of raw materials from our customers for our own use and we also occasionally sold our products to our suppliers (the “**Overlapping Customers/Suppliers**”). During the Track Record Period, we had in total 20 Overlapping Customers/Suppliers.

Our group generally procured raw materials from our customers under the circumstances when we were required to source certain raw materials to produce cigarette packaging paper products on an urgent basis, and such raw materials were not then readily available from our suppliers. Meanwhile, our group generally sold our products to our suppliers upon their requests when they were unable or did not have the manufacturing capacity to perform certain processing to satisfy the demands of their customers.

The following table sets forth the details of our transactions with our Overlapping Customers/Suppliers that were either (i) our top customers/suppliers during the Track Record Period; or (ii) our customers/suppliers with procurement amount/sales amount representing over 1.0% of our total purchases/revenue for any financial year during the Track Record Period:

	Nature of the product(s) or service involved	FY2019		FY2020		FY2021	
		RMB’000	%	RMB’000	%	RMB’000	%
Hubei Golden Three Gorges							
Revenue derived and approximate % of our total revenue	Transfer paper, laminated paper and provision of cigarette packaging paper processing services	84,918	27.1	91,766	28.8	94,173	25.4
Procurement amounts and approximate % of our total purchases	Other accessory materials	111	Negligible	6	Negligible	3	Negligible
Gross profit margin			32.6		29.9		34.4

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	Nature of the product(s) or service involved	FY2019		FY2020		FY2021	
		RMB'000	%	RMB'000	%	RMB'000	%
Change Dayang							
Revenue derived and approximate % of our total revenue	Transfer paper and laminated paper	26,161	8.4	34,162	10.7	50,659	13.7
Procurement amounts and approximate % of our total purchases	White cardboard	—	—	—	—	307	0.1
Gross profit margin			22.2		14.0		17.2
Hubei Xinjiarui							
Revenue derived and approximate % of our total revenue	Transfer paper and laminated paper	15,488	5.0	17,845	5.6	15,573	4.2
Procurement amounts and approximate % of our total purchases	White cardboard	2	Negligible	—	—	—	—
Gross profit margin			33.2		32.4		22.9
Supplier D							
Revenue derived and approximate % of our total revenue	Transfer paper	2,443	0.8	1,482	0.5	1,913	0.5
Procurement amounts and approximate % of our total purchases	Film	20,038	8.3	18,400	7.6	19,628	6.5
Gross profit margin			10.1		11.0		14.0
Supplier F							
Revenue derived and approximate % of our total revenue	Transfer paper and laminated paper	2,102	0.7	4,858	1.5	3,659	1.0
Procurement amounts and approximate % of our total purchases	White cardboard	7,026	2.9	19,246	7.9	17,809	5.9
Gross profit margin			19.5		9.3		9.0
Company A ^(Note 1)							
Revenue derived and approximate % of our total revenue	Transfer paper and laminated paper	2,680	0.9	4,335	1.4	5,534	1.5
Procurement amounts and approximate % of our total purchases	White cardboard	6,186	2.6	1,862	0.8	828	0.3
Gross profit margin			10.7		13.9		14.0

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	Nature of the product(s) or service involved	FY2019		FY2020		FY2021	
		RMB'000	%	RMB'000	%	RMB'000	%
Company B <i>(Note 2)</i>							
Revenue derived and approximate % of our total revenue	Transfer paper and laminated paper	9,669	3.1	2,516	0.8	838	0.2
Procurement amounts and approximate % of our total purchases	White cardboard	6,854	2.8	80	Negligible	1,317	0.4
Gross profit margin			9.5	82.7	<i>(Note 3)</i>		5.6
Remaining eight customers							
Revenue derived and approximate & of total revenue	Transfer paper and laminated paper	28,153	9.0	19,404	6.1	16,657	4.5
Procurement amounts and approximate % of our total purchases	Film and other accessory materials	344	0.1	1,270	0.5	3,452	1.1
Gross profit margin			17.0		20.4		19.5
Remaining five suppliers							
Revenue derived and approximate & of total revenue	Transfer paper and laminated paper	3,105	1.0	745	0.2	513	0.1
Procurement amounts and approximate % of our total purchases	Film and other accessory materials	22,160	9.2	15,338	6.3	12,224	4.0
Gross profit margin			7.8		18.1		22.1

Notes:

1. Company A, being one of our Group’s customers, is a limited liability company established in Hubei, the PRC. Meanwhile, our Group has on occasions procured white cardboard from Company A when our Group’s production capacity was close to being fully utilised during the Track Record Period. In addition, our Group had made purchase for a type of white cardboard in the amount of approximately RMB6.0 million from Company A in FY2019 because, at the material time, we needed a relatively large quantity of white cardboard within a tight timeframe to meet our production schedule, while through our communication with Company A, we learnt that Company A happened to have some spare white cardboard which could readily match our needs.
2. Company B, being one of our Group’s customers, is a subsidiary of a company listed on the Stock Exchange. Meanwhile, our Group has on occasions procured white cardboard from Company B when our Group’s production capacity was close to being fully utilised during the Track Record Period. Given certain processing works had already been performed by Company B on the white cardboard supplied to our Group, we could save our production capacity from performing such processing works.
3. The gross profit margin of Company B was approximately 82.7% in FY2020. Such higher gross profit margin was mainly attributable to the revenue generated from the provision of cigarette packaging paper processing services. The revenue generated from the provision of cigarette packaging paper processing services accounted for approximately 99.5% of our revenue derived from such customer for FY2020. As the customers are responsible for the procurement of raw materials which they will provide us for further processing, we incurred labour costs, depreciation and utilities costs, thereby leading to high gross profit margin for our cigarette packaging paper processing services.

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4. Our gross profit margin of customers/suppliers may vary depending on the types of products ordered/procured by the customers/suppliers during the year. In particular, a product's selling price and production cost are affected by (i) its product features and technical requirements (e.g. anti-counterfeiting, laser, seamless, eco-friendliness); (ii) product specifications (e.g. grammage, texture); (iii) quality (e.g. folding endurance, surface evenness); and (iv) whether the production of the product involves the use of patents owned by us.

Principal terms of engagement

The salient terms of the framework sales agreements between us and our customers are as follows:

Product description

The framework sales agreements set out the type of products to be supplied by us and other product specifications and requirements, such as size, colour, materials, texture and cuttings.

Pricing

The framework sales agreements set out the unit price for each of our products to be supplied, which is typically agreed at a fixed price per tonne. Customers are not bound by any minimum purchase commitment under the framework sales agreements. The actual volume of products supplied by us are subject to the purchase orders made by the customers during the contract period, which are charged according to the unit price as stated in the framework sales agreements.

Contract term

The contract term of our framework sales agreements normally ranges from one year to two years. During the contract term, the customers are entitled to place purchase orders with us. In general, if the customers intend to continue our engagements upon expiry of the contract term, they may renew the framework sales agreements with us under a new unit price for the products with similar terms and conditions.

Payment term

We generally grant our customers a credit term of 60 to 180 days from the date of billing. Our customers generally settle their payments by bank transfer or bank acceptance bills.

Delivery arrangements

In general, we are responsible for the transportation of products to the destination specified by our customers on or before the date as stipulated in the purchase orders. The transportation costs and other related expenses are borne by us.

Quality requirements

Our products shall comply with the quality, technical and packaging requirements as specified in the framework sales agreements. Inspection will be conducted by our customers, on a sampling basis, on the quality and technical standards of our products. For each batch of product

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delivery, we are required to provide delivery notes and our outgoing quality inspection reports. If so requested by our customers, we may have to issue an undertaking to our customers on the quality and safety standards of our products. Our customers are generally entitled to return defective or substandard products to us.

We may be liable to pay damages to our customers if we are unable to deliver the ordered products within the specified time, or our products fail to meet our customers' requirements and/or specifications which results in damages suffered by our customers. Such damages are generally calculated on the basis of a fixed sum per day or according to a pre-agreed damages calculating mechanism. Our Directors confirm that during the Track Record Period and up to the Latest Practicable Date, no damages had been claimed by our customers against us.

Performance guarantee

Depending on the contract terms of the framework sales agreement, we may be required to deposit a specified amount with our customer as performance guarantee to secure our compliance with the framework sales agreement. The amount of performance guarantee is generally a fixed sum or based on a certain percentage, generally equivalent to 5%, of the estimated contract sum of the framework sales agreement. During the Track Record Period, the amount of performance guarantee provided by us generally ranged from approximately RMB50,000 to RMB0.4 million. If we fail to comply with the framework sales agreement, our customer would be entitled to guaranteed compensation for any monetary loss up to the amount of the performance guarantee. The performance guarantee will be released generally 30 days after the expiry of the framework sales agreement.

Anti-corruption

Depending on the contract terms of the framework sales agreement, we may be specifically required to strictly abide by the PRC laws and regulations related to anti-bribery and corruption. For instance, we may be strictly prohibited from (i) malicious collusion or bribery such as provision or acceptance of gifts or other improper benefits to/from the staff of our customers; (ii) provision of false information in our tender submission or for our customers' inspection; and (iii) disclosing commercial sensitive information in relation to the framework sales agreement.

Safety management

Depending on the contract terms of the framework sales agreement, we may be required by our customers to adhere to their safety management policies. For instance, our staff is (i) required to attend safety education and training before carrying out repair and maintenance activities at our production facility; and (ii) is strictly prohibited from smoking at our production facility.

Termination

Our customers are entitled to terminate our framework sales agreement if, among others, our performance ratings fall below the specified standards, we repeatedly fail to comply with the specified quality standards or repeatedly delay in our product delivery. During the Track Record Period and up to the Latest Practicable Date, none of our framework sales agreements with customers were terminated pursuant to the termination clause.

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Credit policy

Our marketing staff generally perform sales reconciliation with our customers after our products are delivered and accepted by our customer or our customer acknowledges acceptance after being satisfied with the results of its quality inspection and testing on the products. We generally perform sales reconciliation with our customers at the end of each month in respect of those products delivered within the same month. On occasions where the products are delivered close to the end of a month, the sales reconciliation for the same would be performed in the following month.

Once the sales reconciliation is completed, our marketing staff would submit application together with the sales reconciliation schedule to our finance department for issue of invoice. Our finance department would then cross-check the details set forth in the sales reconciliation schedule, including unit price, sales amount and sales volume, with our internal record. Should the details set forth in the reconciliation schedule conform with our internal record, the application will then be passed to our accountant and finance manager for approval. After our accountant and finance manager signs on the application as approval, our finance department will issue the invoice which will then be passed to the responsible marketing staff for handing over to the relevant customers. Our marketing staff is responsible for returning the acknowledgement of receipt of invoice from our customers to our finance department on a monthly basis.

