

12 January 2023

*To: The Independent Board Committee and  
the Independent Shareholders of  
Xinjiang Tianye Water Saving Irrigation System Company Limited*

Dear Sirs or Madams,

**DISCLOSEABLE TRANSACTION AND CONNECTED  
TRANSACTION IN RELATION TO ACQUISITION OF 51%  
EQUITY INTEREST IN SUBJECT COMPANY**

**INTRODUCTION**

We refer to our appointment as the independent financial adviser to the Independent Board Committee and the Independent Shareholders in respect of the terms of the Acquisition Agreement and the transactions contemplated thereunder, details of which are set out in the letter from the board (the “**Letter from the Board**”) contained in the circular of the Company dated 12 January 2023 (the “**Circular**”), of which this letter forms part. Capitalised terms used in this letter shall have the same meanings as defined in the Circular unless the context requires otherwise.

With reference to the announcements of the Company dated 25 November 2022 and 1 December 2022, on 25 November 2022, the Company (as the purchaser) and Tianhe Yida (as the vendor) entered into the Acquisition Agreement, pursuant to which the Company has conditionally agreed to purchase, and Tianhe Yida has conditionally agreed to sell, the Target Equity Interest at a consideration of RMB15,647,200.

As at the Latest Practicable Date, Tianhe Yida is a wholly-owned subsidiary of Tianye Group, the actual controller of the Company, which directly and indirectly holds a total of approximately 60.42% of the issued share capital of the Company, and therefore Tianhe Yida is a connected person (as defined in the Listing Rules) of the Company. Accordingly, the Acquisition constitutes a connected transaction of the Company under Chapter 14A of the Listing Rules.

Except for being appointed as independent financial adviser to the Company regarding the renewal of continuing connected transactions of the Company, which the circular has been despatched on 14 January 2021, we have not acted as an independent financial adviser and as not provided any other services to the Company during the past two years. As at the Latest Practicable Date, we were not aware of any relationships or interests between us and the Company or any other parties that could reasonably be regarded as hindrance to our independence as defined under Rule 13.84 of the Listing Rules to act as the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders in respect of the Acquisition. We are not associated with the Company, its subsidiaries, its associates or their respective substantial shareholders or associates or any other parties to the Acquisition, and accordingly, are eligible to give independent advice and recommendations on the Acquisition Agreement and the transactions contemplated thereunder. Apart from normal professional fees payable to us in connection with this appointment as the Independent Financial Adviser, no arrangement exists whereby we will receive any fees from the Company, its subsidiaries, its associates or their respective substantial shareholders or associates or any other parties that could reasonably be regarded as relevant to our independence.

#### **INDEPENDENT BOARD COMMITTEE**

An Independent Board Committee comprising all the independent non-executive Directors, namely Mr. Li Lianjun, Ms. Gu Li, Mr. Hung Ee Tek and Mr. He Xinlin, has been established to advise the Independent Shareholders in respect of the terms of the Acquisition Agreement and as to whether the Acquisition Agreement and the transactions contemplated thereunder are fair and reasonable and in the interests of the Company and the Shareholders as a whole, taking into account our recommendation.

As the Independent Financial Adviser, our role is to give independent opinions to the Independent Board Committee and the Independent Shareholders as to whether the Acquisition Agreement and the transactions contemplated thereunder are fair and reasonable so far as the Independent Shareholders are concerned, and in the interests of the Company and the Shareholders as a whole.

#### **BASIS OF OUR OPINION**

In formulating our opinion and recommendations, we have relied on the statements, information, opinions and representations relating to the operations, financial condition and prospects of the Group contained or referred to in this Circular and/or provided to us by the Company and the management of the Group. We have assumed that such information and any representation made to us were true, accurate and complete in all material respects as at the Latest Practicable Date and considered that the information we have received is sufficient for us to reach our advice and recommendation as set out in this letter and to justify our reliance on such information. The Directors jointly and severally accept full responsibility for the accuracy of the information contained in this Circular and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief, opinions expressed by them in this Circular have been arrived at after due and careful consideration and there are no other material facts not contained in this Circular, the

omission of which would make any such statement made by them that contained in this Circular misleading in all material respects. We have no reason to doubt the truth or accuracy of the information provided to us, or to believe that any material information has been omitted or withheld.

Our review and analyses were based upon, among others, the information provided by the Group including this Circular, the Asset Valuation Report prepared by the PRC Independent Valuer as set out in Appendix I to this Circular and certain published information from the public domain, including but not limited to, the annual report of the Company for the year ended 31 December 2021 (the “**Annual Report 2021**”) and the interim report of the Company for the six months ended 30 June 2022 (the “**Interim Report 2022**”). We have also discussed with the Directors and the management of the Group with respect to the terms of and the basis and assumptions adopted in the Asset Valuation Report and the reasons for and benefits of the Acquisition. We have not, however, for the purpose of this exercise, conducted any in-depth independent investigation into the businesses, affairs and financial positions of the Group nor have we carried out any independent verification of the information supplied.

