Giraffe
智富

9 December 2024

To the Independent Board Committee and the Independent Shareholders

Dear Sirs,

(1) CONNECTED AND DISCLOSEABLE TRANSACTION: ACQUISITION OF ASSETS; AND (2) CONNECTED AND MAJOR TRANSACTION: PROVISION OF THE LOAN

INTRODUCTION

We refer to our appointment as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in respect of (i) the Second Assets Transfer Agreement and the transactions contemplated thereunder; and (ii) the Loan Agreement and the transactions contemplated thereunder, details of which are set out in the letter from the Board (the "**Letter from the Board**") of the circular issued by the Company dated 9 December 2024 (the "**Circular**"), of which this letter forms part. Capitalised terms used in this letter shall have the same meanings as those defined in the Circular unless the context otherwise requires.

On 1 November 2024 (after trading hours), the Company and Chuncheng Investment, a controlling shareholder of the Company, entered into the Second Assets Transfer Agreement, pursuant to which the Company has conditionally agreed to purchase, and Chuncheng Investment has conditionally agreed to sell, the Assets for the Consideration of RMB82,886,461.00 in accordance with the terms and conditions of the Second Assets Transfer Agreement. On 1 November 2024 (after trading hours), the Company, as lender, and Chuncheng Investment, a controlling shareholder of the Company, as borrower, entered into the Loan Agreement, pursuant to which the Company has agreed to advance the Loan in an amount of not more than RMB300 million to Chuncheng Investment in accordance with the terms and conditions of the Loan Agreement.

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As disclosed in the Letter from the Board, pursuant to Chapter 14A of the Listing Rules, the transactions contemplated under the First Assets Transfer Agreement and the Second Assets Transfer Agreement shall be aggregated because both agreements are entered into with Chuncheng Investment and both transactions involve the acquisition of assets which were used by Chuncheng Investment for heat production purposes. As one or more of the applicable percentage ratios as calculated under Rule 14.07 of the Listing Rules in respect of the Proposed Acquisition (on a standalone basis or when aggregated with the transactions contemplated under the First Assets Transfer Agreement) exceed(s) 5% but all of them are less than 25%, the Proposed Acquisition constitutes a discloseable transaction for the Company under Chapter 14 of the Listing Rules and is therefore subject to the reporting and announcement requirements thereunder.

Given that Chuncheng Investment is a controlling shareholder of the Company holding approximately 69.75% of the total share capital of the Company as at the date of the Second Assets Transfer Agreement, Chuncheng Investment is a connected person of the Company and the Proposed Acquisition constitutes a connected transaction for the Company under Chapter 14A of the Listing Rules. As one or more of the applicable percentage ratios as calculated under Rule 14.07 of the Listing Rules in respect of the Proposed Acquisition (on a standalone basis or when aggregated with the transactions contemplated under the First Assets Transfer Agreement) exceed(s) 5%, the Proposed Acquisition is subject to the reporting, announcement and independent shareholders' approval requirements under Chapter 14A of the Listing Rules.

As disclosed in the Letter from the Board, as the assets ratio (as defined in the Listing Rules) in respect of the Loan exceeded 8%, the Loan is subject to the announcement requirements under Rule 13.13 of the Listing Rules. As one of the applicable percentage ratios as calculated under Rule 14.07 of the Listing Rules in respect of the Loan exceeds 25%, the provision of the Loan constitutes a major transaction for the Company under Chapter 14 of the Listing Rules and is therefore subject to the reporting, announcement and shareholders' approval requirements thereunder.

Given that Chuncheng Investment is a controlling shareholder of the Company holding approximately 69.75% of the total share capital of the Company as at the date of the Loan Agreement, Chuncheng Investment is a connected person of the Company and the provision of the Loan constitutes a connected transaction for the Company under Chapter 14A of the Listing Rules. As more than one of the applicable percentage ratios as calculated under Rule 14.07 of the Listing Rules in respect of the Loan exceed 5%, the provision of the Loan is subject to the reporting, announcement and independent shareholders' approval requirements under Chapter 14A of the Listing Rules.

THE INDEPENDENT BOARD COMMITTEE

The independent committee of the Board, comprising all the independent non-executive Directors, namely Mr. Fu Yachen, Mr. Poon Pok Man and Ms. Zhang Yan, has been formed to advise the Independent Shareholders in relation to (i) the Second Assets Transfer Agreement and the transactions contemplated thereunder; and (ii) the Loan Agreement and the transactions contemplated thereunder. We have been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in the same regard.

OUR INDEPENDENCE

During the past two years immediately preceding and up to the date of our appointment as the Independent Financial Adviser, we have acted as the independent financial adviser to the independent board committee and independent shareholders of the Company in respect of the 2024–2026 heat procurement framework agreement (Chuncheng Investment), the 2024–2026 heat procurement framework agreement (Datang JV), the 2024–2026 construction framework agreement and the 2024–2026 pipes supply framework agreement as detailed in the circular of the Company dated 7 November 2023. Notwithstanding the above engagement, as at the Latest Practicable Date, we were independent from and not connected with the Group in accordance with Rule 13.84 of the Listing Rules, and accordingly, are qualified to act as the Independent Financial Adviser to the Independent Board Committee and Independent Shareholders considering that (i) our independent roles in the aforesaid engagement (the "**Previous Engagement**"); (ii) the aggregate professional fees paid/to be paid by the Company to us represent an insignificant portion of our revenue during the relevant period; and (iii) we have maintained our independence from the Company since the Previous Engagement, and our independence from the Company has not been compromised because of the Previous Engagement.

Besides, apart from the advisory fee and expenses payable to us in connection with our appointment as the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders, no arrangement exists whereby we shall receive any other fees or benefits from the Company.

BASIS OF OUR OPINION

In formulating our opinion and recommendation, we have reviewed, among others, (i) the announcement of the Company dated 1 November 2024 in relation to the Proposed Acquisition and provision of the Loan; (ii) the terms of the Second Assets Transfer Agreement and the Loan Agreement; (iii) the annual report of the Company for the year ended 31 December 2023 ("**FY2023**") (the "**2023 Annual Report**") and the interim report of the Company for the six months ended 30 June 2024 ("**6M2024**") (the "**2024 Interim Report**"); (iv) the information and facts supplied by the Group; (v) the opinions expressed by and the representations of the Directors and management of the Group (the "**Management**"); and (vi) certain relevant public information, and have assumed that all such information and facts provided and any opinions and representations made to us are true, accurate and complete in all material aspects at the time they were made and up to the date of the EGM.

We have relied on the statements, information, opinions and representations contained or referred to in the Circular and the information, opinions and representations provided to us by the Group and/or its Management and/or the Directors. We have assumed that all such statements, information, opinions and representations contained or referred to in the Circular and the information, opinions and representations provided to us by the Group and/or its Management and/or the Directors were true and accurate at the time when they are made and continue to be true up to the Latest Practicable Date. We have no reason to believe that any statements, information, opinions and representations relied on by us in forming our opinion is untrue, inaccurate or misleading, nor are we aware of any material facts the omission of which would render the information provided and the representations made to us untrue, inaccurate or misleading. We have not, however, conducted any independent verification and in-depth investigation into the information provided by the Company as well as the business and affairs of the Group, Chuncheng Investment Group, or their respective subsidiaries or associates (if applicable), nor have we considered the taxation implication on the Group or the Shareholders. Our opinion is necessarily based on the financial, economic, market, industry-specific and other conditions in effect and the information made available to us as at the Latest Practicable Date. Shareholders should note that subsequent developments (including any change in market and economic conditions) may affect and/or change our opinion and we have no obligation to update this opinion to take into account events occurring after the Latest Practicable Date or to update, revise or reaffirm our opinion. Nothing contained in this letter should be construed as a recommendation to hold, sell or buy any Shares or any other securities of the Company.