Further, we would monitor the status of invoicing process in respect of our delivered products. In particular, by the end of each quarter, we would conduct analysis on those products which had been delivered but yet to be invoiced. Where necessary, internal meetings would be held to discuss and address any issue identified in our analysis.

We determine the credit period for our customers based on business relationship, the background, financial condition and credit records of the customers and current market conditions. We generally grant our customers a credit term of 60 to 180 days from the date of billing. Our customers generally settle their payments by bank transfer or bank acceptance bills. During the Track Record Period, all of our revenue was dominated in the Renminbi.

Our marketing department is responsible for the initial assessment of credit limits subject to the approval of our management and other monitoring procedures to ensure that follow-up actions are taken to recover overdue debts. We periodically review the credit terms and our customer's payment track record and, if appropriate, we will revise the credit terms granted to our customers.

Product return policy

We have implemented procedures to ensure that feedbacks from our customers are handled in a timely and appropriate manner. As a general policy, we accept product returns due to defects caused by us and bear the costs of having such products returned to us after our investigation on the cause of the defects. Our customers are required to report any quality issue to us within a prescribed time, normally three to ten days, upon their receipt or use of our products. We do not accept any product return unless it is related to quality issue. We did not experience any material product return during the Track Record Period.

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OUR SUPPLIERS

Raw materials

The principal types of raw materials for our production process include white cardboard, film and other accessory materials such as glue and ink. We source raw materials from various suppliers in the PRC. We generally enter into framework supply agreements with our suppliers for a specified term of one year in general. During the contract term of the framework supply agreement, we are entitled to place purchase orders with the supplier for procurement of raw materials at the specified pre-agreed unit price. This allows us to mitigate the risk arising from abrupt increase in market price of raw materials. Further, we generally source each type of raw materials from various suppliers. In the event of an abrupt increase in price of materials charged by a particular supplier, we are generally able to procure raw materials from other suppliers at commercially acceptable price.

Save as disclosed in the paragraph headed "Impact of the outbreak of COVID-19 on our operations" below in this section, our Group did not experience any material shortage or delay in the supply of raw materials during the Track Record Period and up to the Latest Practicable Date.

Top suppliers

For FY2019, FY2020 and FY2021, the percentage of our total purchases attributable from our top supplier amounted to approximately 15.4%, 21.9% and 22.6%, respectively, while the percentage of our total purchases from our top five suppliers combined amounted to approximately 52.3%, 59.0% and 54.0%, respectively.

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The following tables set out information of our top five suppliers during the Track Record Period:

FY2019

Rank	Supplier	Principal business activities	Type of product(s) provided by our suppliers	Year of commencement of business relationship	Typical credit terms and payment method	Purchase by us from the suppliers	
						RMB'000	%
1	Supplier A	A limited company engaged in, among others, supply of white cardboard with its headquarters in Shanghai Municipality	White cardboard	Since 2017	90 days; by bank acceptance bills	37,143	15.4
2	Supplier B <i>(Note 1)</i>	A limited company engaged in, among others, supply of white cardboard with its headquarters in Hubei Province	White cardboard	Since 2019	90 days; by bank acceptance bills	25,064	10.4
3	Supplier C <i>(Notes 2)</i>	A limited company engaged in, among others, supply of white cardboard with its headquarters in Hubei Province	White cardboard	Since 2014	90 days; by bank acceptance bills	24,185	10.0
4	Supplier D	A company listed on the Shenzhen Stock Exchange which is principally engaged in supply of film with its headquarters in Zhejiang Province	Film	Since 2017	90 days; by bank acceptance bills	20,038	8.3
5	Wuhan Jinfengda Paper Co., Ltd.* (武漢金豐達紙業有限公司)	A limited company engaged in, among others, supply of white cardboard with its headquarters in Hubei Province	White cardboard	Since 2017	90 days; by bank acceptance bills	19,659	8.2
Total five suppliers combined						126,089	52.3
All other suppliers						<u>114,593</u>	<u>47.7</u>
Total purchase						<u><u>240,682</u></u>	<u><u>100.0</u></u>

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FY2020

Rank	Supplier	Principal business activities	Type of product(s) provided by our suppliers	Year of commencement of business relationship	Typical credit terms and payment method	Purchase by us from the suppliers	
						RMB'000	%
1	Supplier B <i>(Note 1)</i>	A limited company engaged in, among others, supply of white cardboard with its headquarters in Hubei Province	White cardboard	Since 2019	90 days; by bank acceptance bills	53,196	21.9
2	Supplier A	A limited company engaged in, among others, supply of white cardboard with its headquarters in Shanghai Municipality	White cardboard	Since 2017	90 days; by bank acceptance bills	35,210	14.5
3	Supplier F	A limited company engaged in, among others, supply of white cardboard with its headquarters in Henan Province	White cardboard	Since 2019	90 days; by bank acceptance bills	19,246	7.9
4	Supplier D	A company listed on the Shenzhen Stock Exchange which is principally engaged in supply of film with its headquarters in Zhejiang Province	Film	Since 2017	90 days; by bank acceptance bills	18,400	7.6
5	Shenzhen Bolida Paper Industry Co., Ltd.* (深圳市博立達紙業有限公司)	A limited company engaged in, among others, supply of white cardboard with its headquarters in Guangdong Province	White cardboard	Since 2017	90 days; by bank acceptance bills	17,286	7.1
Total five suppliers combined						143,338	59.0
All other suppliers						99,983	41.0
Total purchase						<u>243,321</u>	<u>100.0</u>

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FY2021

Rank	Supplier	Principal business activities	Type of product(s) provided by our suppliers	Year of commencement of business relationship	Typical credit terms and payment method	Purchase by us from the suppliers	
						RMB'000	%
1	Supplier B <i>(Note 1)</i>	A limited company engaged in, among others, supply of white cardboard with its headquarters in Hubei Province	White cardboard	Since 2019	60 to 90 days; by bank acceptance bills	68,446	22.6
2	Supplier A	A limited company engaged in, among others, supply of white cardboard with its headquarters in Shanghai Municipality	White cardboard	Since 2017	60 to 90 days; by bank acceptance bills	42,564	14.1
3	Supplier D	A company listed on the Shenzhen Stock Exchange which is principally engaged in supply of film with its headquarters in Zhejiang Province	Film	Since 2017	60 to 90 days; by bank acceptance bills	19,628	6.5
4	Supplier F	A limited company engaged in, among others, supply of white cardboard with its headquarters in Henan Province	White cardboard	Since 2019	90 to 120 days; by bank acceptance bills	17,809	5.9
5	Supplier H	A limited company engaged in, among others, supply of film with its headquarters in Guangdong Province	Film	Since 2020	120 days; by bank acceptance bills	14,796	4.9
Total five suppliers combined						163,243	54.0
All other suppliers						<u>139,414</u>	<u>46.0</u>
Total purchase						<u><u>302,657</u></u>	<u><u>100.0</u></u>

Notes:

1. According to publicly available information, as at the Latest Practicable Date, Supplier B was owned as to 60% and 40% by an independent third party (“**Independent Third Party A**”) and another independent third party, respectively. Independent Third Party A has become the majority shareholder, holding 60% of the equity interests in Supplier B, since June 2021. Independent Third Party A has also been a supervisor of Supplier B since June 2021 until the Latest Practicable Date. The overall management and business operations of Supplier B has been overseen by an independent third party (“**Independent Third Party B**”) who joined Supplier B since 2019. Independent Third Party B previously owned 40% equity interest in Supplier C since its incorporation in August 2003 and he ceased to be a shareholder following the disposal of all of his equity interests in Supplier C in November 2018. Independent Third Party B had worked as a sales manager at Supplier C and was primarily responsible for the daily business operation of Supplier C since its incorporation in August 2003 up to November 2018, then subsequently left Supplier C and joined Supplier B in 2019.

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2. According to publicly available information, Supplier C was deregistered on 28 June 2020. Prior to its deregistration, Supplier C was owned as to 60% and 40% by Independent Third Party A and another independent third party, respectively. Since its incorporation in August 2003 up to its dissolution, Independent Third Party A owned 60% equity interest in Supplier C and had been the executive director and general manager of Supplier C. Independent Third Party A then subsequently became a supervisor and majority shareholder of Supplier B in June 2021 as mentioned in note 1 above.

None of our Directors, their close associates or any Shareholders who owned more than 5% of the number of issued shares of our Company as at the Latest Practicable Date had any interest in any of our top five suppliers during the Track Record Period.

Selection and evaluation of suppliers

We maintain an internal list of approved suppliers which is updated on a continual basis. As at 31 December 2021, we had more than 120 approved suppliers on our internal list. To ensure our product quality, our raw materials procurement policy is to make procurement from those approved suppliers who have passed our quality control assessment and have a satisfactory record of quality and on-time delivery.

Our procurement department is responsible for procuring raw materials based on our production needs and inventory level. We have maintained a set of internal manual on the procedures and standards for procurement of raw materials. Our procurement department generally invites our approved suppliers to submit tender or quotation for supply of materials. In selecting our suppliers, we take into account various factors, including pricing, product quality, production capacity, timeliness of delivery, after-sales service and ability to comply with our requirements and specifications. Depending on the volume of our purchase, once a supplier is selected, we typically enter into a framework supply agreement with the supplier. During the contract term of the framework supply agreement, we are entitled to place purchase orders with the supplier for procurement of raw materials at the specified pre-agreed unit price. Where the volume of our purchase is relatively insignificant, we may directly place purchase orders with the suppliers without entering into a framework supply agreement with them.

Principal terms of engagement

The salient terms of the framework supply agreements between us and our suppliers are as follows:

Product description

The framework supply agreements set out the type of products to be provided by our suppliers and other product specifications and requirements, such as size, colour, materials, texture and cuttings.

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Pricing

The framework supply agreements set out the unit price for each type of product, which is typically agreed at a fixed price. We are not bound by any minimum purchase commitment under the framework supply agreements. The actual volume of raw materials purchased is subject to the purchase orders placed by us during the contract period, which are charged according to the unit price as stated in the framework supply agreements.

Contract term

The contract term of framework supply agreements is one year in general. During the contract term, we may make procurement by placing purchase orders with our suppliers. Upon expiry of the contract term, we may (i) enter into negotiation with our existing suppliers for renewing the framework supply agreement with similar terms and conditions; or (ii) invite our approved suppliers to submit tender or quotation for our selection.