## **PRINCIPAL FACTORS AND REASONS CONSIDERED**

In formulating our opinion and recommendation to the Independent Board Committee and the Independent Shareholders in respect of the Acquisition, we have taken into account the following principal factors and reasons:

### **1. Background and financial information of the Group**

#### *(a) Background of the Group*

The Company and its subsidiaries are principally engaged in the design, manufacturing and sales of drip tapes, PVC/PE pipelines and drip assemblies used in water saving irrigation systems, and is also engaged in the provision of installation services of water saving irrigation systems for its customers, as well as land circulation and engineering business, and strategic development of digital agriculture and agriculture service business.

Tianhe Yida is principally engaged in industrial investments, project investments, investment management and asset restructuring. As at the Latest Practicable Date, Tianhe Yida is wholly owned by Tianye Group, which are owned as to 90% and 10% of its registered capital by 新疆生產建設兵團第八師國資委 (Xinjiang Production and Construction Corps Eighth Division SASAC\*) and 新疆生產建設兵團國資委 (Xinjiang Production and Construction Corps SASAC\*), respectively.

As at the Latest Practicable Date, (i) Shihezi Baiyang is substantially owned by 新疆天築建工集團有限公司 (Xinjiang TianZhu Construction Group Co. LTD\*) (92%) and 石河子南山水泥廠 (Shihezi Nanshan Cement Factory\*) (8%); (ii) 新疆天築建工集團有限公司 (Xinjiang TianZhu Construction Group Co. LTD\*) is owned by 石河子國有資產經營(集團)有限公司 (Shihezi State-owned

Assets Management (Group) Co., Ltd.\*) (99.7%) and 新疆天築建工集團有限公司工會委員會 (Xinjiang Tianzhu Group Co., Ltd. Trade Union Committee\*) (0.3%); (iii) 石河子國有資產經營(集團)有限公司 (Shihezi State-owned Property Management (Group) Co. LTD\*) is owned by 新疆生產建設兵團第八師國資委 (Xinjiang Production and Construction Corps Eighth Division SASAC\*) (86.3%), 新疆生產建設兵團國有資產監督管理委員會 (State-owned Assets Supervision and Administration Commission of Xinjiang Production and Construction Corps\*) (8.8%) and 中國農發重點建設基金有限公司 (China Agricultural Development Key Construction Fund Co. LTD\*) (4.9%); (iv) 中國農發重點建設基金有限公司 (China Agricultural Development Key Construction Fund Co. LTD\*) is an indirect wholly owned subsidiary of the State Council of the PRC; and (v) 石河子南山水泥廠 (Shihezi Nanshan Cement Factory\*) is a wholly owned subsidiary of Tianye Group.

**(b) Financial information of the Group**

Set out below is a summary of the financial performance of the Group for the two financial years ended 31 December 2020 (“FY2020”) and 31 December 2021 (“FY2021”) respectively as extracted from the Annual Report 2021 and the six months ended 30 June 2021 (“HY2021”) and 30 June 2022 (“HY2022”) respectively as extracted from the Interim Report 2022:

	FY2020	FY2021	HY2021	HY2022
	<i>approximately</i>	<i>approximately</i>	<i>approximately</i>	<i>approximately</i>
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
	(audited)	(audited)	(unaudited)	(unaudited)
<b>Operating Income</b>				
(a) Drip tape and drip assemblies	168,462	50,938	35,918	27,211
(b) PVC/PE pipelines	343,484	285,668	135,945	105,772
(c) Provision of installation services	162,564	224,452	51,182	427,746
(d) Trading income	—	500,369	107,100	89,839
(e) Other operating income	32,048	50,191	53,950	22,583
<b>Total operating income</b>	<b>706,558</b>	<b>1,111,618</b>	<b>384,095</b>	<b>673,151</b>
<b>Profit/(Loss) from operations</b>	<b>(66)</b>	<b>(63,511)</b>	<b>175</b>	<b>(24,003)</b>
<b>Net profit/(loss) attributable to owners of the parent company</b>	<b>650</b>	<b>(66,836)</b>	<b>(127)</b>	<b>(24,514)</b>

*FY2020 vs FY2021*

As stated in the Annual Report 2021, the total operating income of the Group was approximately RMB1,111,618,000 for FY2021, representing an increase of approximately 57.32% from approximately RMB706,558,000 for FY2020. The increase in operating income was mainly attributable to recognition of the operating income of Urumuqi Hongrui Plastic Trade Limited following its acquisition by the Company in 2021.