The Directors collectively and individually accept full responsibility, including particulars given in compliance with the Listing Rules for the purpose of giving information regarding the Group. The Directors, having made all reasonable enquiries and careful consideration, confirm that to the best of their knowledge and belief, the information contained in the Circular is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement herein or the Circular misleading. We, as the Independent Financial Adviser, take no responsibility for the contents of any part of the Circular, save and except for this letter of advice.

This letter is issued for the information of the Independent Board Committee and the Independent Shareholders solely in connection with their consideration of (i) the terms of the Second Assets Transfer Agreement and the transactions contemplated thereunder; and (ii) the terms of the Loan Agreement and the transactions contemplated thereunder, and, except for its inclusion in the Circular, is not to be quoted or referred to, in whole or in part, nor shall this letter be used for any other purposes, without our prior written consent.

PRINCIPAL FACTORS AND REASONS CONSIDERED

In arriving at our opinion and recommendation in respect of (i) the Second Assets Transfer Agreement and the transactions contemplated thereunder; and (ii) the Loan Agreement and the transactions contemplated thereunder, we have taken into consideration the following principal factors and reasons:

1. Information on the Group

1.1 *Business of the Group*

As disclosed in the Letter from the Board, the Company is a China-based company mainly engaged in heating service business. The Group operates its business through two segments, namely heat supply segment and construction, maintenance and design services segment. Heat supply segment mainly provides heat supply services within Jilin Province. Construction, maintenance and design services segment mainly provides maintenance related services such as engineering construction, engineering maintenance, design, electrical appliances and instrument maintenance. The Group mainly conducts its business in the Chinese domestic market.

According to the 2023 Annual Report, the Group has continued to increase investment in the informatisation and intelligentisation of heat supply. Since its establishment, it has continued to build a smart heat supply network system in a planned and phased manner. The current smart heat supply network system has achieved real-time monitoring, remote control, big data comprehensive analysis and other functions, and has been identified as the leading system in the heating industry by China District Heating Association (中國城鎮供熱協會). With heat supply as its core business, the Group has established long-term and stable cooperative relationships with a number of thermal power plants. Heat supply services are provided to around 550,000 residential and non-residential users in Changchun with cogeneration as the main heat supply mode. As at 31 December 2023, the heat service area of the Group was approximately 67.1 million sq.m., representing an increase of approximately 2.9% compared to approximately 65.2 million sq.m. as at 31 December 2022. According to the 2024 Interim Report, the heat service area of the Group further increased to approximately 67.4 million sq.m..

According to the 2023 Annual Report and the 2024 Interim Report, the Group's construction, maintenance, design and others cover the peripheral services business of the heat supply industry chain. The Group mainly provides services include engineering construction, engineering maintenance, design services and so on for heat supply companies or end-users. These services mainly cover northeast China.

1.2 *Financial performance of the Group*

Set out below is a summary of the Group's operating results as extracted from the 2023 Annual Report and 2024 Interim Report:

	For the year ended 31 December		**For the six months ended 30 June**	
	2022	**2023**	**2023**	**2024**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Revenue				
— Heat supply business	1,538,419	1,570,725	879,343	900,324
— Construction, maintenance and design services	116,286	123,692	19,011	6,305
	1,654,705	**1,694,417**	**898,354**	**906,629**
Gross profit	230,648	265,890	225,618	220,038
Gross profit margin	*13.9%*	*15.7%*	*25.1%*	*24.3%*
Net profit	**114,668**	**120,956**	**124,924**	**148,142**

For the years ended 31 December 2022 ("**FY2022**") and 2023 and for the six months ended 30 June 2023 and 2024, the Group generated revenue from two operating segments, being (i) heat supply services and (ii) construction, maintenance and design services. Revenue generated from heat supply segment includes fees for provision and distribution of heat, entrance fees charged for connections to the Group's heat distribution network and heat transmission fees charged to other heat service providers. Revenue generated from construction, maintenance and design services includes engineering construction, engineering maintenance, design services and electrical instrument maintenance and repair.

Comparison of financial performance between the year ended 31 December 2022 and 2023

Based on the 2023 Annual Report, the Group's revenue increased by approximately 2.4% from approximately RMB1,654.7 million in FY2022 to approximately RMB1,694.4 million in FY2023 mainly attributable to the increase in revenue generated from the heat supply business by RMB32.3 million as a result of the increase in heat service area from approximately 65.2 million sq.m. as at 31 December 2022 to approximately 67.1 million sq.m. as at 31 December 2023, representing an increase of approximately 2.9%.

The Group's gross profit increased by approximately 15.3% from approximately RMB230.6 million in FY2022 to approximately RMB265.9 million in FY2023, and the gross profit margin increased from approximately 13.9% in FY2022 to approximately 15.7% in FY2023, mainly attributable to (i) the increase in the revenue generated from heat supply business as mentioned above; (ii) the decrease in heat procurement costs primarily resulting from the decrease in total heat procurement from approximately 24.2 million GJ in FY2022 to approximately 23.0 million GJ in FY2023; and (iii) the decrease in costs of coal consumed in the heat supply business primarily resulting from the lower coal consumption as a result of the partial adoption of purchased heat sources by Jilin Province Xixing Energy Limited* (吉林省西興能源有限公司), a subsidiary of the Company, in FY2023.

The Group's net profit increased from approximately RMB114.7 million in FY2022 to approximately RMB121.0 million in FY2023, which was in line with the increase in gross profit contributed by the Group's heat supply business.

Comparison of financial performance between the six months ended 30 June 2023 and 2024

Based on the 2024 Interim Report, the Group's revenue remained relatively stable at approximately RMB898.4 million for the six months ended 30 June 2023 ("**6M2023**") and RMB906.6 million in 6M2024.

The Group's gross profit remained relatively stable at approximately RMB225.6 million in 6M2023 and approximately RMB220.0 million in 6M2024. The gross profit margin decreased from approximately 25.1% in 6M2023 to approximately 24.3% in 6M2024, mainly due to (i) increase in wages resulting from the increase in number of labor workers; and (ii) increase in utilities costs.

The Group's net profit increased by approximately 18.6% from approximately RMB124.9 million in 6M2023 to approximately RMB148.1 million in 6M2024 mainly due to (i) the decrease in credit impairment loss which was mainly attributable to the decrease in gross balance of trade receivables as at 30 June 2024 as compared to the balance as at 30 June 2023; and (ii) the reversal of impairment loss on assets of approximately RMB21.6 million in relation to contract assets recovered in 6M2024.

1.3 *Financial position of the Group*

Set out below is a summary of the Group's financial position as extracted from the 2023 Annual Report and 2024 Interim Report:

	As at 31 December 2022 *RMB'000*	As at 31 December 2023 *RMB'000*	As at 30 June 2024 *RMB'000*
Assets			
— Cash and cash equivalents	1,030,236	1,111,042	553,826
— Fixed assets	984,809	897,056	863,079
— Prepayments	587,425	560,281	176,197
Liabilities			
— Contract liabilities	1,410,923	1,381,514	467,567
Total equity	911,901	989,846	1,137,988
Gearing ratio *(Note 1)*	**N/A**	**N/A**	**N/A**

Notes:

1. Gearing ratio is the percentage of total interest-bearing liabilities (including interest-bearing bank and other borrowings and lease liabilities), net of cash and cash equivalents, to total equity at the end of each financial period.