Delivery arrangements

Our suppliers are responsible for the transportation of products to our warehouse on or before the date as stipulated in the purchase orders. The transportation costs and other related expenses are borne by our suppliers.

Quality requirements

The products provided by our suppliers shall comply with the quality, technical, environmental and packaging requirements as specified in the framework supply agreements. For each batch of product delivery, we require our suppliers to provide us the delivery notes, outgoing quality inspection reports and environmental inspection report to ensure the quality of raw materials. We shall be entitled to return to the suppliers any defective raw materials which do not meet the agreed quality standard.

Termination

We are entitled to terminate the framework supply agreement if, among others, the performance ratings of our suppliers fall below the specified standards, our suppliers repeatedly fail to comply with our specified quality standards or deliver the products on or before the date as stipulated in the purchase orders.

INVENTORY CONTROL

Our inventories mainly comprise raw materials, finished goods and packaging materials and others. Our inventories are stored at the warehouse in our production facility under a suitable environment to maintain their quality. As at 31 December 2019, 2020 and 2021, our inventories amounted to approximately RMB40.7 million, RMB37.4 million and RMB50.1 million, respectively. For FY2019, FY2020 and FY2021, our inventory turnover days were approximately 62.2 days, 57.4 days and 55.4 days, respectively. For further details on our inventory analysis, please refer to the paragraph headed “Financial information — Discussion on selected financial position items — Inventories” in this document.

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Our Group has implemented inventory management policies to monitor and control our inventory level so as to facilitate our production in a timely manner and control our inventory at an optimal level to avoid obsolescence. We maintain an inventory register which clearly records each inflow and outflow of our inventory. Periodic stock-take is conducted to ensure the accuracy of stock-in and stock-out information on record. Throughout the year, our Group reviews the stock-take records and performs inventory ageing analysis to ensure that inventory is properly used and there is no unnecessary accumulation of aged inventory.

We generally maintain inventory of raw materials such as white cardboard and film based on our estimated production needs. For other raw materials, such as glue and ink, we generally maintain certain inventory level to ensure stable operations.

LOGISTICS

We engage third party logistics service providers for the delivery of our finished goods to the destination specified by our customers. The logistics service providers are responsible for the risks associated with the delivery of finished goods and have to bear any losses or other liabilities should the finished goods be damaged during delivery. For FY2019, FY2020 and FY2021, we incurred freight charges of approximately RMB4.6 million, RMB4.1 million and RMB5.3 million to third party logistics service providers, respectively.

QUALITY CONTROL

We place significant emphasis on product quality and safety by implementing stringent and comprehensive quality control measures covering all stages of our operations. Our quality management system has been certified to be in compliance with ISO 9001 certification. As at the Latest Practicable Date, our quality control department comprises 11 staff members who are responsible for conducting inspection and quality control tests throughout the production process. We are committed to achieving a low product defect rate and ensuring our products meet the requirements and specifications of our customers. Our quality control staff would conduct sample testing on our goods using our testing equipment throughout the production process. Our quality control department reports regularly in writing any quality issues arising from our production process and any defective products identified by our in-house inspectors or returned by our customers. We also communicate regularly with our customers to obtain feedback on the quality standards of our products.

Our Directors confirm that we had not experienced any material sales return during the Track Record Period and up to the Latest Practicable Date. Our Directors further confirmed that we had not experienced any cancellation of orders due to product quality issues and we had not been subject to any material product liability claim during the Track Record Period and up to the Latest Practicable Date.

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Quality control on raw materials

To ensure our product quality, our raw materials procurement policy is to make procurement from those approved suppliers who have passed our quality control assessment and have a satisfactory record of quality and on-time delivery. Our internal list of approved suppliers is reviewed on a continuous basis based on factors such as pricing, product quality, production capacity, timeliness of delivery, after-sales service and ability to comply with our requirements and specifications.

We generally require our suppliers to provide outgoing quality inspection report and environmental inspection report for each batch of product delivery to ensure the quality of raw materials. Our quality control department conducts inspection and testing on raw materials on a sampling basis when they are delivered to our production facility. Our suppliers are responsible for replacing any materials which do not meet the relevant standards and bear any associated costs incurred. Furthermore, we would conduct site visits at our suppliers’ production facilities and conduct periodic evaluation on our suppliers’ performance.

Quality control on the production process

Our quality control department closely monitors our production process to ensure strict compliance with our standard operating procedures. Our quality control department conducts various quality control measures throughout the production process including sample-testing on our goods based on their size, appearance, colour shading, temperature resistance and chemical compositions with the use of our testing equipment. We maintain a daily record of the number of defective products as an internal quality control measure to identify any malfunctioning production lines. If any defective raw material comes to light during our production process, we are generally entitled to request for product return.

We have implemented a maintenance system for our machinery, which includes regular inspection and regular repair and maintenance of machinery. Our production department is responsible for conducting management, examination, repair and maintenance of our production machinery from time to time in order to ensure their proper functioning and safe operation, thus enhancing our productivity and product quality. For further details on the repair and maintenance of our machinery, please refer to the paragraph headed “Production facility and capacity — Repair and maintenance” above in this section.

Quality control on finished goods

We perform in-house inspections on each batch of finished goods to ensure our products comply with applicable national and industrial standards, including, amongst others, *YC 263–2008 Tolerance Values of Volatile Organic Compounds in Cigarette Carton and Packet Packaging Papers* (卷煙條與盒包裝紙中揮發性有機化合物的限量), *YC/T 195–2005 Standard System of Material for Cigarette* (煙用材料標準體系) and *YC/T 273–2014 Requirements for Design of Cigarette Package* (卷煙包裝設計要求). We are generally required to provide outgoing quality inspection reports to our customers for each batch of product delivery.

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Any defective products identified will not be delivered to our customers. Our quality control inspectors will identify the causes for any product defects and follow up closely with our quality control department to confirm any deficiencies in our production process. Our quality control department is also responsible for identifying quality issues on returned products which do not meet our customers’ quality specifications.

RESEARCH AND DEVELOPMENT

Our Directors believe that research and development is crucial to maintaining our competitiveness in offering products that match with the evolving requirements and specifications of our customers. During the Track Record Period, the expenses incurred by us on research and development amounted to approximately RMB10.7 million, RMB10.4 million and RMB13.1 million for FY2019, FY2020 and FY2021, respectively. Our research and development department comprised 18 personnel as at the Latest Practicable Date and 17 of them have worked with us for over three years. Approximately half of our research and development personnel have possessed university degrees. Moreover, as at the Latest Practicable Date, we possessed more than ten sets of equipment for performing testing in the process of research and development. Through our research and development, we had continuously enhanced the anti-counterfeit features, appearances and eco-friendliness of our products, improved our production efficiency and expanded our product offerings in terms of texture, durability and colour mixture. In 2018, we have collaborated with a university in Xi’an (the “**University**”) in the development of new products and fine-tuning of our production process. We entered into a research and development collaboration agreement with the University (the “**First R&D Collaboration**”). The table below sets forth the salient terms of the First R&D Collaboration agreement:

Term	:	from January 2018 to December 2020
Principal objectives	:	(i) improving the anti-counterfeiting feature of holographic laser cigarette packaging paper; and (ii) formulation of high-gloss coating on cigarette packaging paper.
Obligations of our Group	:	Our Group shall: (i) provide the required production machinery and testing equipment for the First R&D Collaboration; (ii) provide funding and latest market information for the First R&D Collaboration; (iii) designate the specified number of personnel to participate in the First R&D Collaboration;

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- (iv) give priority to recruiting graduates of the University who participated in the First R&D Collaboration; and
- (v) allow lecturers of the University to conduct site visit and practice at our production facility.

- Obligations of the University** : the University shall:
- (i) assist our Group in developing and enhancing our products, technologies, craftsmanship, materials and application of new machinery and equipment;
 - (ii) give priority to sharing with our Group any technological advancement in production developed by the University;
 - (iii) assign the specified number of professional designers to participate in designing the structure and appearance of cigarette packaging paper; and
 - (iv) assist our Group in providing trainings to our employees.
- Intellectual property rights** : Each of our Group and the University shall have the right to use and transfer the intellectual properties arising from the First R&D Collaboration (the "**Intellectual Properties**"). Either party shall obtain prior written approval from the other party before any transfer of the Intellectual Properties.

In 2021, we have further collaborated with the University in the advancement of our technological innovation capacity by entering into a second research and development collaboration agreement with the University (the "**Second R&D Collaboration**"). The table below sets forth the salient terms of the Second R&D Collaboration.

- Term** : from October 2021 to December 2023
- Principal objectives** : improving our technological innovation capacity through collaboration with the University to achieve joint development in academic and production.

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- Obligations of our Group** : our Group shall:
- (i) provide the required production machinery and testing equipment for the Second R&D Collaboration;
 - (ii) provide funding and latest market information for the Second R&D Collaboration;
 - (iii) give priority to recruiting graduates of the University; and
 - (iv) allow lecturers of the University to conduct site visit and practice at our production facility.

- Obligations of the University** : the University shall:
- (i) provide technological support to the long-term development, strategic positioning and advancement of innovation of our Group;
 - (ii) assist our Group in developing and enhancing our products, technologies, craftsmanship, materials and application of new machinery and equipment;
 - (iii) give priority to sharing with our Group any technological advancement in production developed by the University; and
 - (iv) assist our Group in providing trainings to our employees.

During the Track Record Period, we undertook a total of 37 research and development projects. Set forth below are the scope of some of our research and development projects undertaken during the Track Record Period:

- research, development and application of a glue to be used for gravure printing;
- research and development of a colour tuning method;
- research on anti-dilution of ink used for anti-counterfeiting purpose;
- further research on the production method of transfer paper;
- research on eco-friendly coating as a substitute for solvent coating;
- use of eco-friendly water system for cooling in production process;

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- utilisation of hot air discharged from laminating machines for heating;
- research on expediting the drying process of back coating;
- research on the anti-counterfeiting feature of cigarette boxes for one of the “Dual 15 cigarette brand”; and
- research on reducing paper dust generated from winding machines.

As at the Latest Practicable Date, our Group had registered 24 patents in the PRC which are, in the opinion of our Directors, material to our business. For further details on our intellectual property rights, please refer to the paragraph headed “Statutory and general information — B. Further information about the business of our Group — 2. Intellectual property rights” set out in Appendix IV to this document.