The net loss attributable to owners of the parent company for FY2021 was approximately RMB66,836,000 while the net profit attributable to owners of the Group for FY2020 was approximately RMB650,000. The loss making for FY2021 was mainly due to (i) the increase of cost of sales of approximately RMB423,565,000, which mainly comprised direct material costs, direct labour and production overhead; and (ii) the assets impairment loss for FY2021 of approximately RMB47,820,000, which mainly consisted of inventory impairment loss, allowance for fixed assets and bad debt loss. Increase in provision for various impairment losses are attributable to (a) a greater increase in the amount of impairment loss on fixed assets is mainly due to the impairment adjusted by audit, as a result of the market contraction of the drip tape business in 2021, with the majority of fixed assets including drip tapes and drip assembles being idle and depreciated towards expiration, which cannot generate economic benefits to the Company; (b) credit impairment losses mainly due to the impairment adjusted by audit, as a result of failure to recover some accounts receivable overdue for a long period in 2021 as well as failure to recover the project payment on time due to postponement of the completion and acceptance of some projects; and (c) inventory impairment losses mainly due to provision for impairment losses adjusted by audit in that the existing inventory price is higher than the existing market price.

#### *HY2022 vs HY2021*

As stated in the Interim Report 2022, the total operating income of the Group was approximately RMB673,151,000 for HY2022, representing an increase of approximately 75.26% from approximately RMB384,095,000 for HY2021. The increase in the total operating income was mainly due to increase in operating income from engineering projects, including provision of installation services.

The Group recorded the unaudited net loss attributable to owners of the parent company of approximately RMB24,514,000 and RMB127,000 for HY2022 and HY2021 respectively. Such increase was mainly due to (i) greater volatility in the price of raw materials over the period and the decrease in gross profit from the principal business; (ii) the decrease in operating income from the Group's engineering projects in HY2022 as well as the decrease in profit from engineering projects stemmed from the higher product costs due to the impact of raw material prices; and (iii) the higher product costs caused by the lower production volume of the Group.

Taking into account that (i) the Acquisition is to further expand the business scale and market share of the engineering services of the Group; and (ii) the principal business of the Subject Company can support the Group's construction projects which will be further discussed under the paragraph headed "5. Reasons for and benefits of the Acquisition" of this letter below, we consider that the Acquisition is an expansion of the existing business of the Group and is in line with the Group's business strategy.

## 2. Background of the Subject Company

The Subject Company is a company legally established and subsisting with limited liability in China on 5 October 2017. As at the Latest Practicable Date, its registered capital and paid-in capital are both RMB25,000,000. Its business scope includes pre-mixed concrete and products; vehicle leasing; construction engineering equipment leasing; on-road general cargo transportation, special cargo transportation (tank-based container) (exclusive of hazardous chemicals, flammables and explosives). To the best of the Directors' knowledge, information and belief after making all reasonable enquiries, Tianhe Yida subscribed for the registered capital of RMB12,750,000 in the Subject Company on 31 December 2017, representing a shareholding percentage of 51%.

The Subject Company is a manufacturer specialized in concrete production with an annual output up to 300,000 cubic meters of concrete. Besides two leading specialized automatic "double-180" concrete production lines, the Subject Company has more than 22 concrete mixer trucks of various types and 7 concrete pump trucks of various models with advanced performance, which can meet the demand of concrete transportation for various construction projects, as well as ultra-distance and ultra-height projects.

The following major financial data is extracted from the audited financial information of the Subject Company for FY2020, FY2021 and HY2022 based on the latest financial information of the Subject Company available to the Company:

	FY2020 (RMB) (audited)	FY2021 (RMB) (audited)	HY2022 (RMB) (audited)
Net profit/(loss) before taxation	6,206,768.70	7,550,183.12	(1,672,621.69)
Net profit/(loss) after taxation	4,533,985.14	5,574,331.68	(1,406,128.59)

As at 30 June 2022, the audited total liabilities, audited total asset and net asset of the Subject Company were RMB31,416,005.76, RMB60,524,060.34 and RMB29,108,054.58, respectively.

We have enquired the management of the Company in respect of the loss making of the Subject Company for HY2022 and the management of the Company replied that due to the unique climate features in the Xinjiang region, the first half of 2022 was an off-season period for construction works, and construction sites commenced the construction work in May 2022, which led to comparatively low demand for commercial concrete. Following full commencement of construction works in the second half of 2022, the financial performance of the Subject Company will be improved. According to the Letter from the Board, as at 31 October 2022, the unaudited profit before tax of Subject Company amounted to RMB1,680,936.64, while the unaudited net profit was RMB1,071,490.94.

### **3. Principal terms of the Acquisition Agreement**

The principal terms of the Acquisition Agreement are set out as follows:

#### ***Date***

25 November 2022 (after trading hours)

#### ***Parties***

1. the Company (as the purchaser); and
2. Tianhe Yida (as the vendor)

#### ***Subject Matter***

In accordance with the terms and conditions of the Acquisition Agreement, the Company has conditionally agreed to purchase, and Tianhe Yida has conditionally agreed to sell, the Target Equity Interest.

#### ***Target Equity Interest***

51% equity interest in the Subject Company.

#### ***Consideration***

The consideration of the Target Equity Interest is RMB15,647,200.