2. For the avoidance of doubt, only selected major asset and liability components are disclosed in the table above.

According to the 2023 Annual Report, the Group's cash and cash equivalents increased by 7.8% from approximately RMB1,030.2 million as at 31 December 2022 to approximately RMB1,111.0 million as at 31 December 2023, which was the combined effect of (i) net cash inflow from operating activities of approximately RMB399.3 million in FY2023 mainly comprised cash received from sales of goods or rendering of services partially offset by cash paid for purchase of goods or receipts of services; and (ii) net cash outflow from investing activities and financing activities of RMB318.5 million in FY2023. According to the 2024 Interim Report, the Group's cash and cash equivalents decreased to RMB553.8 million as at 30 June 2024 mainly due to net cash outflow from operating activities for 6M2024 of approximately RMB495.5 million as heat fee was generally collected in the second half of the year before the commencement of the heat supply period.

The Group's fixed assets primarily comprised pipeline network and machinery and equipment. The decrease in the net book value of fixed assets was mainly attributable to the depreciation charged in respective years/periods.

The Group's prepayments mainly represented heat procurement costs paid to local cogeneration plants in advance before the commencement of heat supply period. As at 31 December 2023 and 2022, the Group's prepayments remained relatively stable at RMB560.3 million and RMB587.4 million respectively. As at 30 June 2024, the Group's prepayments decreased to RMB176.2 million mainly due to the decrease in prepaid heat procurement costs as the relevant costs were recognized as cost of sales during the period.

The Group's liabilities mainly derived from contract liabilities which represented the Group's obligation to provide goods to the customer for the consideration received or receivable. As at 31 December 2023 and 2022, the Group's contract liabilities remained relatively stable at RMB1.38 billion and RMB1.41 billion respectively. As at 30 June 2024, the Group's contract liabilities decreased to RMB467.6 million as the heat service fees, which were received from the customers before the commencement of heat supply period, were recognized as revenue during the period.

The equity attributable to owners of the Group increased from approximately RMB911.9 million as at 31 December 2022 to approximately RMB989.8 million as at 31 December 2023, and further to RMB1,138.0 million as at 30 June 2024, mainly attributable to the profit for FY2023 and 6M2024.

As at 30 June 2024, 31 December 2023 and 2022, the Group's borrowings amounted to RMB35.0 million, nil, and RMB234.0 million respectively. Since the Group's cash and cash equivalents exceeded the Group's total interest-bearing liabilities, the gearing ratio was not applicable as at 30 June 2024, 31 December 2023 and 2022.

1.4 *Business outlook*

According to the National Bureau of Statistics of China (the "**NBS**") and the Statistic Bureau of Jilin* (吉林省統計局), the urbanization rates of the PRC and Jilin Province increased from approximately 54.8% and 54.8% in 2014 to approximately 66.2% and 64.7% in 2023, respectively. The number of urban residents of Jilin Province reached approximately 15.1 million in 2023. The rising urbanization rates in the PRC and Jilin Province lead to increasing demand for heating service and related urban municipal infrastructure, which is the fundamental driver of the development of heat supply and related construction, maintenance and design industry.

Pursuant to the National 14th Five-Year Plan for Urban Infrastructure Construction* (《「十四五」全國城市基礎設施建設規劃》) published in 2022 by National Development and Reform Commission* (國家發展和改革委員會) and Ministry of Housing and Urban-Rural Development* (住房和城鄉建設部), the PRC government continued to improve the central heating capacity, the municipal infrastructure, and service area, and to reduce heat loss rate of heating pipe network. Further, the government proposed to strengthen the construction and transformation of clean heat sources and pipe networks, and develop new energy, renewable energy, and other low-carbon energy sources. These favorable policies are expected to stimulate the demand for the high-quality heating infrastructure and drive the growth of the heat supply industry. According to the China Statistical Yearbook compiled by NBS, the length of heating pipelines construction and area of centralised heating of Jilin Province of the PRC has increased from approximately 17,309 k.m. to 36,535 k.m. and from approximately 450 million sq.m. to 719 million sq.m., respectively from 2014 to 2022.

According to the 14th Five-Year Plan for National Economic and Social Development of Changchun City and the Outline of Vision 2035* (《長春市國民經濟和社會發展第十四個五年規劃和2035年遠景目標綱要) issued in 2021 by the government of Changchun, the municipal government proposed to construct city heating network, promote the application of "Internet+" in the heating industry and realize smart heating through integration. Moreover, it is proposed to carry out key projects such as reconstruction and expansion of regional boiler rooms and natural gas distributive heating, facilitating the speeding up of heating pipelines construction and improving the municipal heating infrastructure. With the development of national efforts on developing heating from clean energy sources and the goal of "carbon peaking and caron neutrality", the PRC government emphasized on accelerating the clean reform of coal-fired heating facilities, promoting the use of renewable energy for heating, eliminating the burning of bulk coal and speeding up the renovation of old heating pipelines.

In March 2022, the Ministry of Housing and Urban-Rural Development* (住房和城鄉建設部) published the notice of the "14th Five-Year Plan for Building Energy Conservation and Green Building Development" (《「十四五」建築節能與綠色建築發展規劃》), aiming to complete the energy efficiency retrofit of more than 100 million sq.m. in existing residential buildings nationwide by 2025. The release of a series of policies implies the future development of the heating industry will focus on promoting the provision of heat from clean energy sources, improving the efficiency of heating energy use, and accelerating the construction and renovation of heating pipelines. As disclosed in the 2023 Annual Report, the Group would uphold its original intention while deepening reform to adapt to industry trend in the future to advance its development in clean energy heating business. By actively improving its layout in heat supply industry, the Group is committed to making further contribution to the industrial development.

2. Information on Chuncheng Investment

As disclosed in the Letter from the Board, Chuncheng Investment is a state-owned company established on 28 April 1998 in Changchun City, the PRC, and is wholly-owned by the State-owned Assets Supervision and Administration Commission of Changchun (長春市人民政府國有資產監督管理委員會). Chuncheng Investment and its subsidiaries are mainly engaged in property management, water supply, pipeline manufacturing, heat production and supply, sale of industrial steam and financial investments. Chuncheng Investment is a controlling shareholder of the Company holding approximately 69.75% of the total share capital of the Company.

* *For identification purpose only*

3. The Proposed Acquisition

3.1 *Principal terms of the Second Assets Transfer Agreement*

Details of the Second Assets Transfer Agreement are set out in the Letter from the Board. The principal terms and conditions of the Second Assets Transfer Agreement are as follows:

Date	1 November 2024
Parties	(a) The Company, as the purchaser (b) Chuncheng Investment, as the vendor
Assets to be acquired	Pursuant to the Second Assets Transfer Agreement, the Company has conditionally agreed to purchase, and Chuncheng Investment has conditionally agreed to sell, the Assets, subject to the terms and conditions therein. The Assets comprise certain structures, coal-fired boilers and ancillary equipment currently used by Chuncheng Investment for heat production purposes. According to the information provided by Chuncheng Investment, the book value of the Assets amounted to RMB42,111,854.46 as at 31 August 2024.
Consideration	The Consideration is RMB82,886,461.00, which shall be satisfied by the Company in cash on the Completion Date. The Consideration has been arrived at after arm's length negotiations between the Company and Chuncheng Investment with reference to the total appraised value of the Assets of RMB82,886,461.00 as at 31 August 2024 (the "**Valuation Date**") as stated in the valuation report prepared by the Valuer, using the cost method. The Group intends to finance the Consideration by its existing internal resources.
Conditions precedent	Completion is conditional upon the following conditions having been fulfilled: (a) Chuncheng Investment having completed the applicable internal decision-making procedure in respect of the Second Assets Transfer Agreement and the transactions contemplated thereunder in accordance with the requirements of its articles of association;

(b) the Second Assets Transfer Agreement and the transactions contemplated thereunder having been approved by the Board and the Shareholders at general meeting of the Company in accordance with the requirements of the Listing Rules, the Articles of Association and applicable laws and regulations; and

(c) (where applicable) as regards the entering into and performance of the Second Assets Transfer Agreement, each of Chuncheng Investment and the Company having obtained and completed all necessary consents, approvals and filings from or with any relevant governmental or regulatory authorities in the PRC, Hong Kong or other jurisdictions.