CERTIFICATION AND RECOGNITIONS

Awards and recognitions

The following table summarises the major awards and recognitions obtained by us during our operating history:

Issuance date	Recognitions	Awarding authorities
November 2017	High and New Technology Enterprise (高新技術企業)	Department of Science and Technology of Hubei Province (湖北省科學技術廳), Department of Finance of Hubei Province (湖北省財政廳) and Hubei Provincial Tax Service, State Taxation Administration (國家稅務總局湖北省稅務局)
December 2018	Hong’an County 2015–2017 Outstanding Enterprises in Scientific and Technological Innovation Work (紅安縣2015–2017年度科技創新工作成果突出企業)	Hong’an County People’s Government (紅安縣人民政府)
May 2019	The 2019 (7th) Huanggang City Excellent Enterprise (Golden Eagle Award) (2019年(第七屆)黃岡市優秀企業(金鷹獎))	Huanggang City Entrepreneurs Association of Hubei Province* (湖北省黃岡市企業家協會) and Huanggang City Enterprise Confederation* (黃岡市企業聯合會)

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Certifications

The following table summarises the major certifications obtained by us during our operating history:

Certification	Issuing authority	Expiry date
ISO 9001:2015	China International Certification & Assessment (Beijing) Co., Ltd	22 September 2022
ISO 14001:2015	China International Certification & Assessment (Beijing) Co., Ltd	22 September 2022
ISO 45001:2018	China International Certification & Assessment (Beijing) Co., Ltd	22 September 2022
AAA-Level Enterprise Credit Rating Certificate	Beijing Zhiyunxin International Credit Evaluation Co., Ltd. (北京智雲信國際信用評價有限公司)	23 March 2024
AAA-Level Contract Abiding and Trustworthy Unit	Beijing Zhiyunxin International Credit Evaluation Co., Ltd. (北京智雲信國際信用評價有限公司)	23 March 2024
AAA-Level Quality Service Integrity Unit	Beijing Zhiyunxin International Credit Evaluation Co., Ltd. (北京智雲信國際信用評價有限公司)	23 March 2024

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EMPLOYEES

Number of employees

As at the Latest Practicable Date, we had a total of 131 employees (including our two executive Directors but excluding our non-executive Director and three independent non-executive Directors). All our employees were stationed in the PRC. The following table sets out a breakdown of our employees by function:

	As at the Latest Practicable Date
General management	2
Procurement	10
Production	47
Quality control	11
Marketing	14
Research and development	18
Finance	7
Administration	<u>22</u>
Total	<u><u>131</u></u>

Recruitment

We recruit our employees based on their work experience, education background and qualifications. We recruit our employees through online recruitment platform, referral from existing employees and recruitment exhibition. We assess our available human resources on a continuous basis to determine whether additional personnel are required to cope with our business development. We have entered into employment contracts with our employees, which set out, among others, the employee's remuneration, benefits, confidentiality obligations and grounds for termination of the employment. These employment contracts either have no fixed term, or if there is a fixed term, the term is generally up to three years, after which we will evaluate renewals based on performance appraisals.

Remuneration to our employees comprises salaries and allowances and bonuses. We generally review the performance of our employees by way of annual appraisals. The results of these reviews are used for the purposes of salary adjustments and promotion. We provide various trainings including induction training for new employees, on-the-job training, team-building training and external training for our employees to keep them abreast of the latest technical development relevant to our industry.

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We have established a labour union for our employees in 2017 in the PRC. We organise from time to time various social activities to create a harmonious working environment for our employees. During the Track Record Period and up to the Latest Practicable Date, we did not have any significant difficulty in recruiting employee and there had been no incidence of labour disputes, claims, litigation, administrative action or arbitration relating to labour disputes that had materially and adversely affected our operations.

Social insurance and housing provident funds contributions

Pursuant to applicable PRC laws and regulations, employers are required to make contributions to, and employees are required to participate in, a number of social security funds, including funds for basic pension insurance, basic medical insurance, unemployment insurance, work-related injury insurance and maternity insurance, and the housing provident fund. For further information, please refer to the paragraph headed "Regulatory overview — Laws and regulations relating to labor, social insurance and housing provident fund" in this document.

OCCUPATIONAL HEALTH AND SAFETY

We are subject to PRC occupational health and safety laws and regulations. For further details, please refer to the paragraph headed "Regulatory overview — Laws and regulations relating to labor, social insurance and housing provident fund" in this document. We are committed to providing a safe and healthy environment for our employees. We have established work safety policies and procedures to ensure that our operations are in compliance with applicable work safety laws and regulations. Our occupational health and safety management system has been certified to be in compliance with ISO 45001 certification.

We provide safety education and training to employees and have in place safety guidelines and operating manuals for our manufacturing process. We also provide our employees with training programmes on work safety in connection with matters such as the operation of machinery with a view to enhancing occupational safety and minimising the occurrence of work-related accidents and occupational illness. Our production department carries out regular safety inspections on our production facility to ensure compliance with the safety measures. Protective devices are installed and warning signs are posted to ensure production machinery is operated safely. Our production staff are provided with regular training on the operation of production machinery and occupational safety gear.

We have established a policy in recording and handling accidents. Upon occurrence of an accident, the employees shall report to the relevant department head and the administration department. The relevant department head shall prepare a report detailing the accident, including date and time of the accident, employees involved, cause, confirmation of responsibility, suggestion on rectification, and submit to the administration department. The department shall then carry out an investigation, assess the impact of the accident and recommend appropriate measures to improve safety.

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As advised by our PRC Legal Advisers, no administrative sanctions or penalties that have a material and adverse effect on our financial condition or business operations have been imposed upon us for the violation of PRC occupational health and safety laws and regulations during the Track Record Period. Further, as confirmed by our Directors, there were no material work-related injuries or fatalities at our production facility during the Track Record Period.

ENVIRONMENTAL, SOCIAL AND CORPORATE GOVERNANCE MATTERS

Environmental matters

We are subject to general PRC laws and regulations on environmental protection which govern environmental matters such as air pollution, noise emissions, discharge of waste water and waste residues. For details on these regulations, please refer to the section headed “Regulatory overview — Laws and regulations relating to environmental protection” in this document.

We are committed to conducting our business operations to comply with all applicable environmental laws and regulations, and endeavour to mitigate any negative effects of our operations on the environment. Our Directors believe that our production process does not generate a large amount of environmental hazards and does not impose significant adverse impact on the environment and that our environmental protection measures are adequate to comply with all applicable PRC laws and regulations on environmental protection. We have implemented various measures to ensure our compliance with the applicable environmental protection laws and regulations and our environmental management system has been certified to be in compliance with ISO 14001 certification. We engage third-party agencies to inspect, examine and evaluate environmental management system annually. For FY2019, FY2020 and FY2021, we incurred approximately RMB0.3 million, RMB0.2 million and RMB0.1 million, respectively, in relation to compliance with the applicable environmental requirements. We estimate that our annual cost of compliance with applicable PRC laws and regulations on environmental protection going forward will be consistent with our scale of operation.

During the Track Record Period and up to the Latest Practicable Date, we did not record any material non-compliance with applicable environmental requirements that results in prosecution or conviction being brought against us.

Governance regarding environmental, social and climate-related risks

We have established and implemented an environmental, social and governance (“ESG”) policy, which provides guidelines to the management of our Group’s ESG-related issues. Our Directors consider that the establishment and implementation of a comprehensive ESG policy will help increase the investment value of our Company and provide long term returns to our stakeholders. In particular, our policy on the management of severe weather conditions includes measures to be taken against increasing rate of extreme weather conditions such as heavy rainfall and flooding, which may damage our products in storage or during the course of delivery, resulting in delay to our product delivery schedule.

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Our Board is responsible for evaluating and managing any material ESG issues and climate-related risks and opportunities of our Group. Our Board will meet regularly to discuss issues and risks that are pertinent to the business development of our Group. Our Board will keep track of the latest policies implemented by the PRC Government in tackling climate change. For better identification of the risks and opportunities, our Board and senior management will attend to discussion on sustainability of the cigarette packaging paper manufacturing industry and low-carbon economy. Our Board will work closely in identifying future risks and opportunities, as well as identifying appropriate actions to cope with the ever-changing situations. Furthermore, our Board closely follows and monitors the latest requirements regarding ESG disclosure and regulatory compliance. We keep ourselves abreast of the Stock Exchange's ESG requirements and our Board will oversee the compilation of our ESG report after the [REDACTED] and shall review its content and quality before publication. We will seek advice from external professionals on enhancing our ESG compliance level where necessary.

Emissions management

Our major sources of greenhouse gas ("GHG") emissions generated from our production process mainly include the usage of electricity. Each of our laminating machines is equipped with overhead ventilation system which helps to filter GHG before emission. The fan blades of ventilation system are cleaned regularly and the equipment for filtering dust and smoke is maintained regularly to ensure its normal operation. In order to save energy and reduce emissions, we promote and adopt the use of energy-saving and efficient equipment, and switch off machinery and electronic appliances when they are not in use.

Wastewater management

We have obtained pollutant discharge permit to discharge industrial waste water and sewage legally. Wastewater produced during operation is mainly domestic sewage, which is processed through wastewater treatment facilities prior to being discharged to municipal wastewater system.

Waste management

In order to reduce the impact of solid waste on the environment, we have formulated clear guidelines for employees to identify, collect, store and dispose solid waste. Proper trainings are provided for our employees on waste classification. Reusable waste, such as paper and toner cartridge are handled by third-party waste management and recycling companies. Other waste which cannot be recycled are handled by waste disposal companies.

Noise management

Our machinery emanates noise during operation. To mitigate the disturbance created to the community and environment, we have implemented noise isolation at our production facility and provided hearing protection devices to our employees.

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Use of resources

We implement various measures to reduce wastage and consumption levels at our production facility. Our Group has promoted various energy conservation measures, including promoting and adopting the use of energy-saving and efficient equipment and switching off machinery and electronic appliances when they are not in use. Our Group has also established water conservation measures such as conducting periodic checks and maintenance on water supply system to avoid any leakage of faucets and gaskets.

Actual and potential impact of environmental and climate-related risks on our business, strategy and financial performance

We may be exposed to possible financial loss and non-financial detriments arising from environmental and climate-related risks which can be mainly categorised into (i) physical risks; and (ii) transitional risks.

(A) *Physical risks*

Physical risks represent risks arising from acute weather-related events and chronic shifts in climate patterns such as global warming and extreme weather conditions that potentially cause physical impact to us. Our business operations could be susceptible to the physical damages resulting from intense precipitation and floods. For instance, Henan Province which is located in proximity to Hubei Province experienced severe flooding caused by a period of prolonged intense precipitation in July 2021, which resulted in loss of life, widespread damage to property and severe disruption to the transportation network. Properties were washed away and the downpour disrupted electricity, water supplies and internet network in some parts of the Henan Province.