The aforesaid consideration was determined after arm's length negotiations between the Company and Tianhe Yida with reference to the appraised market value of the 100% equity interest of RMB30,680,800 (of which the corresponding appraisal value of the Target Equity Interest was RMB15,647,200) in the Subject Company on the Valuation Benchmark Date, which was appraised by the PRC Independent Valuer using the asset-based valuation approach in the Asset Valuation Report.

The aforesaid consideration will be financed by the Company's internal resources.

### ***Payment Terms***

The consideration of the Target Equity Interest shall be paid by the Company in a lump sum by cash to such an account as designated by Tianhe Yida within fifteen working days from the date the Acquisition Agreement takes effect.

### ***Conditions Precedent***

The Acquisition Agreement shall take effect upon fulfilment of all of the following conditions:

1. The Acquisition Agreement has been duly executed and sealed by the Company and Tianhe Yida;
2. Shihezi Baiyang has waived the first right of refusal in respect of the Target Equity Interest;
3. The Acquisition Agreement and the transactions as contemplated thereunder has been approved by the Stock Exchange; and
4. The Company has been in compliance with the relevant requirements under the Listing Rules in respect of the Acquisition Agreement and the transactions as contemplated thereunder, including but not limited to reporting to the Stock Exchange, making announcements and obtaining Independent Shareholders' approval.

Upon satisfaction of the aforesaid conditions precedent, the Company and Tianhe Yida will complete the Acquisition on the Date of Completion, in which case Tianhe Yida shall actively cooperate and assist the Company in completing the filing and registration procedures, including but not limited to, industrial and business registration, and taxation registration.

As at the Latest Practicable Date, the first conditions precedent has been fulfilled, and in respect of the second conditions precedent, Shihezi Baiyang has waived the first right of refusal regarding the Target Equity Interest.

### ***Transitional Period Arrangement***

Prior to the Date of Completion, Tianhe Yida continues to be the shareholder of the Subject Company, who is entitled to the relevant shareholder's rights and assumes the corresponding shareholder's obligations. Upon the Date of Completion, the Company shall be entitled to the relevant shareholder's rights and assume the corresponding shareholder's obligations as the shareholder of the Subject Company. In other words, during the Transitional Period, Tianhe Yida shall be responsible for the profit or loss of the Subject Company in proportion to its shareholding percentage.



### *Termination*

In accordance with the Acquisition Agreement, the Acquisition Agreement will forthwith be terminated or canceled in any of the following conditions:

- (1) Force majeure results in a delay in the performance or failure to perform the Acquisition Agreement;
- (2) The Company and Tianhe Yida have agreed to cancel the Acquisition Agreement upon negotiations; and
- (3) Without prejudice to other terms and conditions of the Acquisition Agreement, prior to Completion of the Target Equity Interest, the Company or Tianhe Yida is in possession of sufficient evidence to prove that the opposing party has given any untruthful or misleading statement, guarantee, and undertaking under, or failed to perform, the Acquisition Agreement, the non-defaulting party shall be entitled to terminate the Acquisition Agreement by serving a written notice to the defaulting party, who shall unconditionally agree to such termination.

### *Basis of Determination of the Consideration*

The consideration was determined after arm's length negotiations between the Company and Tianhe Yida with reference to the corresponding appraised market value of the Subject Company on the Valuation Benchmark Date, which was appraised by the PRC Independent Valuer. The Board understands that the asset-based approach was finally adopted by the PRC Independent Valuer for the valuation of the Target Equity Interest. The PRC Independent Valuer has considered all commonly adopted valuation approaches in the market (namely market approach, income approach and asset-based approach) for the purpose of determining the valuation of the Target Equity Interest.

The market approach was not appropriate in the valuation, given that the principal business of the Subject Company is concrete production with an annual output up to 300,000 cubic meters of concrete. Hence, there were only a few comparable companies based on the selection criteria of listed comparable companies with sufficient public information. As a result, the comparability requirement cannot be met.

The income approach was also not appropriate in the valuation as the overall value of the Subject Company is reflected mainly from the perspective of net cash flow generated from the operating activities of the Subject Company in the future. Affected by certain restrictive measures of COVID-19, the production activities of the Subject Company have been greatly restricted in 2022, thereby resulting in great uncertainties in using income approach.

As such, the asset-based approach was considered to be the most appropriate valuation approach in the valuation, since under the asset-based approach, the appraised value of the Subject Company is determined based on the balance sheet of the Subject Company, which is more capable of showing the real value of the Subject Company. For details of the valuation methodology and valuation assumptions adopted by the PRC Independent Valuer in preparing the Asset Valuation Report, please refer to the paragraphs headed “VII. APPRAISAL METHODS” and “IX. APPRAISAL ASSUMPTIONS” of the Asset Valuation Report as set out in Appendix I to this Circular.