None of the conditions above may be waived (whether in whole or in part) by either party.

Completion

Upon the fulfilment of all of the conditions precedent set out in the Second Assets Transfer Agreement, Completion shall take place on the Completion Date.

With effect from the Completion Date, all interests, rights and obligations attached to the Assets shall be transferred from Chuncheng Investment to the Company.

As discussed with the Management, they have conducted due diligence on the Assets, including, among others, (i) obtaining key documents such as state-owned land use rights certificate, the certificates of special equipment use registration for the boilers, and the contract for the construction of centralized heat supply; (ii) engaging a Valuer to appraise the Assets based on independent, objective, and fair principles; and (iii) consulting a PRC legal adviser to perform a legal analysis regarding the transfer of the Assets through a non-public method, and considered that no material issues that may affect the feasibility of the Proposed Acquisition had been identified. According to the valuation descriptions given by the Valuer, various approaches were employed, including site inspections, surveys of day-to-day management practices and operation, information gathering from third parties, verification of vouchers, etc. As confirmed in the Valuation Report, the Assets are free from pledges or guarantees. Additionally, we obtained a legal opinion prepared by the PRC legal adviser, who conducted an analysis on the feasibility of transferring the Assets through a non-public method. It is noted that the transfer is feasible provided that the necessary approvals are obtained from the relevant regulatory authorities overseeing state-owned assets. We inquired the PRC legal adviser on their qualifications, experience and independence and reviewed their credentials, and noted that the PRC legal adviser holds a practicing license in accordance with the Law of the PRC on Lawyers and the Measures for the Administration of Law Firms, and the personnel in charge is awarded an Outstanding Lawyer in Jilin Province.

Consideration

To assess the fairness and reasonableness of the Consideration, we obtained the valuation report prepared by the Valuer (the "**Valuation Report**"), details of which are set out in Appendix II to the Circular.

We understood from the Management that the Assets were appraised by Beijing Zhong Ping Heng Xin Asset Appraisal Co., Ltd.* (北京中評恒信資產評估有限責任公司), an independent firm of qualified valuers in the PRC. According to the Valuation Report prepared by the Valuer, the total appraised value of the Assets as of 31 August 2024 was RMB82,886,461.00, among which RMB4,547,466.00 was attributable to the structures and RMB78,338,995.00 was attributable to the coal-fired boilers and ancillary equipment.

According to the Letter from the Board, as at the Valuation Date, the book value of the Assets amounted to RMB42,111,854.46. The difference between the appraised value and the book value was mainly attributable to:

(a) the increase in the original value of equipment is mainly due to the continued price increase in the PRC whereby the prices in the materials market have shown an upward trend, the direct costs of construction projects, labour costs and prices of machineries also increase simultaneously, resulting in an increase in the value of the replacement cost of the Assets under appraisal; and

(b) differences in the depreciation rate adopted by Chuncheng Investment in calculating the net book value and the integrated newness rate adopted by the Valuer in the valuation process. Generally, the period adopted in the valuation which takes into account the physical state of the equipment's effective usability is longer than the useful life adopted by Chuncheng Investment determined in accordance with applicable accounting standards. For instance, some equipment can continue to operate normally even when it has surpassed its useful life. For illustration purpose only, the useful life adopted by Chuncheng Investment in calculating the net book value in accordance with applicable accounting standards is 5 years for electronic equipment and 10 years for machinery and equipment while the economic life ranged from 8 to 20 years and the used life of the respective assets ranged from 0.67 to 21.85 years.

(1) *Valuer's qualification and independence*

For our due diligence purpose, we have obtained and reviewed (i) the terms of engagement between the Valuer and the Company; (ii) the Valuer's work scope for preparing the Valuation Report; (iii) the Valuer's qualifications and experience in relation to the preparation of the Valuation Report; and (iv) track records on other valuations conducted by the Valuer. We noted from the engagement letter entered into between the Company and the Valuer that the scope of work was appropriate for the Valuer to form the opinion required to be given and there were no limitations on the scope of work which might adversely impact the degree of assurance given by the Valuer in the Valuation Report. Furthermore, based on the relevant information provided by the Valuer and our interview with them, we are satisfied with their qualifications for preparing the Valuation Report. We also noted that the personnel in charge and signing the Valuation Report is a practicing member of China Appraisal Society with over 20 years of valuation experience, particularly in asset or equity acquisitions for state-owned enterprises. The Valuer also confirmed that they are independent to the Group and Chuncheng Investment.

(2) *Valuation's methodology*

We noted from the Valuation Report that the Assets consist of (i) structures such as walls and peak-shaving chimney and (ii) coal-fired boilers and ancillary equipment, and the value of the Assets was determined based on the cost approach. We further reviewed and inquired about the methodology, basis, and assumptions used in the Valuation Report. The Valuer has considered three generally accepted appraisal approaches, namely, income approach, market approach and cost approach.

The income approach in asset value appraisal refers to the appraisal approach that determines the value of an asset by capitalizing or discounting the expected earnings of the asset. The income approach measures the value of an asset from the perspective of the profitability.

The market approach in asset value appraisal refers to the appraisal approach that compares the appraised subject with comparable assets or assets with transaction cases in the market to determine the value of the appraised subject.

The cost approach in asset value appraisal is as follows. Firstly, the replacement cost is determined by all cost required to re-construct a brand-new appraised asset under the current condition. Then the newness rate is determined by the comparison between the appraised asset and the brand-new one. The appraised value is determined by the replacement cost multiplying the newness rate.

As discussed with the Valuer, the Assets, which include (i) structures such as walls and peak-shaving chimney and (ii) coal-fired boilers and ancillary equipment, are unable to generate income individually. Furthermore, for the Assets as a whole, it is difficult to quantify costs and expenses related to labor, management and operation, land, and boilers that are assigned to the Assets in monetary terms, the estimation of which involves a variety of assumptions and improper assumptions will impose significant impact on the fair value. Therefore, the income approach is not appropriate for this appraisal. As advised by the Valuer, the market approach typically appraises assets collectively rather than individually. The market approach is unsuitable in this case due to the difficulty in collecting transaction records of assets similar to the subject of appraisal in the market. The cost approach, which takes into account the physical deterioration and all relevant forms of obsolescence and optimisation, is an appropriate approach for appraising the Assets. In light of the above, we concur with the Valuer's view that the income approach and the market approach are considered less suitable than the adopted cost approach.

The formulae adopted by the Valuer in arriving at the appraised value of the Asset are as follows:

Appraised value = Replacement cost × Integrated newness rate

Integrated newness rate = (Newness rate determined by the survey method × 60% + Newness rate determined by the lifetime method × 40%)

Newness rate determined by the lifetime method = (economic life – used life) ÷ economic life

(3) *Analysis on integrated newness rate*

As discussed with the Valuer, the economic life of the Assets was referenced from the Handbook of Common Methods and Parameters for Asset Valuation* (資產評估常用資料與參數手冊). We obtained and reviewed the data used by the Valuer for appraising the structures and boilers, which aligns with their methodology.

The newness rate determined by the survey method involved scoring the structures through site inspections based on (i) the completeness of the main structure and (ii) its functionality for business operations. For the coal-fired boilers and ancillary equipment, scoring was primarily based on (i) degrees of corrosion and scale, (ii) deformation and breakage, (iii) furnace bar operation, (iv) the frequency of inspections on instruments and safety valves, (v) abnormal heating and vibration, and (vi) boiler outlet vapor pressure. We also obtained and reviewed the scoring records for sampled assets and inspection photos of the Valuer's site visit.