Our Directors consider that physical damages resulting from intense precipitation and floods could result in material adverse effect on our business operations, financial conditions and prospects. Our Group is principally engaged in the production of cigarette packaging paper products and our products are highly susceptible to water damage. Our cigarette packaging paper products will become unusable if they are submerged by flood, resulting in material financial loss to our Group. Further, extreme weather conditions could result in damages to our production facility and machinery, resulting in increased maintenance and replacement cost. In addition, intense precipitation and floods could endanger the health and safety of our employees. In order to strengthen our protection against intense precipitation and floods, we may have to implement enhanced flood protection measures such as installation of flood gate system and improvement in the water and drainage system at our production facility, resulting in an increase in our operation costs.

(B) *Transitional risks*

Transitional risks represent risks arising from climate change and climate-related issues resulting in potential changes to our operational practices. Owing to the increasing public awareness on eco-friendliness and the promotion of the use of environmentally friendly cigarette packaging materials by the PRC Government, the cigarette industry is steering towards the use of cigarette packaging paper with eco-friendliness features. The increase in public awareness on eco-friendliness will likely result in a shift in consumer preferences for cigarette packages which are

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more environmentally friendly. Our research and development capability is crucial to the development of cigarette packaging paper products with enhanced eco-friendliness features that match with the evolving requirements and specifications of our customers. Failing to enhance our research and development capabilities to meet the evolving demand of customers may result in a loss of sales and materially and adversely affect our business, results of operations and financial conditions.

Further, our production activities in the PRC are subject to applicable laws, regulations and standards promulgated by the relevant PRC Government authorities. For FY2019, FY2020 and FY2021, we incurred approximately RMB0.3 million, RMB0.2 million and RMB0.1 million, respectively, in relation to compliance with the applicable environmental requirements. In the event of any changes in the PRC laws and/or regulations and/or government policies on environmental protection and more stringent requirements are imposed on our Group, we may have to incur additional costs and expenses to comply with such requirements. Furthermore, if we fail to comply, or are alleged to fail to comply, with the relevant laws and regulations, we may be involved in costly litigation or subject to penalties or other sanctions imposed by the relevant PRC judicial or governmental authorities. Our reputation may also be adversely affected, resulting in a loss of business as our customers may be less inclined to purchase from manufacturers with environmental non-compliance. Regulatory development and evolution may potentially have significant impacts on our business operations and present transition risks to us.

Metrics used to assess and manage environmental and climate-related risks

We have taken into account the quantitative information that reflect our management for environmental and climate-related risks, which includes GHG emissions, resources consumption and waste production. The following table sets forth an analysis of our environmental performance during the Track Record Period:

Indicator	Unit	FY2019	FY2020	FY2021
GHG emissions				
Electricity consumption	tCO ₂ e	5,328	4,680	6,443
Electricity consumption intensity	tCO ₂ e per million RMB revenue	17.03	14.70	17.40
Resources consumption				
Freshwater consumption	m ³	8,227	9,891	10,485
Freshwater consumption intensity	m ³ per million RMB revenue	26.30	31.07	28.31
Waste production				
Solid waste	tonne	49	40	44
Solid waste intensity	tonne per million RMB revenue	0.16	0.13	0.12

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We will make continuous efforts in reaching the target of maintaining the electricity consumption intensity, freshwater consumption intensity and solid waste intensity at a level of 17.40 tCO₂e per million RMB revenue, 30.00m³ per million RMB revenue and 0.15 tonne per million RMB revenue, respectively, or below per annum in the three years ending 31 December 2024.

Social matters

Employment

We are committed to upholding the principles of equal opportunities, diversity and anti-discrimination in our workplace. Recruitment and retention of employees are based on a range of diversity parameters, including but not limited to gender, age, cultural and educational background, nationality, ethnicity, industry experience, skills and knowledge. We conduct performance appraisal to analyse our employees' personal strengths and weaknesses, and suitability for promotion or further training. Discretionary bonus and salary adjustment are given to our employees based on their performance appraisal.

Supply chain management

We have adopted a stringent policy and procedure on the selection of suppliers. We maintain an internal list of approved suppliers which is updated on a continuous basis. As at 31 December 2021, we had more than 120 approved suppliers on our internal list. To ensure our product quality, our raw materials procurement policy is to make procurement from those approved suppliers who have passed our quality control assessment and have a satisfactory record of quality and on-time delivery.

In selecting our suppliers, we take into account various factors, including pricing, product quality, production capacity, timeliness of delivery, after-sales service and ability to comply with our requirements and specifications. We carry out quality assurance checks on materials received from suppliers to ensure the quality and reliability of materials meet our requirements and specifications.

Caring for the community

We actively participate in community building and care for the disadvantaged. We will continue to promote social development and encourage employees to participate in charitable activities.

Anti-corruption

We strictly abide by the laws and regulations related to anti-corruption, including but not limited to the Anti-Unfair Competition Law of the PRC and the Criminal Law of the PRC. We uphold a high standard of integrity and have zero tolerance for corruption. We promote clear work ethics to employees, and strictly prohibit bribery, extortion, fraud, money laundering and other unethical behaviours, including gambling, misappropriation of our Group's assets, provision or acceptance of gifts or other improper benefits, etc..

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ESG and climate-related risks identification, assessment and management

Based on our management’s assessment and the ESG Industry Materiality Map issued by MSCI, a well-known investment research firm, we have identified the material ESG issues related to our business operation. In addition to the environment and climate-related issues as aforementioned, we have identified the following material ESG issues and their potential impacts:

Material topics	Potential risks, opportunities and impacts	Assessment and management
Increase in public awareness on eco-friendliness	In 2014, the State Tobacco Monopoly Administration for the PRC Tobacco Industry Standard issued the “Requirements for Design of Cigarette Package (卷煙包裝設計要求) YC/T 273–2014” which encouraged cigarette manufacturers to use environmentally friendly cigarette packaging materials. The more stringent requirements for cigarette packages have resulted in an increase in demand for quality cigarette packaging materials with eco-friendliness features.	We had continuously enhanced the eco-friendliness of our products through research and development. While this may potentially increase our operation costs, our capability in developing products which fulfil the evolving requirements of our customers can be strengthened.
Human capital development	Human capital development could lead to a stronger employee base and a lower turnover rate.	Our Group strives to maintain good relationship with our employees by (i) establishing direct communication channels between our employees and our senior management team; and (ii) organising regular social activities and trainings for our employees to enhance their sense of belonging and job satisfaction.
Business ethics and corporate governance	Regulatory risks in failing to maintain virtuous business ethics and corporate governance may result in compliance issues, while outstanding performance may help us yield a positive reputation.	Our Directors will constantly evaluate our corporate governance measures and business ethics, including ownership, control, diversity, remuneration and transparency.

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Corporate governance matters

Our Company will comply with the Corporate Governance Code as set out in Appendix 14 to the Listing Rules. We have established procedures for developing and maintaining internal control systems covering areas such as corporate governance, operations management, compliance matters, financial reporting, as appropriate for our business operations. We believe that our internal control systems and current procedures are sufficient in terms of comprehensiveness, practicability and effectiveness. In particular, we have adopted the following internal control measures to enhance our corporate governance:

- (i) our Board includes three independent non-executive Directors, whose backgrounds and profiles are set out in the section headed “Directors and senior management” in this document, to ensure transparency in management and fairness in business decisions and operations. Our independent non-executive Directors contribute to the enhancement of corporate value by providing advice and oversight based on their extensive administrative experience and specialised knowledge;
- (ii) our Directors will review and provide recommendation on our risk management related policies and procedures, and review the effectiveness and adequacy of our risk management activities annually;
- (iii) we have established three board committees, namely, the Audit Committee, the Nomination Committee and the Remuneration Committee, with respective terms of reference in compliance with the Corporate Governance Code. For details, please refer to the paragraph headed “Directors and senior management — Board committees” in this document;
- (iv) we have strengthened our internal audit system to ensure the appropriate functioning of the risk management and operation oversight systems. We have established the Audit Committee which comprises three independent non-executive Directors to review and monitor the effectiveness of our financial controls, internal control and risk management systems. Our internal control system will be reviewed by our internal audit personnel or independent internal control consultant on an annual basis to ensure that effective internal control procedures are in place;
- (v) our Directors have attended a training session on 6 July 2021 conducted by our legal advisers as to Hong Kong law on, among others, the obligations, on-going corporate governance requirements and the duties of directors of a company [REDACTED] on the Stock Exchange;
- (vi) our company secretary, Mr. Yu Tsz Ngo, will attend external professional training each year to keep himself abreast of the latest accounting and/or regulatory regime in Hong Kong;
- (vii) we have appointed Grande Capital as our compliance adviser to advise us on compliance matters in relation to the Listing Rules;

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- (viii) to avoid potential conflicts of interest, we will implement corporate governance measures as set out in the paragraph headed “Relationship with our Controlling Shareholders — Non-competition undertakings — 3. Corporate governance measures” in this document; and
- (ix) our Directors will review our corporate governance measures and our compliance with the Corporate Governance Code each financial year and comply with the “comply or explain” principle in our corporate governance reports to be included in our annual reports after [REDACTED].

IMPACT OF THE OUTBREAK OF COVID-19 ON OUR OPERATIONS

There was an outbreak of COVID-19 in the PRC in early 2020. The PRC Government imposed a lockdown in Huanggang, Hubei Province from 23 January 2020 to 25 March 2020 (the “**Lockdown Period**”). Transport was severely restricted, public transits, airports and major highways were closed and all non-essential companies, including manufacturing companies like our Group, was ordered to suspend operations during the Lockdown Period.