As the PRC Independent Valuer is required under applicable PRC laws and regulations to conduct the valuation of the Subject Company using at least two valuation approaches, apart from the asset-based approach, the PRC Independent Valuer also chose the income approach as an alternative valuation method despite that the asset-based approach was finally adopted. In addition, the Directors were aware that the use of income approach was only to meet relevant PRC regulatory requirements and solely for reference purpose. In light of the above, the Company was not involved in the preparation of Asset Valuation Report and/or the preparation of valuation assumptions based on the income approach in respect of the Subject Company. The Asset Valuation Report and the valuation assumptions based on the income approach in respect of the Subject Company were prepared by the PRC Independent Valuer based on applicable valuation standards and its professional judgment.

Having discussed with the PRC Independent Valuer the basis and rationale for different valuation approaches, and having considered the analysis of the PRC Independent Valuer in relation to the applicability of each appraisal method and approach and assumptions as explained above, the Board concurred with the PRC Independent Valuer’s analysis and adoption of the asset-based approach as the appropriate valuation methodology and considered that the valuation had fairly and reasonably reflected the market value of the Target Equity Interest.

As stated in paragraph headed “8. EXPERTS AND CONSENTS” in Appendix II to this Circular, the PRC Independent Valuer, CAREA Assets Appraisal Co., Ltd, is an independent certified PRC valuer with over 20 years of experience in PRC assets valuation. It holds valid PRC qualification certificates for asset valuation and securities and futures related business valuation. Based on the above and having considered that (i) the qualifications and experience of the PRC Independent Valuer in relation to the preparation of the Asset Valuation Report; (ii) the scope of work of the valuation of the Target Equity Interest; (iii) the asset-based approach adopted was an appropriate valuation methodology and the valuation had fairly and reasonably reflected the market value of the Target Equity Interest; and (iv) the assumptions made by the PRC Independent Valuer for the valuation are in line with industry practices, the Directors are of the view that the consideration for the Acquisition and the terms and conditions of the

Acquisition Agreement are on normal commercial terms and are fair and reasonable to the Company and in the interests of the Company and its Shareholders as a whole.

#### **4. Valuation of the Subject Company**

As disclosed in the Letter from the Board, the consideration for the Acquisition Agreement was determined after arm's length negotiations between the Company and Tianhe Yida with reference to the appraised market value of the 100% equity interest of RMB30,680,800 (of which the corresponding appraisal value of the Target Equity Interest was RMB15,647,200) in the Subject Company on the Valuation Benchmark Date, which was appraised by the PRC Independent Valuer using the asset-based valuation approach in the Asset Valuation Report.

For our due diligence purpose, we have reviewed and enquired into (i) the terms of engagement of the PRC Independent Valuer with the Company; (ii) the PRC Independent Valuer's background and qualification in relation to the preparation of the Asset Valuation Report; and (iii) the steps and due diligence measures taken by the PRC Independent Valuer for conducting the Asset Valuation Report. From the information provided by the PRC Independent Valuer and based on our discussion with them, we understand that the responsible officer of the PRC Independent Valuer for the valuation of the Subject Company has over 17 years of experience in valuation. Furthermore, the PRC Independent Valuer has provided a wide range of valuation services to numerous companies, including stated-owned enterprises, A-Share companies and Hong Kong-listed companies. In the past three years, the PRC Independent Valuer has provided 16 valuation services of business similar to the Subject Company in different provinces in the PRC. Therefore, we were satisfied with the PRC Independent Valuer's qualification for preparation of the Asset Valuation Report.

In assessing the fairness and reasonableness of the consideration of the Acquisition, we have reviewed the Asset Valuation Report and upon our further enquiry with the PRC Independent Valuer, we understood that, as the PRC Independent Valuer is required under applicable PRC laws and regulations to conduct the valuation of the Subject Company using at least two valuation approaches, the PRC Independent Valuer has adopted asset-based approach in arriving the appraised value of the Subject Company and selected income approach as an alternative approach to cross check the valuation after considering the following reasons as stated in the Asset Valuation Report:

##### ***(1) Asset-based approach***

The asset-based approach refers to an appraisal method where the values of assets and liabilities in the financial statement and identifiable off-balance sheet of an enterprise are individually appraised on the basis of the balance sheet of the appraised entity on the benchmark date. The PRC Independent Valuer considered that the Subject Company has a sound accounting and audit system as well as orderly management in place, and the quantity of assets subject to appraisal can

be determined based on financial information and construction data, and can be verified through on-site investigation. Therefore, the PRC Independent Valuer concluded that the asset-based approach can be adopted as primary valuation approach for the valuation of the Subject Company.

***(2) Income approach***

The income approach refers to a specific model where the expected income is capitalized or discounted to determine the value of the appraised subject. The cash flow discount model is where expected future net cash flow is discounted to determine the value of the appraised subject, which includes the discounted enterprise free cash flow model and the discounted equity free cash flow model. The PRC Independent Valuer considered that, based on the data in the audited accounting statement of the Subject Company, the future income of the Subject Company can be reasonably predicted and measurable by monetary value. Therefore, the PRC Independent Valuer concluded that the income approach can be adopted to cross check the valuation of the Subject Company.