Furthermore, we inquired with the Valuer about the basis for the weighting rate of the integrated newness rate. According to the Valuer, the newness rate determined by the lifetime method is more theoretical and does not take account of physical condition of a specific asset. The limitation is addressed by incorporating the survey method, which reflects the actual condition of the assets. As a result, a greater weighting is assigned to the newness rate determined by the survey method in the valuation process. Additionally, our online research indicated that a weighting of 40% for the newness rate determined by the lifetime method and 60% for the newness rate determined by the survey method is considered a practical valuation norm in the industry. This approach balances theoretical assessments with the tangible condition of the assets being evaluated.

According to the Letter from the Board, of the 5 structures under valuation, the economic life ranged from 20 to 30 years and the used life of the respective assets ranged from 1.67 to 20.35 years. The integrated newness rate adopted by the Valuer for the valuation of "fixed assets — structures" ranged from 21% to 94%. Of the 527 equipment under valuation, the economic life ranged from 8 to 20 years and the used life of the respective assets ranged from 0.67 to 21.85 years. The integrated newness rate adopted by the Valuer for the valuation of "fixed assets — equipment" ranged from 15% to 97%.

Set out below are further information in relation to the top 5 equipment item with the highest appraised value:

	Equipment item	**Appraised value** *(RMB)*	**Net book value** *(RMB)*	**Newness rate determined by the lifetime method**	**Newness rate determined by the survey method**
1.	Boiler #4–6 Public desulfurization tower	10,474,082.00	4,161,039.08	54%	65%
2.	Public desulfurization tower	4,807,449.00	2,065,731.65	54%	60%
3.	Boiler #1	4,370,610.00	2,876,561.72	67%	65%
4.	Dust collector #4	3,817,130.00	1,625,921.94	54%	60%
5.	Boiler #6	3,642,175.00	2,080,747.19	36%	30%

We obtained a full list of the appraised Assets, and noted that the peak-shaving chimney and walls have been used for approximately 18 to 20 years, while the coal storage yard has been used for approximately 2 years. Of the 527 coal-fired boilers and ancillary equipment, 133 pieces have been utilized for less than 10 years with an appraised value of approximately RMB52.5 million, whereas 394 were used for more than 10 years with an appraised value of approximately RMB25.8 million. Notably, more than 80% of the total appraised value of equipment is derived from desulphurization towers, dust collectors, and boilers. The desulphurization towers and dust collectors have been used for approximately 7 to 9 years whereas the boilers have been used for approximately 7 to 20 years. As discussed with the Valuer, as economic life of an asset does not account for factors such as maintenance, long-aged equipment can remain operational with adequate maintenance even if its used life exceeds its economic life.

Approximately 18.5% of the equipment, in terms of appraised value, was evaluated with a higher newness rate determined by the lifetime method compared to the survey method. Conversely, approximately 64.3% of the equipment was evaluated at a higher newness rate determined by the survey method by less than 20% relative to the lifetime method. Additionally, approximately 7.9% of the equipment was assessed with a higher newness rate determined by the survey method by more than 20% compared to lifetime method, while approximately 9.2% of the equipment has been utilized beyond its economic life resulting in a theoretical negative newness rate determined by the lifetime method. The useful life of equipment varies based on its type, quality, usage conditions, and maintenance practices. The newness rate determined by the survey method is generally higher than that determined by the lifetime method, as the survey method takes account of maintenance whereas the lifetime method does not. As regular maintenance has been conducted on aged equipment, higher newness rates determined by the survey method as compared to lifetime method were adopted based on the actual state and the operation efficiency of such equipment. For equipment that has reached its economic life but remains in normal use, the Valuer adopted a 15% integrated newness rate, which aligns with the industry norm developed based on previous Notice on Forwarding the Opinions on the Operating Procedure for Asset Appraisal (for Trial Implementation) (No.23 [1996] of the Office of the State-owned Assets Administration Bureau)* (國資辦發[1996]23號國家國有資產管理局關於轉發《資產評估操作規範意見(試行)》的通知), which stipulated that the newness rate of assets under normal operation should not be less than 15% and that the appraised value should not fall below 15% of the replacement cost.

(4) *Analysis on replacement costs*

According to the Letter from the Board, there are a total of 5 structures under valuation and the replacement cost ranged from RMB162,000 to RMB3,630,480. As part of our work performed on the replacement cost, we obtained the valuation workings for all structures and understood that the replacement cost primarily comprises (i) construction costs of the structures, (ii) upfront and other costs including those related to survey and design, feasibility studies, supervision on construction projects, and construction management, and (iii) opportunity cost of capital. According to the Valuer, the major factors considered in determining the appraised value of structures are commonly used parameters in the replacement cost approach. In this regard, we have (i) reviewed the relevant sources of information and calculations; (ii) discussed with the Valuer the basis and assumptions for the key factors; and (iii) noted that the estimated construction costs per square metre for the coal storage yard were determined with reference to the Construction Project Cost Index of Changchun for the first half of 2024* (2024年上半年長春市建設工程造價指數指標), and the costs for peak-shaving chimney and walls were based on price inquiries and adjusted with reference to materials used and conditions. We obtained the Valuer's price inquiry records containing the supplier's website, contact person, pricing details, and dimensions. Furthermore, we obtained a breakdown of upfront and other costs and noted that these fees were referenced to the Circular of the State Planning Commission on the Issuance of Provisional Regulations on Consultation Fees for Preliminary Work on Construction Projects* (《國家計委關於印發建設項目前期工作諮詢收費暫行規定的通知》, the Provisions for the Management of Construction Costs for Construction Projects* (《基本建設項目建設成本管理規定》) published by Ministry of Finance of the People's Republic of China, the Regulations on the Administration of Engineering Survey and Design Charges* (《工程勘察設計收費管理規定》) published by the State Planning Commission and the Ministry of Construction, and the Regulations on the Administration of Construction Supervision and Related Services Charges* (《建設工程監理與相關服務收費管理規定》) published by the National Development and

Reform Commission and the Ministry of Construction. Additionally, the opportunity cost of capital is determined based on (i) 50% of the aggregate of construction costs and pre-construction engineering fees assuming that the investment is made evenly over the construction period; and (ii) interest rate with reference to the loan prime rate ("**LPR**") published by the National Interbank Funding Center. We conducted an online search and noted on the website of the People's Bank of China that the one-year LPR was 3.35% and the over-five-year LPR was 3.85% as of 20 August 2024, which is consistent with the Valuer's calculations.

According to the Letter from the Board, there are a total of 527 equipment under valuation and the replacement cost ranged from RMB868 to RMB17,170,626. As advised by the Valuer, a total of 527 pieces of equipment were appraised, comprising 9 coal-fired boilers and 518 ancillary equipment. We obtained a full list of equipment and reviewed valuation workings for the top 10 original fair value (before adjustment for the integrated newness rate) and the top 10 net fair value (adjusted for the integrated newness rate) equipment ("**Samples**"). Since the appraised value of the Samples covered over 60% of the total appraised value, we believe we have reviewed a sufficient number of samples in arriving at our conclusion. We further noted that the replacement costs of the 9 coal-fired boilers were based on market purchase prices. We obtained the price inquiry records for all 9 coal-fired boilers from the Valuer and noted that the purchase costs mainly comprise price of the boiler and ancillary parts, transportation expenses, installation fees, and other upfront costs to bring the equipment to the condition ready for use.