In response to the requirements of the local government authorities, our business operations were suspended during the Lockdown Period. Our Group has resumed business operation in full scale since late-March 2020 and our Group had not experienced any material operational disruption thereafter due to the outbreak of COVID-19. Based on publicly available information, there has been an increase in the number of COVID-19 cases in various areas of the PRC during the period from March to early-May 2022, including in particular the Shanghai Municipality (the “**Recent PRC Outbreak**”). The Recent PRC Outbreak has been largely contained by late-May 2022 and Shanghai has lifted COVID-19 lockdown restrictions since 1 June 2022. Our Directors consider that the Recent PRC Outbreak has not resulted in material adverse impact on our business and financial performance up to the Latest Practicable Date because: (i) the COVID-19 lockdown restrictions in Shanghai have been lifted since 1 June 2022; (ii) except for a customer based in Shanghai which has temporarily suspended placing purchase orders with us during the Recent PRC Outbreak, our Group did not experience any significant reduction in purchase orders from other customers up to the Latest Practicable Date; (iii) such customer based in Shanghai was not one of our top five customers during the Track Record Period and it accounted for approximately 4.7% of our Group’s total revenue for FY2021, and our Directors believe that, based on our past experience, reductions in purchase orders from customers due to COVID-19 outbreaks would normally be only temporary and demands for our products from affected customers would generally resume eventually along with the containment of the outbreak in the region; (iv) up to the Latest Practicable Date, there has been no material impact on the supply of raw materials to us as a result of the Recent PRC Outbreak, as none of our suppliers has informed us of any material impact on their operations; and (v) up to the Latest Practicable Date, there has been no material impact on the operation of our Group’s production facilities, as Hubei Province has not experienced any major outbreak of COVID-19 recently despite the Recent PRC Outbreak. Our Directors further confirmed that none of our employees had been tested positive for COVID-19 as at the Latest Practicable Date.

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Precautionary measures in response to the outbreak of COVID-19

To prevent any outbreak of COVID-19 in our production facility, we have established an epidemic prevention and control working group, which is led by our executive Directors, to undertake various precautionary measures such as:

- maintaining environmental hygiene and cleanliness of our production facility through regular cleaning and sanitisation;
- requiring all of our employees to undergo mandatory temperature checks before entering our production facility and those who have fever or upper respiratory tract infection symptoms shall be refrained from working and seek medical advice promptly;
- requesting our employees to wear masks at all time during work and report to us promptly whenever they feel unwell;
- maintaining social distancing at our production facility and designating officers to assist in and oversee the implementation of our hygiene and social distancing measures;
- monitoring the stock of personal protection equipment (including but not limited to surgical masks and hand sanitisers) for our employees;
- placing health education materials on COVID-19 at prominent areas of our production facility; and
- if any of our staff members is requested by government authorities to be quarantined or have been confirmed to have contracted COVID-19, their respective department will be informed and requested to keep on record. The affected staff member (the “**Affected Personnel**”) will be refrained from working immediately and any other staff who has close contact with the Affected Personnel shall also be quarantined.

Impact of the outbreak of COVID-19 on our business and financial performance

Our Directors believe that, based on information up to the Latest Practicable Date, the outbreak of COVID-19 would not have material impact on our business and financial performance in the long-run due to, among others, the following:

- save for the Lockdown Period and the temporary reduction in purchase orders from our customer located in Shanghai Municipality due to the Recent PRC Outbreak, we had not experienced any significant reduction in incoming enquiries or tender invitations nor any material reduction in purchase orders. Our Directors consider that the reduction in purchase orders placed by customer located in Shanghai Municipality did not result in material adverse impact on our business and financial performance taking into consideration (i) the COVID-19 lockdown restrictions in Shanghai have been lifted since 1 June 2022; (ii) based on our past experience, our Directors believe that the reduction in purchase orders from our Shanghai customer is only temporary due to the lockdown measures imposed by the Shanghai government and demand for our products from our Shanghai customer will gradually resume along with the containment of the

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outbreak of COVID-19 in the region; and (iii) save for our customer located in Shanghai Municipality, our Group did not experience any significant reduction in purchase orders from our other customers up to the Latest Practicable Date;

- in response to the requirements of the local government authorities, our business operations were fully suspended during the Lockdown Period. As a result of the complete suspension of all our sales and production activities, we did not generate any revenue or make any purchase of raw materials during the Lockdown Period. Meanwhile, our Group still had to incur certain costs such as staff costs, depreciation expenses and utility costs during the Lockdown Period. Our Group has resumed business operation since late-March 2020 and our Group had not experienced any material operational disruption thereafter due to the outbreak of COVID-19;
- notwithstanding our Group experienced temporary suspension of business during the Lockdown Period, our revenue increased slightly by approximately 1.8% from approximately RMB312.8 million for FY2019 to approximately RMB318.3 million for FY2020 and our gross profit margin remained relatively stable at approximately 21.0% and 22.0%, for FY2019 and FY2020, respectively. Further, our Group experienced an increase in our revenue by approximately 16.3% to approximately RMB370.3 million for FY2021;
- As a result of the complete suspension of our business operations during the Lockdown Period, our Group had delayed product delivery for certain purchase orders received prior to the Lockdown Period. In respect of these purchase orders, our Group had completed product delivery by April 2020. We did not incur any penalties or damages as a result of delay in our product delivery due to the outbreak of COVID-19 up to the Latest Practicable Date;
- we did not experience any cancellation of purchase orders or termination of framework sales agreement due to the outbreak of COVID-19 as at the Latest Practicable Date;
- our Group experienced temporary disruption to our supply of raw materials during the Lockdown Period when major transportation facilities were closed. Some of our suppliers were also required to suspend their business operations temporarily as a result of lockdown restrictions imposed by local government authorities. Our Directors consider that the temporary disruption to our supply of raw materials did not result in long-term adverse impact on our production taking into consideration (i) our Group had maintained inventory of raw materials to fulfil our production needs; and (ii) our major raw materials are primarily white cardboard and film, which are produced and readily available from suppliers in various regions of the PRC, and we are generally able to source alternative supplies if any of our current suppliers are affected by disruption caused by the outbreak of COVID-19. Save for the Lockdown Period, our Group did not experience any material shortage or delay in the supply of raw materials during the Track Record Period and up to the Latest Practicable Date;
- none of our employees had been tested positive for COVID-19;

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- according to the Industry Report, the outbreak of COVID-19 is expected to have limited impact on the demand for PRC cigarette packaging paper manufacturing industry in the long run due to the fact that the disruption of the outbreak of COVID-19 was temporary and the production for cigarette packaging paper in the PRC as well as in Hubei have resumed normal business. According to the Industry Report, the sales value of the cigarette packaging paper manufacturing industry in the PRC was affected by the outbreak of COVID-19 in 2020 and only recorded a year-on-year growth of approximately 1.7% from 2019 to 2020. Along with the resumption of normal production and business activities, the sales value of the cigarette packaging paper manufacturing industry in the PRC recorded a year-on-year growth of approximately 5.8% from 2020 to 2021; For further details, please refer to the paragraph headed “Industry overview — Impact of COVID-19 on the cigarette packaging paper manufacturing industry in the PRC and Hubei” in this document;
- based on information publicly available and reasonable enquiries by our Directors, we are not aware of any suggestion or indication that our major customers suffered from material financial difficulties as a result of the outbreak of COVID-19; and
- in the event that the outbreak of COVID-19 deteriorates and in the worst case scenario where our business operation has to be completely suspended, our Directors believe that we will have sufficient working capital to meet our cash requirements for at least 12 months based on our cashflow analysis, in particular taking into consideration factors and business assumptions such as (i) our cash and cash equivalent as at 30 April 2022; (ii) our customers will settle our trade receivables as at 30 April 2022 based on historical settlement pattern; (iii) we will settle our trade and bills payable as at 30 April 2022 based on historical settlement pattern; (iv) our restricted cash will be released upon the expiry date of the respective bank acceptance bills issued by us; (v) we will continue paying our staff at the minimum wage level permissible under the relevant PRC laws and regulations during the period of suspension of work; (vi) we will continue paying interest on our bank borrowings; and (vii) approximately RMB[REDACTED] million, representing approximately [REDACTED]% of our estimated net [REDACTED] from the [REDACTED], will be reserved as general working capital.

INSURANCE

In addition to the government-mandated social insurance and housing provident fund as detailed in the paragraph headed “Employees — Social insurance and housing provident funds contributions”, we also maintain property insurance which covers loss and theft of, and damage to, property, plant and machinery, and inventory in our production facility and warehouse. We believe that our insurance coverage is adequate and is in line with industry practice. During the Track Record Period and as at the Latest Practicable Date, as confirmed by our Directors, we had not made and did not make or had not been subject to any material insurance claims.

Based on the assessment of the risk exposure of our operations, our Directors are of the view that our insurance coverage is adequate and in line with industry practice. Certain risks disclosed in the section headed “Risk factors” in this document, such as risks in relation to our ability to obtain new contracts, our ability to retain and attract personnel, credit risk, inventory

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obsolescence, rising labour and raw materials costs are generally not covered by insurance because they are either uninsurable or it is not cost justifiable to insure against such risks. Please refer to the paragraph headed “Risk management and internal control systems” below in this section for further details regarding how our Group manages certain uninsured risks.

INTELLECTUAL PROPERTY

As at the Latest Practicable Date, our Group had registered a domain name and 24 patents which are, in the opinion of our Directors, material to our business. For further information, please refer to the paragraphs headed “Research and development” in this section and “Statutory and general information — B. Further information about the business of our Group — 2. Intellectual property rights” in Appendix IV to this document.

As at the Latest Practicable Date, we were not aware of any material infringement of any intellectual property rights of our Group which had an adverse effect on our business nor were we aware of any pending or threatened litigation or legal proceedings against us relating to the infringement of any intellectual property rights owned by third parties.

PROPERTIES

As at the Latest Practicable Date, we owned a parcel of land in Hong’an County, Huanggang, Hubei Province, the PRC with an aggregate site area of approximately 35,243 sq.m. for our production facility, on which buildings with an aggregate gross floor area of approximately 12,000 sq.m. were erected. The table below sets forth the information regarding our owned properties as at the Latest Practicable Date:

Type of property	Address	Approximate gross floor area (sq.m.)	Major usage	Description
Land	6 Zhu Shengtang Road, Hong’an New Industry Park, Hong’an County, Huanggang, Hubei Province, PRC	35,243	Industrial use	A parcel of land with a site area of approximately 35,243 sq.m.
Buildings	6 Zhu Shengtang Road, Hong’an New Industry Park, Hong’an County, Huanggang, Hubei Province, PRC	12,000	Five factory buildings, one staff dormitory and one multi-purpose building	Buildings built on the parcel of land at Hong’an County, Huanggang, Hubei Province, the PRC with an aggregate gross floor area of approximately 12,000 sq.m.

Based on the advice of our PRC Legal Advisers, save as disclosed in the paragraph headed “Legal compliance” in this section, we had obtained the necessary title documents in respect of the aforementioned land and buildings.