***(3) Market approach***

The market approach refers to the appraisal method where the appraised subject is compared against comparable listed companies or comparable transactions to determine the value of appraised subject. According to the Asset Valuation Report, based on the publicly released market information, externally audited financial information and other relevant materials of listed companies available on [www.cnlist.com](http://www.cnlist.com) (中國上市公司網) and the website of iFinD Information (同花順資訊網站), it is concluded that there are a few comparable listed companies in terms of the date of establishment and listing, business scope, business scale, main products, business composition, operation indexes, operation mode, operation stage, financial data or the purpose, time, situation, price and other factors in their transaction cases to the Subject Company in the capital market of the PRC. The PRC Independent Valuer concluded that the limited sample size of the comparable companies could not reach a meaningful valuation for the Subject Company. Therefore, the market approach was not adopted.

We have also reviewed the appraisal assumptions in the Asset Valuation Report as set out in Appendix I to this Circular and confirm that the assumptions are fair and reasonable and appropriate for valuation of the Subject Company.

We have inquired the PRC Independent Valuer on the applicability of the abovementioned assumptions and we understand that such assumptions are generally and consistently adopted in other business valuation exercises and are in line with the market practices. We are therefore of the view that the assumptions adopted in the valuation are reasonable. During the course of our discussion with PRC Independent Valuer, we have not identified any major factors which would lead us to cast doubt on the fairness and reasonableness of the valuation methodology and the principal basis and assumptions adopted in arriving at the appraised value of the Subject Company.

As advised by the PRC Independent Valuer, asset-based approach relates to the valuation of assets and liabilities of the Subject Company as at 30 June 2022, which includes current assets, non-current assets, current liabilities and non-current liabilities. Details of which are set forth below:

*(a) Current assets*

As at 30 June 2022, the current assets of the Subject Company amounted to approximately RMB50.95 million, comprising bank and cash balances of approximately RMB60,000, trade receivables of approximately RMB24.45 million, other receivables of approximately RMB24.42 million and inventories of approximately RMB2.02 million. In view of the nature and liquidity of current assets, the PRC Independent Valuer considered that market value adjustment to the current assets was not necessary. Accordingly, in appraising the market value of the current assets of the Subject Company, the PRC Independent Valuer has based on its audited book value as at 30 June 2022.

*(b) Non-current assets*

As at 30 June 2022, the non-current assets of the Subject Company amounted to approximately RMB9.58 million, which majority were property, plant and equipment of approximately RMB8.97 million. Other non-current assets included construction-in-progress, deferred and prepaid expenses and deferred tax assets.

Property, plant and equipment of the Subject Company comprised 18 machineries (including mixing plant equipment, loaders and monitor of flow of cement mortar), 24 vehicles (including concrete pump trucks, pickup trucks and heavy tank trucks), 7 electronic devices (including computers and printers) and other fixture and furniture. We understood that the PRC Independent Valuer has performed the following steps to evaluate the market value of the property, plant and machinery:

- (1) request the Company to provide detailed full list of property, plant and machinery;
- (2) collect information of ownership of the property rights;
- (3) perform on-site surveys and inspect the specifications, models, origins, maintenance status of plant and machinery;
- (4) determine the newness rate of each plant and machinery based on the above information; and
- (5) search for and compare with market price and cost of property, plant and machinery, if available.

As discussed with the PRC Independent Valuer, such appraisal method is a common methodology in establishing the valuation of fixed assets and complies with the relevant professional standard for valuation in the PRC.

The following table set out the breakdown of the value adjustment made by the PRC Independent Valuer to the property, plant and equipment:

	Net book value as at 30 June 2022 (RMB) (audited)	Value adjustment (RMB)	Appraised value of property, plant and equipment (RMB)
Machinery	3,875,988	111,857	3,987,845
Vehicles	5,037,992	1,442,389	6,480,381
Electronic devices and other fixture and furniture	<u>57,541</u>	<u>18,540</u>	<u>76,081</u>
<b>Total</b>	<b><u>8,971,521</u></b>	<b><u>1,572,786</u></b>	<b><u>10,544,307</u></b>

As shown in the above table, the appraised value of the property, plant and equipment increased by approximately RMB1.57 million. For the reason of the increase in appraised value of property, plant and equipment, we were advised by the PRC Independent Valuer that (i) the cost of replacement of machinery as at the Valuation Benchmark Date is higher than the net book value; and (ii) the newness rate was different from the depreciation rate. Details of the calculation and methodology of the newness rate are set out in the Asset Valuation Report in Appendix I to this Circular.

For other non-current assets, according to the Asset Valuation Report, as the book value of construction-in-progress represented only the initial land reclamation fee for early stage and the construction was not commenced, no value adjustment has been made to the construction-in-progress. The PRC Independent Valuer has also reviewed the documents of prepaid expenses and deferred tax and considered no value adjustment would be necessary.