As discussed with the Valuer, the replacement cost of the remaining equipment is referenced to the original purchase price and adjusted according to the Industrial Producers' Ex-factory Price Index* (工業生產者出廠價格指數) published by National Bureau of Statistics. As advised by the Management, the ancillary equipment to be acquired are generally high-quality products featuring optimized combustion control system and there has been no noticeable technological advancement. We further discussed with the Valuer and understood that there are two commonly used methods for calculating replacement cost: renewal replacement cost and restoration replacement cost. Renewal replacement cost represents the cost of purchasing and constructing a new asset with the same functions as the appraisal object, utilizing new materials, modern construction or manufacturing standards, and upgraded designs, specifications and technologies at current price levels. In contrast, restoration replacement cost involves the cost of repurchasing and building a new asset identical to the appraisal object, using the same materials, construction or manufacturing standards, design, specifications and technology as the original asset, all at current price levels. Due to the difficulty in collecting transaction records for assets similar to the boiler ancillary equipment such as desulphurization towers and dust collectors in the market, the Valuer opted for the restoration replacement cost method. Furthermore, for assets whose design, materials, and specifications remain consistent for decades, there is no material difference in value between the two replacement cost methods. We conducted an online search and noted that there are two categories of replacement cost as outlined in the Code of Practice on Asset Appraisal — Asset Appraisal Methods published by China Appraisal Society in

December 2019, stating that the restoration replacement cost applied by reproducing the appraisal object in its original condition. Accordingly, obsolescence due to technological advancement was not considered when adjusting the price according to relevant price index. We also gathered data from several sources including Indicators of Equipment Installation and Commissioning Rates* (機器設備安裝調試費率指標參考), Indicator of Domestic Equipment Transportation And Miscellaneous Charges* (國產設備運雜費參考指標), and Estimated Domestic Equipment Base Fee Indicators* (國內設備基礎費概算指標) and noted that the information is generally in line with the valuation results.

We also obtained detailed explanation of the Valuation Report from the Valuer and based on our understanding on the workings in arriving at the Valuation, we did not identify any major factors that would lead us to question the fairness and reasonableness of the methodology, principal basis, and parameters used in the Valuation Report.

Having considered (i) the valuation methodology adopted by the Valuer for determining the fair value of the Assets is in line with market practice and the underlying basis and assumptions are reasonable; (ii) the appraised value as set out in the Valuation Report serves as an appropriate benchmark for assessing the consideration of the Assets; (iii) the Consideration is equal to the valuation provided by the Valuer; and (iv) our independent work performed on the Valuation Report, we are of the view that the consideration of the Assets is fair and reasonable.

Based on the above, we concur with the Directors' view that the terms of the Second Assets Transfer Agreement are fair and reasonable, the transactions contemplated thereunder are on normal commercial terms and in the interests of the Company and the Shareholders as a whole.

3.2 *Reasons for and benefits of the Proposed Acquisition*

As disclosed in the Letter from the Board, since the Company is mainly engaged in heating service business and the Assets are used for heat production purposes, the Company is of the view that the Proposed Acquisition would enable the Group to further enhance its heat production efficiency, optimize the structure of the Group's heat supply business, increase its capabilities on heat source protection, significantly reduce the amount of continuing connected transactions between the Group and Chuncheng Investment Group as well as minimize any potential competition between the Group and Chuncheng Investment Group, which in turn is beneficial to the Group's overall strategic development.

Chuncheng Investment has undertaken that upon Completion, it shall grant the Company a right of use of the premises which the Assets currently situate at nil consideration. Chuncheng Investment also warranted that the Company's operations on the aforementioned premises will not be affected by issues on land ownership. Upon Completion, the Assets will be solely operated, maintained and supervised by the Group's employees.

To enhance its heat production efficiency, optimize the business structure and increase its capabilities on heat source protection

Following the acquisition of structures, coal-fired boilers, and ancillary equipment in the Dongling and Jingyue thermal power stations, the Group is better positioned to control a greater share of heat production resources. As discussed with the Management, the coal-fired boilers in these districts serve as peak-shaving boilers, maintaining back-up heating capacity in the heating zone during peak periods or in emergencies. In accordance with the Regulations on Changchun Municipal Heat Supply Management (《長春市城市供熱管理條例》) implemented in October 2018, heat service providers using heat procured from local cogeneration plants are required to maintain peak-shaving boilers to address any suspension or shortage in heat supply from the cogeneration plants. Moreover, the peak-shaving boilers in the Dongling and Jingyue thermal power stations are expected to provide a heat supply of approximately 680,000 GJ per year. Acquiring these Assets from Chuncheng Investment will enhance the quality of the Group's heat supply in both districts, thereby strengthening its capacity for heat source protection.

Further, the provision of heat supply services heavily relies on the heating facilities and infrastructure such as heating pipeline network and boiler facilities, which are subject to the limitation of underground space necessary for pipelines and the local government's overall development plan. According to the A-share listing application prospectus published in October 2023, the Group's heating service area primarily covers inner urban regions of Changchun, including Dongling and Jingyue districts. As advised by the Management, the Group's primary pipeline network is connected to the peak-shaving boilers in the Dongling and Jingyue thermal power stations, allowing heat delivery without the need to construct new pipelines which may incur significant costs and time. According to the Letter from the Board, upon Completion, Chuncheng Investment shall grant the Company a right of use of the premises which the Assets currently situate at nil consideration and the Assets will be solely operated, maintained and supervised by the Group's employees. We have obtained a letter of undertaking issued by Chuncheng Investment, which confirms that the Company is entitled to the right to use the premises where the Assets are located at no cost. Chuncheng Investment has also warranted that the Company's operations on the aforementioned premises will not be affected by issues on land ownership. Additionally, the Company has secured a PRC legal opinion concerning the transfer of the Assets through a non-public method as set out under sub-section headed "3.1 principal terms of the Second Assets Transfer Agreement". Furthermore, following the Proposed Acquisition, the Company will apply to register the use of the boilers with the Changchun Administration for Market Regulation. By consolidating heat sources and allocating them effectively, the Group can enhance production efficiency and optimize its business operations through a stable heat supply.

To reduce the amount of continuing connected transactions

As disclosed in the circular of the Company dated 7 November 2023, the Company entered into the 2024–2026 heat procurement framework agreement with Chuncheng Investment on 11 October 2023, pursuant to which Chuncheng Investment Group shall supply heat to the Group. As advised by the Management, the connected transaction amount was approximately RMB117.3 million for FY2022 and RMB83.0 million for FY2023, and the Proposed Acquisition is expected to reduce the annual connected transaction amount by approximately RMB38.5 million. This will result in a smaller size of continuing connected transactions, leading to lower percentage ratios, which consequently may exempt the Company from the circular and shareholders' approval requirements, ultimately reducing compliance costs.

To minimize any potential competition

According to the Letter from the Board, Chuncheng Investment and its subsidiaries are mainly engaged in property management, water supply, pipeline manufacturing, heat production and supply, sale of industrial steam and financial investments. Through the Proposed Acquisition, the Group will incorporate certain structures, coal-fired boilers, and ancillary equipment located in the Dongling and Jingyue thermal power stations for heat production. The Proposed Acquisition marks a step toward further integrating Chuncheng Investment Group's heat supply business in Changchun into the Group, thereby reducing potential business competition between Chuncheng Investment Group (excluding the Group) and the Group in this business sector. We concur with the Management's view that the Proposed Acquisition would reduce potential competition between the Group and Chuncheng Investment Group, ultimately benefiting Group's overall strategic development.

3.3 *Possible financial effects of the Proposed Acquisition*

Earnings

The Assets mainly consist of peak-shaving boilers, which are able to supply heat through the Group's distribution pipelines, one of the Group's major business segments. Thus the Proposed Acquisition is expected to have positive effect on the Group's earnings. As confirmed by the Management, the taxes and professional fees related to the Proposed Acquisition will have a minimal effect on the Group's net income.