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As at 31 December 2021, our Group had no single property with a carrying amount of 15% or more of our Group’s total assets. On this basis, our Group is not required by Rule 5.01A of the Listing Rules to include any valuation report in this document. Pursuant to section 6(2) of the Companies (Exemption of Companies and Prospectuses from Compliance with Provisions) Notice (Chapter 32L of the Laws of Hong Kong), this document is exempted from compliance with section 342(1)(b) of the Companies (WUMP) Ordinance in relation to paragraph 34(2) of the Third Schedule to the Companies (WUMP) Ordinance in respect of the requirements for a valuation report with respect to interests in land or buildings.

LICENCE AND PERMIT

Our principal operating subsidiary, Hubei Qiangda, possessed the following permit as at the Latest Practicable Date:

Permit	Issuing authority	Expiry date
Pollutant discharge permit* (排污許可證)	Hong’an branch of Huanggang Ecology and Environment Bureau* (黃岡市生態環境局紅安縣分局)	20 May 2023

As advised by our PRC Legal Advisers, we had obtained all material licences, permits and approvals required for our business operation in the PRC during the Track Record Period and up to the Latest Practicable Date.

LEGAL COMPLIANCE

We strive to foster a strong compliance culture among our Group. Our Group has established a regulatory compliance manual governing, amongst others, (i) the roles and responsibilities of personnel involved in monitoring our Group’s regulatory compliance; (ii) guidelines with reference to the relevant rules and regulations; (iii) types, frequency and timing of key documents to be filed or reported to regulatory authorities (if any); (iv) review and approval process; and (v) managing and responding to non-compliance and litigation issues. Depending on their roles and responsibilities, our employees are required to follow the requirements in our regulatory compliance manual. If any deviation from our regulatory compliance manual is identified, our senior management team will investigate the causes and take appropriate rectification measures.

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Non-compliance incidents

Save as disclosed below, our Directors confirm that during the Track Record Period and up to the Latest Practicable Date, there was no non-compliance incident of our Group which is material or systemic in nature:

Non-compliance incidents	Reason for non-compliance	Legal consequences including potential maximum penalty and other financial liabilities	Latest status, remedial actions and measures
<p>Failure to apply for the relevant construction permits before construction and obtain real estate certificates for five properties.</p> <p>During the Track Record Period, Hubei Qiangda occupied five properties (the "Defective Properties"), for which Hubei Qiangda failed to apply for construction land planning permit (《建設用地規劃許可證》), construction project planning permit (《建設工程規劃許可證》) and construction project commencement permit (《建設工程施工許可證》) prior to the commencement of construction according to the Urban and Rural Planning Law of the PRC (《中華人民共和國城鄉規劃法》) (the "Urban and Rural Planning Law"), the Construction Law of the PRC (《中華人民共和國建築法》) (the "Construction Law"), the Measures for Construction Permission Management of Construction Projects (《建築工程施工許可管理辦法》), and other relevant laws and regulations. As at the Latest Practicable Date, Hubei Qiangda did not obtain real estate certificates for the Defective Properties pursuant to the Civil Code of the PRC (the "Civil Code").</p> <p>The Defective Properties are currently used by us as security office, business office, reception room, solvent storage room and carpentry workshop separately, with a total aggregate floor area of approximately 483.84 sq.m.</p>	<p>The non-compliance was primarily due to our staff's lack of professional knowledge of the relevant laws and regulations.</p>	<p>Pursuant to Article 209 of the Civil Code, the establishment, alteration, transfer and elimination of the real estate right shall take effect after registration; without registration, it shall not take effect, except as otherwise provided. Therefore, the possession, use, lease, mortgage and transfer of Defective Properties may not be recognised and protected under the Civil Code and other relevant laws and regulations.</p> <p>According to the Urban and Rural Planning Law, the relevant authority may order Hubei Qiangda to demolish the Defective Properties within a prescribed time limit, confiscate the income from the Defective Properties and impose a fine of not more than 10% of the construction project cost of the Defective Properties for our failure to obtain the construction land planning permit and construction project planning permit prior to commencement of construction. Furthermore, in accordance with the Construction Law and the Measures for Construction Permission Management of Construction Projects, the relevant authority may order us to pay a fine of not more than 1% and less than 2% of the contractual cost for our failure to obtain construction project commencement permit prior to commencement of construction of the Defective Properties. The construction project cost of the Defective Properties is about RMB 918,000, so the maximum amount that Hubei Qiangda may be fined by the competent authorities is RMB 91,800.</p>	<p>We have obtained letters of confirmation dated 17 May 2021, 19 August 2021, 6 January 2022 and 8 June 2022 from Hong'an County Natural Resources and Planning Bureau (紅安縣自然資源和規劃局) and letters of confirmation dated 17 May 2021, 20 August 2021, 5 January 2022 and 8 June 2022 from Hong'an County Housing and Urban Rural Development Bureau (紅安縣住房和城鄉建設局) respectively, confirming that we had not been penalised for violating the laws and regulations relating to the construction of the Defective Properties.</p> <p>On 2 June 2021 and 9 July 2021, our PRC Legal Advisers have consulted Hong'an County Natural Resources and Planning Bureau and Hong'an County Housing and Urban Rural Development Bureau, which confirmed that (i) the authorities were fully aware of the production and operation situation of Hubei Qiangda and the Defective Properties; (ii) the construction of Defective Properties without the relevant construction permits was not a material violation of relevant laws and regulations; (iii) Hubei Qiangda will not be required to demolish the Defective Properties immediately or apply for the relevant real estate certificates of the Defective Properties immediately and Hubei Qiangda can continue to occupy and use the Defective Properties legally; (iv) the authorities will not impose a fine or any other form of administrative penalty on us. As advised by our PRC Legal Advisers, the aforementioned government authorities have the authorities and are competent to make the aforesaid confirmation.</p> <p>On 8 June 2021, Mr. Chen issued a letter of commitment, pursuant to which he undertook that if Hubei Qiangda is required to demolish the Defective Properties or apply for the real estate certificates of the Defective Properties, or bear any fine or loss due to the Defective Properties, he would make up the payment for Hubei Qiangda unconditionally and actively cooperate with the competent authorities to rectify the Defective Properties according to the requirements of the competent authorities.</p> <p>Our Directors confirmed that none of our key manufacturing processes has taken place in the Defective Properties and the Defective Properties were designated only for ancillary purposes including security office, business office, reception room, solvent storage room and carpentry workshop. Further, the Defective Properties represents a relatively insignificant portion of our production facility in terms of floor area. In the event that we are required to demolish the Defective Properties, our Directors confirm that it will unlikely result in any material disruption to our business operations.</p> <p>Based on the foregoing, our PRC Legal Advisers are of the view that (i) our failure to apply for relevant construction permits prior to commencement of construction of the Defective Properties and our failure to obtain the real estate certificates of the Defective Properties will not have a significant impact on our operations; (ii) risk of our production and operation income from the Defective Properties being confiscated is remote; and (iii) the risks of us being fined or being required to demolish the Defective Properties immediately or to apply for the real estate certificates of the Defective Properties immediately by the competent authorities are remote. Accordingly, our Directors are of the view that this non-compliance will not have a material adverse effect on our business operations or financial condition as a whole.</p>

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Furthermore, the table below sets forth the summaries of certain non-compliance incidents during the Track Record Period which our Directors believe that these non-compliance incidents, whether individually or collectively, are non-material in nature and will not have any material financial or operational impact on us:

Non-compliance incidents	Reason for non-compliance	Legal consequences including potential maximum penalty and other financial liabilities	Latest status, remedial actions and measures
<p>1. Failure to make adequate social insurance contributions for all employees.</p> <p>During the Track Record Period, Hubei Qiangda failed to make adequate social insurance contributions for all of its employees in accordance with provisions of the Social Insurance Law of the PRC (《中華人民共和國社會保險法》) (the "Social Insurance Law"). The social insurance contributions paid by Hubei Qiangda for its employees have reached the minimum amount required by the local government, but less than the amount calculated based on the actual salaries of the employees.</p> <p>For FY2019, FY2020 and FY2021, the outstanding amount of social insurance contributions was approximately RMB1.1 million, RMB0.5 million and RMB1.2 million, respectively.</p>	<p>The non-compliance was primary due to (i) we made the social insurance contributions based on the local minimum wages; and (ii) some of the Hubei Qiangda's employees preferred not to make social insurance contributions at the actual salary level or at all, in particular, certain employees have made the social insurance contribution in their hometown and did not want to make additional contribution.</p>	<p>Pursuant to Article 86 of the Social Insurance Law, if an employer fails to pay its social insurance contributions in accordance with the Social Insurance Law, the relevant authority may demand the employer to pay all outstanding social insurance contributions within a prescribed time limit.</p> <p>The employer may also be subject to a surcharge at a daily rate of 0.05% on the outstanding amount, accruing from when the social insurance contribution was due. If the employer fails to make such payment within the prescribed time limit, the relevant authority may impose a further fine of one to three times the outstanding amount.</p> <p>According to Article 20 of the Regulation on Labour Security Supervision (《勞動保障監察條例》), if the violation of labour security laws, regulations or rules has not been discovered by the labour security administrative department within 2 years, nor has it been reported or complained, labour security administrative department shall no longer investigate and deal with it. According to the Law of the PRC on Administrative Penalty (《中華人民共和國行政處罰法》), where an illegal act is not discovered within two years of its commission, administrative penalty shall no longer be imposed. Therefore, as advised by our PRC Legal Advisers, Hubei Qiangda might be demanded to pay the outstanding social insurance contributions for a period of two years prior to the Latest Practicable Date of approximately RMB2.3 million and a late payment fee of approximately RMB0.8 million within a prescribed time limit. If Hubei Qiangda fails to make such payment within the prescribed time limit, the relevant authority may impose a maximum fine of approximately RMB6.8 million.</p>	<p>We have obtained letters of confirmation dated 17 May 2021, 19 August 2021, 4 January 2022 and 8 June 2022 from Hong'an County Human Resource and Social Security Bureau (紅安縣人力資源及社會保障局) and letters of confirmation dated 17 May 2021, 19 August 2021, 5 January 2022 and 8 June 2022 from Hong'an County Medical Security Bureau (紅安縣醫療保障局) respectively, confirming that we had not been penalised for violating the laws and regulations for social insurance contributions.</p> <p>On 2 June 2021, our PRC Legal Advisers consulted Hong'an County Human Resource and Social Security Bureau and Hong'an County Medical Security Bureau, both of which confirmed that (i) the authorities were fully aware of the production and operation situation of Hubei Qiangda and the social insurance payment; (ii) it is common in Hong'an County for labor-intensive production enterprises like Hubei Qiangda failing to pay adequate social insurance contributions for all employees based on employees' actual salaries, and our past failure to make adequate social insurance contributions is not a material violation of laws; (iii) as of the date of the consultation, the authorities had not received any complaints or reports from any individual or other government department about the payment of social insurance contributions made by Hubei Qiangda, nor found any dispute between Hubei Qiangda and its employees on the payment of social insurance contributions; (iv) the authorities have never initiated and will not initiate any proceedings including requiring us to pay all outstanding social insurance contributions, imposition of surcharge or fine against us. As advised by our PRC Legal Advisers, the aforementioned government authorities have the authority and are competent to make the aforesaid confirmations.</p> <p>On 7 June 2021, Mr. Chen issued a letter of commitment, pursuant to which he undertook that if Hubei Qiangda is required to pay outstanding social insurance contributions or housing provident fund contributions for its employees, or bear any fine or loss due to Hubei Qiangda's failure to fully pay social insurance contributions or housing provident fund contributions for its employees, he would make up such payment for Hubei Qiangda unconditionally and undertake responsibilities on behalf of Hubei Qiangda.</p> <p>During the Track Record Period and up to the Latest Practicable Date, we (i) had not received any notification from Hong'an County Human Resource and Social Security Bureau and Hong'an County Medical Security Bureau requiring us to pay the outstanding social insurance contributions or imposing surcharge or fine against us; and (ii) were not aware of any complaint from its employees or dispute with its employees in respect of social insurance contributions.</p> <p>Based on the foregoing, our PRC Legal Advisers are of the view that the risk of our Group being required to pay outstanding social insurance contributions or being imposed surcharge penalties on us is remote.</p> <p>According to the applicable rules promulgated by Hong'an County Human Resource and Social Security Bureau and Hong'an County Medical Security Bureau, the adjustment time of payment basis of social insurance contribution is in July each year. Therefore, we plan to adjust the payment basis of social insurance contribution in July 2022.</p> <p>Based on the above, our Directors are of the view, and the Sponsor concurred, that this non-compliance will not have a material adverse effect on our business operations or financial condition as a whole and there is no need to make provision for such immaterial non-compliance.</p>