*(c) Current and non-current liabilities*

According to the Asset Valuation Report, we note that the PRC Independent Valuer has reviewed and verified the contracts, invoices, tax computation, financial breakdown and other supporting documents and financial record in respect of the liabilities of the Group and the PRC Independent Valuer concluded that market value adjustment to the liabilities of the Subject Company was not necessary after performing their due diligence. Accordingly, in appraising the market value of the liabilities of the Subject Company, the PRC Independent Valuer has based on its audited book value as at 30 June 2022.

We note that the PRC Independent Valuer has conducted the valuation of the Subject Company under the requirements of the applicable PRC laws and regulations, whereby the valuation report prepared using asset-based approach has been cross-checked by income approach. According to the Asset Valuation Report, the appraised equity interests of the Subject Company using asset-based approach and income approach are approximately RMB30.68 million and RMB21.65 million respectively. The difference of valuation results between the asset-based approach and the income approach is approximately RMB9.03 million or approximately 29.43% (representing the difference of the valuation results divided by the valuation result using asset-based approach). Based on the Asset Valuation Report and our discussion with the PRC Independent Valuer, the main reason for the aforesaid difference is that, due to the outbreak of the COVID-19 and various preventive measures implemented by the PRC government, the PRC Independent Valuer considered the valuation using income approach may be subject to limitations and uncertainties of the market condition, while the asset-based approach, which evaluated from the audited accounts of the Subject Company and reflected the value of an enterprise from the perspective of asset replacement, was relatively more representative. Therefore, the valuation using asset-based approach was adopted as the final valuation conclusion.

Based on our review of the Asset Valuation Report and discussion with the PRC Independent Valuer regarding, among others, the scope of work and experiences of the PRC Independent Valuer, the reasons and appropriateness of adopting the asset-based approach for the valuation of the Subject Company, the basis, assumptions and methodology adopted in the Asset Valuation Report, and the valuation work and adjustments performed by the PRC Independent Valuer, nothing has come to our attention that causes us to doubt the fairness and reasonableness of the preparation of the Asset Valuation Report. In the view of the above, we consider that the valuation performed by the PRC Independent Valuer as well as the basis, assumptions and methodology adopted in the Asset Valuation Report are appropriate.

## **5. Reasons for and benefits of the Acquisition**

Immediately following Completion of the Acquisition, the Subject Company will become a non-wholly owned subsidiary of the Company. The financial results of the Subject Company will be consolidated into the consolidated financial statements of the Company.

As stated in the Letter from the Board, the Subject Company is principally engaged in pre-mixed concrete production, construction engineering equipment, cargo transportation, and other business activities related to construction projects. With engineering construction-related experience and equipment, an excellent management team, an outstanding track record and convenient service conditions, the Subject Company is well positioned to provide a full range of engineering construction auxiliary services and work. Due to the unique climate features in the Xinjiang region, the first half of 2022 was an off-season period for construction works, and construction sites commenced the construction work in May 2022, which led to comparatively low demand for commercial concrete. As a result, the Subject Company recorded a minor

loss in the first half of 2022. Following full commencement of construction works in the second half of 2022, sales and profitability are improving (as at 31 October 2022, the unaudited profit before tax of Subject Company amounted to RMB1,680,936.64, while the unaudited net profit was RMB1,071,490.94). Pursuant to the terms and conditions of the Acquisition Agreement, Tianhe Yida will be responsible for the profit or loss of the Subject Company prior to the completion of the Acquisition in accordance with its shareholding proportion. On the other hand, in the ordinary course of business of the Company, the Company transacts with various construction project companies for its engineering business, including the Subject Company. The Subject Company has also provided various types of commercial concrete to Tianye Group's projects. The Board believe that, the Acquisition is in line with the Company's strategic planning of "product + engineering" by maintaining stable supplies of quality commercial concrete for the Company's construction projects, integrating upstream and downstream industry chains thereby expanding the Company's engineering business, which is conducive to safeguarding Shareholders' interests and achieve a win-win cooperation for both the Company and the Subject Company.

As the segment of construction projects is a primary orientation under the Company's development strategy, five subsidiaries of the Company are currently in possession of the third-grade qualifications for building construction, water conservancy and hydropower construction, and municipal construction which have the capabilities to engage in infrastructure construction for workshops, houses and water conservancy facilities, as they demonstrate their advantages and qualifications in project construction experiences, technologies, market position, personnel, and other areas. Centering on the strategic planning of "product + engineering" to fulfil its mission of higher quality, higher efficiency and sustainable development, the Company proposes the acquisition of 51% equity interest in the Subject Company held by Tianhe Yida, which aims to build a strong partnership with the Subject Company, share resources, and leverage their respective advantages and synergy, so as to further expand into the engineering market, strengthen the brand influence, expand the business scale and market share. As a result, the Company will continue to enhance operating capacity and profitability, which provides solid guarantee for the Company's rapid engineering business expansion, extends its industry chain, and shore up the weak links of its engineering segment, thereby transforming the Company from a simple engineering construction business into a construction service provider of engineering, procurement, and construction (EPC) turnkey projects integrated with related resources in the future.