Net asset value

As discussed with the Management, upon Completion, the Group's cash and cash equivalents will decrease by the amount of the Consideration, while fixed assets will increase. Since the Consideration matches the appraised value of the Assets, the Group's total assets would have remained unchanged. Although there are associated taxes and professional fees from the Proposed Acquisition, their impact on liabilities and net assets is minimal.

Working capital

As set out in the Letter from the Board, the Consideration of RMB82,886,461.00 will be financed by the Group's existing internal resources and settled in cash. It is anticipated that the Group's bank balance will decrease by the amount of the Consideration upon the Completion. According to the Management, based on the cash flow and earnings forecast for 2024 and 2025, the outflow of the Consideration will not have a material adverse effect on the Company's business operations.

4. The provision of the Loan

4.1 *Principal terms of the Loan*

Details of the Loan are set out in the Letter from the Board. The principal terms of the Loan are as follows:

Date	1 November 2024
Lender	the Company
Borrower	Chuncheng Investment
Amount of the Loan	Not more than RMB300 million During the term of the Loan, Chuncheng Investment may draw down the Loan in one or more tranches by providing the Company with a drawdown request (the "**Drawdown Request**"), specifying the intended drawdown amount. Within 15 business days of receiving the Drawdown Request, the Company shall inform Chuncheng Investment whether or not the Company accepts such Drawdown Request and make available such funds to Chuncheng Investment if such Drawdown Request is accepted. The Company has absolute discretion in determining whether to accept any Drawdown Request.

Interest rate	4.5% per annum The interest rate was arrived at after arm's length negotiations between the Company and Chuncheng Investment having taking into consideration the prevailing market interest rates. Interest shall be payable by Chuncheng Investment to the Company by the 15th calendar day of the month following the end of each quarter.
Term of the Loan	From the date when the Independent Shareholders approved the Loan Agreement at the EGM up to 31 December 2029 (the "**Maturity Date**") (both days inclusive)
Maturity and repayment	Chuncheng Investment shall repay the Loan together with any accrued interest in full on the Maturity Date. Upon obtaining the Company's prior consent, Chuncheng Investment may repay the Loan or any part thereof at any time before the Maturity Date without penalty. Chuncheng Investment acknowledged that the Company has the right to require Chuncheng Investment to repay the Loan or any part thereof at any time before the Maturity Date due to the Company's business needs or capital market operation requirements.
Purpose of the Loan	The Loan is provided to Chuncheng Investment for the "Retreat from the City and Enter into the Suburbs Project" (退城進郊項目) (the "**Retreat Project**"), transformation of old pipe network(s) (the "**Transformation Project**"), as well as to supplement Chuncheng Investment Group's general working capital.

To assess the fairness and reasonableness of the key terms of the Loan Agreement, we have conducted research, using our best endeavours, of recent similar transactions in which listed companies on the Stock Exchange or their subsidiaries provided loan or financial assistance to controlling shareholder or its controlled company. Based on our best effort and as far as we are aware, we have identified 17 comparable transactions (the "**Comparables**"), which meet the aforementioned criteria and were announced by companies listed on the Stock Exchange between 1 November 2023 and 31 October 2024 (the "**Comparison Period**"), being one year, to provide a general reference for recent market practices in relation to the key terms of the Loan Agreement under similar market condition. We believe that the Comparison

Period is appropriate since it offers a reasonable and meaningful sample size for our analysis and the Comparables collectively provide a fair and representative overview of the market practice.

Independent Shareholders should be aware that (i) the principal businesses, operations, size of assets, and prospects of the Company may not be exactly the same as those of the Comparables; and (ii) the credit risk associated with the underlying borrowers of the Comparables may not be the same as that of Chuncheng Investment. Notwithstanding the above, after considering that (i) all Comparables are similar in nature to the Loan Agreement, namely provision of loan or financial assistance to a controlling shareholder or its controlled company by a listed issuer on the Stock Exchange or its subsidiary; (ii) all of underlying transactions of the Comparables occurred within one year from the date of the Loan Agreement, reflecting recent market practices in respect of the interest rate and other terms charged to controlling shareholders, thereby offering a more relevant reference; and (iii) to the best of our knowledge, the list of the Comparables is exhaustive based on the specified criteria, we consider the Loan to be comparable to the Comparables, and our assessment on the Comparables serves as a general reference to the recent market practice in respect of the transactions with controlling shareholders for loans or financial assistance under the current market conditions and sentiment so as to assess the fairness and reasonableness of the Loan Agreement. Set out below are the details of the Comparables:

No.	Date of announcement	Name of company	Stock code on the Stock Exchange	Principal amount *(Note 1)*	Term (year) *(Note 2)*	Interest rate p.a.	Guarantee	Pledge
1	25 Oct 2024	China Shuifa Singyes New Materials Holdings Limited	8073	RMB30,000,000	3.0	6.00%	No	No
2	7 Oct 2024	Minshang Creative Technology Holdings Limited	1632	HKD9,500,000	1.0	8.00%	No	No
3	30 Sep 2024	S-Enjoy Service Group Co., Limited *(Note 3)*	1755	RMB1,120,000,000	3.0	6.05%	No	Yes
4	3 Sep 2024	Regal Hotels International Holdings Limited *(Note 4)*	78	HKD857,000,000	11.0	5.85%	Yes	Yes
5	16 Aug 2024	Henan Jinyuan Hydrogenated Chemicals Co., Ltd.*(Note 5)*	2502	RMB30,000,000	1.0	5.00%	No	No
6	25 Jul 2024	Chinney Alliance Group Limited *(Note 6)*	385	HKD250,000,000	2.0	6.00%	No	No
7	23 Jul 2024	A-Living Smart City Services Co., Ltd.	3319	RMB51,749,360	0.4	3.45%	No	Yes
8	19 Jul 2024	MicroPort CardioFlow Medtech Corporation *(Note 7)*	2160	RMB10,000,000	2.0	3.45%	No	Yes
9	2 Jul 2024	iMotion Automotive Technology (Suzhou) Co., Ltd.	1274	RMB11,000,000	3.0	3.45%	No	No
10	26 Jun 2024	Arrail Group Limited *(Note 8)*	6639	USD11,000,000	2.5	5.50%	No	Yes
11	17 Jun 2024	JH Educational Technology INC.	1935	RMB55,000,000	2.0	3.10%	No	No
12	11 Jun 2024	China East Education Holdings Limited *(Note 9)*	667	RMB150,000,000	1.6	7.00%	Yes	No
13	28 Dec 2023	Readboy Education Holding Company Limited *(Note 10)*	2385	RMB5,000,000	1.6	3.95%	No	No
14	18 Dec 2023	Wai Yuen Tong Medicine Holdings Limited	897	HKD100,000,000	5.0	10.00%	No	No

No.	Date of announcement	Name of company	Stock code on the Stock Exchange	Principal amount *(Note 1)*	Term (year) *(Note 2)*	Interest rate p.a.	Guarantee	Pledge
15	1 Dec 2023	ZTO Express (Cayman) Inc. *(Note 11)*	2057	RMB500,000,000	6.0	5.00%	Yes	No
16	1 Dec 2023	AAC Technologies Holdings Inc	2018	RMB74,000,000	3.0	3.45%	No	No
17	6 Nov 2023	China Taiping Insurance Holdings Company Limited *(Note 12)*	966	HKD1,250,000,000	10.0	5.80%	No	No
			min	RMB5,000,000	0.4	3.10%		
			mean	RMB254,982,315	3.4	5.36%		
			median	RMB74,000,000	2.5	5.50%		
			max	HKD1,250,000,000	11.0	10.00%		
		The Company	1853	Not more than RMB300,000,000	5	4.5%	No	No

Source: website of the Stock Exchange

Notes:

(1) For the revolving loan or loan framework agreements, the maximum loan amount is considered the principal amount. For illustration purpose only, amounts denominated in HKD have been translated into RMB at an exchange rate of HKD1 = RMB0.9, and amounts denominated in USD have been translated into RMB at a rate of USD1 = RMB7.1.