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Non-compliance incidents	Reason for non-compliance	Legal consequences including potential maximum penalty and other financial liabilities	Latest status, remedial actions and measures
<p>2. Failure to make adequate housing provident fund contributions for all employees</p> <p>During the Track Record Period, Hubei Qiangda failed to make adequate housing provident fund contributions for all of its employees in accordance with the Regulations Concerning the Administration of Housing Provident Fund (《住房公积金管理条例》). The housing provident fund contributions paid by Hubei Qiangda for its employees have reached the minimum amount required by the local government, but less than the amount calculated based on the actual salaries of the employees.</p> <p>For FY2019, FY2020 and FY2021, the outstanding amount of housing provident fund contributions was approximately RMB0.2 million, RMB0.2 million and RMB0.2 million, respectively.</p>	<p>The non-compliance was primary because (i) we made the housing provident fund contributions based on the local minimum; and (ii) some of Hubei Qiangda's employees preferred not to make housing provident fund contributions at the actual salary level or at all given that they had their own housing in Hong'an County or had made housing provident fund contributions in other cities of the PRC, and Hubei Qiangda has provided dormitory space as staff welfare for its employees.</p>	<p>Pursuant to Article 38 of the Regulations Concerning the Administration of Housing Provident Fund, if an employer fails to pay its housing provident fund contributions in accordance with the Regulations Concerning the Administration of Housing Provident Fund, the relevant authority has the power to order the employer to pay all outstanding housing provident fund contributions within a prescribed time limit. If the employer fails to make such payment within the prescribed time limit, an application of compulsory enforcement can be made to the People's Court of the PRC.</p> <p>Therefore, in respect of the outstanding housing provident fund contributions during the Track Record Period and up to the Latest Practicable Date, the maximum amount that Hubei Qiangda might be ordered to pay would be approximately RMB0.7 million.</p>	<p>We have obtained letters of confirmation dated 17 May 2021, 19 August 2021, 5 January 2022 and 8 June 2022 from Hong'an Office of Huanggang Housing Provident Fund Management Center (黄冈住房公积金管理中心红安办事处), confirming that we had not been penalised for violating the laws and regulations for housing provident fund contributions.</p> <p>On 2 June 2021, our PRC Legal Advisers consulted the Hong'an Office of Huanggang Housing Provident Fund Management Center, which confirmed that (i) the authority was fully aware of the production and operation situation of Hubei Qiangda and the housing provident fund contributions; (ii) it is common in Hong'an for labor-intensive production enterprises like Hubei Qiangda failing to pay adequate housing provident fund contributions based on employees' actual salaries for all employees, and our past failure to make adequate housing provident fund contributions is not a material violation of laws; (iii) as of the date of the consultation, the authority had not received any complaints or reports from any individual or other government department about the payment of housing provident fund contributions on Hubei Qiangda, nor found any dispute between Hubei Qiangda and its employees on the payment of housing provident fund contributions; (iv) the authority has never initiated and will not initiate compulsory enforcement to the court on us. As advised by our PRC Legal Advisers, the aforementioned government authority has the authority and is competent to make the aforesaid confirmation.</p> <p>On 7 June 2021, Mr. Chen issued a letter of commitment pursuant to which he undertook that if Hubei Qiangda is required to pay outstanding social insurance contributions or housing provident fund contributions for its employees, or bear any fine or loss due to Hubei Qiangda's failure to fully pay social insurance contributions or housing provident fund contributions for its employees, he would make up payment for Hubei Qiangda unconditionally and undertake responsibilities on behalf of Hubei Qiangda.</p> <p>During the Track Record Period and up to the Latest Practicable Date, we (i) had not received any notification from Hong'an Office of Huanggang Housing Provident Fund Management Center requiring us to pay the outstanding housing provident fund contributions or about initiation of any compulsory enforcement at the court against us in relation to housing provident fund contributions; and (ii) were not aware of any complaint from its employees or dispute with its employees in respect of housing provident fund contributions.</p> <p>Based on the foregoing, our PRC Legal Advisers are of the view that the risk of us being required to pay outstanding housing provident fund contributions in limited time or being subject to compulsory enforcement to court is remote.</p> <p>According to the applicable rules promulgated by Huanggang Housing Provident Fund Management Centre, the adjustment time of payment basis of housing provident contribution is in July each year. Therefore, we plan to adjust the payment basis of housing provident contribution in July 2022.</p> <p>Based on the above, our Directors are of the view, and the Sponsor concurred, that this non-compliance will not have a material adverse effect on our business operations or financial condition as a whole and there is no need to make provision for such non-compliance. Further, Hubei Qiangda has provided dormitory space as staff welfare to its employees.</p>

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Our Directors consider that the abovementioned non-compliance incidents would not affect the suitability for [REDACTED] of our Company under Rule 8.04 of the Listing Rules having considered: (i) the nature and reason for such non-compliance incidents; and (ii) such non-compliance incidents did not involve any fraudulent act or dishonesty on the part of our Directors and did not raise any question as to the integrity of our Directors.

The Sponsor, after considering the above, concurs with the view of our Directors that (i) the abovementioned non-compliance incidents would not affect the suitability for [REDACTED] of our Company under Rule 8.04 of the Listing Rules; and (ii) the non-compliance incidents would not give rise to the concerns on the ability of our Directors to oversee our Company's operation and the suitability of our Directors under Rules 3.08 and 3.09 of the Listing Rules.

LITIGATION AND CLAIMS

As at the Latest Practicable Date, we were not engaged in any litigation, arbitration or claim of material importance, and no litigation, arbitration or claim of material importance is known to our Directors to be pending or threatened by or against us, that would have a material adverse effect on our business, results of operations or financial condition.

RISK MANAGEMENT AND INTERNAL CONTROL SYSTEMS

Key risks relating to our business are set out in the section headed "Risk factors" in this document. The following sets out the key measures adopted by our Group under our risk management and internal control system for managing the more particular operational and financial risks relating to our business operation:

(i) Customer concentration risk

Please refer to the paragraph headed "Our customers — Customer concentration" above in this section.

(ii) Credit risk management

We are subject to risks in relation to the collectability of our trade receivables, details of which are summarised in the paragraph headed "Risk factors — We are subject to credit risk in relation to the collectability of our trade receivables from customers" in this document.

For the purpose of mitigating our exposure to credit risk, our marketing staff and finance staff are responsible for conducting individual credit evaluations on our customers on a regular basis. Prior to entering into framework sales agreement with new customers, our marketing staff would check on the background of the potential customer in order to assess their credibility.

Material overdue payments are closely monitored and evaluated on a case-by-case basis in order to deduce the appropriate follow-up actions having regard to our business relationship with our customer, its history of making payments, its financial position as well as the general economic environment. During the Track Record Period, our follow-up actions for recovering

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long-overdue payment included active communications and conducting follow up calls with the relevant customers. We also have an internal assessment system in place to assess the credit rating of our customers.

We generally grant our customers a credit term of 60 to 180 days from the date of billing. As at 31 December 2019, 2020 and 2021, we recorded trade receivables (net of allowance for impairment) of approximately RMB148.5 million, RMB142.4 million and RMB145.1 million, respectively. For FY2019, FY2020 and FY2021, our trade receivables turnover days were approximately 158.7 days, 166.8 days and 141.7 days, respectively. To ensure timely identification of doubtful or irrecoverable debts, our finance staff would report to our chief financial officer on the collection status and ageing analysis of outstanding payments on a regular basis. Trade receivables overdue will be reviewed by our chief financial officer and, if appropriate, provisions for impairment of trade receivables will be made accordingly.

(iii) Liquidity risk management

In order to manage our liquidity position, we have adopted the following measures:

- our chief financial officer is responsible for the overall monitoring of our current and expected liquidity requirements on a monthly basis to ensure that we maintain sufficient financial resources to meet our liquidity requirements;
- as a general policy, we maintain inventory of raw materials based on our estimated production needs to prevent excessive purchases; and
- we closely monitor our working capital to ensure that our financial obligations can be fulfilled when due, by, among other things, (i) ensuring healthy bank balances and cash for payment of our short-term working capital needs; (ii) performing monthly review of our trade receivables and ageing analysis; and (iii) performing monthly review of our trade payables and ageing analysis.

(iv) Quality control risk management

Please refer to the paragraph headed "Quality control" in this section.

(v) Regulatory risk management

We keep ourselves abreast of any changes in PRC Government policies, regulations, and licensing requirements in relation to our business operations, as well as the relevant environmental and safety requirements. We will ensure that any changes of the above are closely monitored and communicated to our senior management for proper implementation and compliance.