To the best knowledge of the Company, Tianye Group will proceed with various key project constructions during the 14<sup>th</sup> Five-year Plan, and therefore the Group expects to participate in such infrastructure projects. To control and ensure that the Group's construction quality as compared to other market players, and to simultaneously safeguard the consistency in construction service by ensuring the supplies of quality concrete (in particular to minimise the volatility of market demands and supplies of commercial concrete), the Company proceeds with the Acquisition so that the close integration of the upstream and downstream sectors may be achieved and



the Group will be able to maintain a steady supply of commercial concrete. Eventually, the Group targets to become an advance player in the industry chain, with its engineering business and market size expanding continuously.

We have discussed with the management of the Company and the Company considers that the Subject Company possesses qualifications in road transportation of general cargo and specialized transportation of cargo (tank container) with an annual output up to 300,000 cubic meters of concrete. The Subject Company has equipped 18 leading production machineries and equipment, mainly including specialized automatic “double-180” concrete production lines, equipment in batching plants, sand flow meters, loaders, wheel loaders and other advanced equipment; and 24 concrete mixer trucks, mainly including heavy-duty special operation vehicles including concrete pump trucks, pickup trucks, and heavy-duty tank trucks. All of them have advanced performance and can meet the demand of concrete transportation for various construction projects with long distance and ultra-height construction. The Subject Company has a team of 62 personnel, including 7 management personnel and 55 construction personnel. The management team are professional technicians with high professional standard who have been engaged in the industry for more than 10 years, which provides solid guarantee for the performance of the Subject Company. The Subject Company has provided concrete and other related products and services in good quality to large scale construction projects, including the construction of 147 Corps Chemical Industrial Park\* (147團化工園區), which is invested by Tianye Group with an annual production capacity of 1 million tons of ethylene glycol (Phase 1 of which have an annual production capacity of 600,000 tons) and was completed in 2019. Furthermore, the revenue of the Subject Company for the year ended 31 December 2020 and 2021 amounted to approximately RMB42.9 million and RMB45.3 million, respectively which was relatively stable. After considering and reviewing (i) the list of the production machineries and equipment and concrete mixer trucks; (ii) the resume of the management personnel of the Subject Company; (iii) the sale and cooperative agreements of the provision of concrete products and other related products and services by the Subject Company to 147 Corps Chemical Industrial Park, and (iv) the financial track record of the Subject Company, we concur with the Company’s view that the Subject Company has possessed engineering construction-related experience and equipment, an excellent management team, an outstanding track record and convenient service conditions as stated in the Letter from Board, and we consider that the well-established business of the Subject Company could provide immediate benefit of creating synergy to the Group after the Acquisition as compared with a newly established concrete business by the Group from scratch.

We note that the Company recently entered into the project construction services framework agreement (“**Framework Agreement**”) with Tianye Group, pursuant to which, Tianye Group agreed to purchase infrastructure construction services, including but not limited to project construction services and other services related to construction, works, maintenance, and safety rectification, from the Group. Therefore, we consider the Group’s construction business will continue to expand and develop and the Subject Company after the Acquisition could become one of the stable suppliers of quality pre-mixed concrete for the construction projects of the Group, including but not limited to the construction projects under the Framework Agreement, and also the Acquisition could share resources and leverage the respective advantages and synergy of the Group and Subject Company.

After considering that (i) the Acquisition was in line with the business strategy of expansion of construction and engineering segment; and (ii) the Subject Company could provide stable supply of pre-mixed concrete to the Group’s construction projects, we consider that the Acquisition is fair and reasonable investment to the Company and the Shareholders as a whole.

## **RECOMMENDATION**

Having considered the abovementioned principal factors and reasons, in particular, that (i) the principal terms of the Acquisition Agreement; (ii) the valuation of the Subject Company by the PRC Independent Valuer; and (iii) the reasons for and benefits of the Acquisition, we are of the view that although the Acquisition Agreement and the transactions contemplated thereunder are not in the ordinary and usual course of business of the Company, the terms are on normal commercial terms and fair and reasonable so far as the Company and the Independent Shareholders are concerned and in the interests of the Company and the Shareholders as a whole.

Accordingly, we advise the Independent Board Committee to recommend the Independent Shareholders to vote in favour of the resolution to approve the Acquisition Agreement and the transactions contemplated thereunder.

Yours faithfully,  
For and on behalf of  
**INCUBORPORATE FINANCE LIMITED**



**Gina Leung**  
*Managing Director*

*Ms. Gina Leung is a licensed person registered with the SFC and a responsible officer of INCUBORPORATE Finance Limited to carry out Type 6 (advising on corporate finance) regulated activity under the SFO. She has over 20 years of experience in the corporate finance industry and has participated in the provision of independent financial advisory services for various transactions involving companies listed in Hong Kong.*