(2) For the extension loan agreements, the total length of loan period is used for the term of loan after taking into account the original loan agreements.

(3) As disclosed in the announcement of S-Enjoy Service Group Co., Limited ("**S-Enjoy**") dated 30 September 2024, S-Enjoy and the borrower entered into (i) a loan framework agreement with an aggregate principal amount of RMB1,000.0 million and (ii) a loan agreement with a principal amount of RMB120.0 million. Since both agreements were made by the same parties and shared the same interest rate and maturity date, the total amount of RMB1,120 million is used for the principal amount. The interest rate was the higher of: (i) the loan prime rate ("**LPR**") for loans of more than one year (inclusive) and less than five years (if any) published by the People's Bank of China ("**PBOC**") applicable on the date of drawdown; and (ii) the fixed lending rate of 6.05% per annum. According to the Announcement on Loan Prime Rate (September 20, 2024) published by the PBOC, the one-year LPR was 3.35% and the over-five-year LPR was 3.85%. Accordingly, 6.05% was selected for the interest rate.

(4) As disclosed in the joint announcement of Regal Hotels International Holdings Limited ("**Regal**") and Cosmopolitan International Holdings Limited dated 3 September 2024, the maturity date had been extended twice, with the final maturity date set for October 2027. The original loan facilities were granted in 2016, resulting in a total loan term of approximately 11 years. The revised interest rate was 1-month HIBOR plus 1.95% per annum. According to The Hong Kong Association of Banks, one-month HKD Interest Settlement Rates were 3.89929% as of 3 September 2024. Accordingly, the applicable interest rate was approximately 5.85%.

(5) As disclosed in the announcement of Henan Jinyuan Hydrogenated Chemicals Co., Ltd. dated 16 August 2024, a 51% subsidiary of Henan Jinyuan Hydrogenated Chemicals Co., Ltd. entered into the loan agreement on 2 January 2024 with the borrower for a term from 2 January 2024 to 30 June 2024.

Subsequently on 30 June 2024, the renewal agreement was entered into to extend the loan for a further term from 1 July 2024 to 31 December 2024. Accordingly, the total loan term amounted to approximately 1 year.

(6) As disclosed in the joint announcement of Chinney Alliance Group Limited and Chinney Kin Wing Holdings Limited dated 25 July 2024, the loan agreement has a term of twelve months. The borrower may seek an extension for a further twelve months provided that the borrower shall have given to the lender a written request with no less than one month prior to the date falling twelve months from the drawdown date. The lender shall accordingly provide a written reply (which shall not be unreasonably withheld) upon receipt of such request. Should the lender fail to reply in writing by the date falling twelve months from the drawdown date, the request for extension is deemed to be granted and in such case, the maturity date will become the date falling twenty-four months from the drawdown date. Given the borrower's right to extend, a total term of 2 years is selected.

(7) As disclosed in the announcement of MicroPort CardioFlow Medtech Corporation dated 19 July 2024, the interest rate for the loan was equivalent to the one-year LPR on the date of the loan agreement. According to the Announcement on Loan Prime Rate (June 20, 2024) published by the PBOC, the one-year LPR was 3.45%. Accordingly, the applicable interest rate was 3.45%.

(8) As disclosed in the announcements of Arrail Group Limited dated 29 September 2022, 27 June 2023, and 26 June 2024, the term of the loan was extended first from 9 months to 18 months, and then to 30 months. The interest rate was also revised from 4.5% to 5.5% per annum. Therefore, 30 months and 5.5% are selected as the term and interest rate respectively to reflect the latest status of the loan.

(9) As disclosed in the announcement of China East Education Holdings Limited dated 11 June 2024, a revolving loan facility with a maximum daily balance (excluding the accrued interests) of RMB50 million was granted to each of the three borrowers, all of whom are directors and substantial shareholders of the company, with one being the controlling shareholder. The total maximum daily balance (excluding the accrued interests) was RMB150 million. According to the 2023 annual report of China East Education Holdings Limited, the three borrowers are cousins of each other. Accordingly, RMB150 million is chosen for the principal amount of the loan.

(10) As disclosed in the announcement of Readboy Education Holding Company Limited dated 28 December 2023, the term of the loan had been extended, changing the loan period from 17 May 2023 to 31 December 2023 to a new period from17 May 2023 to 31 December 2024. Accordingly, the total loan term amounted to approximately 1.6 years.

(11) As disclosed in the announcement of ZTO Express (Cayman) Inc. dated 1 December 2023, the original loan agreement was entered into in December 2020 for a term of 36 months. On 1 December 2023, a loan extension agreement was executed for an additional term of 36 months. Accordingly, the total loan term amounted to 6 years.

(12) As disclosed in the announcement of China Taiping Insurance Holdings Company Limited dated 6 November 2023, the original loan agreements were made in November 2018 for a term of 60 months. On 6 November 2023, new loan agreements were entered into for a term of 60 months. Accordingly, the total loan term amounted to 10 years. Although there are three new loan agreements, they were executed between three subsidiaries of China Taiping Insurance Holdings Company Limited and the same borrower. Accordingly, the aggregate amount of HK$1,250 million is used for the principal amount of the loan.

Principal

As illustrated in the table above, the principal loan amount of the Comparables ranges from RMB5 million to HK$1,250 million with an average of approximately RMB255.0 million. The principal amount of up to RMB300 million under the Loan Agreement falls within this range. Although the maximum principal amount of the Loan is higher than the average, the actual amount to be drawn under the Loan Agreement will depend on the Company's cash flow position and working capital needs and the Company has absolute discretion in determining whether to accept any Drawdown Request. Therefore, we concur with the Directors' view that the principal amount of the Loan is fair and reasonable so far as the Independent Shareholders are concerned.

Interest rate

According to the Letter from the Board, the interest rate was arrived at after arm's length negotiations between the Company and Chuncheng Investment having taking into consideration the prevailing market interest rates.

As shown in the table above, the interest rates of the Comparables range from 3.10% to 10.00% per annum, with an average of approximately 5.36% and a median of 5.5% per annum. The interest rate of the Loan falls within this range but is lower than both the average and the median of the Comparables. However, the Comparables include loans denominated in USD, HKD, and RMB, with USD and HKD typically exhibiting higher interest rates than RMB mainly attributed to the continuous increase in the federal fund rate from February 2022 to August 2024. According to the Board of Governors of the Federal Reserve System (US), the Federal Funds Effective Rate rose steadily from 0.08% in February 2022 to 5.33% in August 2024. In contrast, the LPR, as reported by the PBOC, declined continuously from 3.7% in February 2022 to 3.35% in August 2024. For analytical purposes, among the Comparables, there are eleven loans denominated in RMB, with a median interest rate of 3.95% and an average interest rate of approximately 4.54%. The interest rate of the Loan is higher than the median and close to the average. Additionally, we understood from the Management that the interest rate for the Group's borrowings as of 30 June 2024 was 3.9% p.a., which is lower than that of the Loan. Furthermore, Chuncheng Investment is a state-owned company established on 28 April 1998 and wholly-owned by the State-owned Assets Supervision and Administration Commission of Changchun (長春市人民政府國有資產監督管理委員會). Accordingly, we concur with the Directors' view that the interest rate is fair and reasonable so far as the Independent Shareholders are concerned.

Term and repayment

As further illustrated in the table above, the loan term of the Comparables ranges from 0.4 year to 11 years after considering any extensions. The term of the Loan, which is approximately 5 years, falls within this range. Additionally, as advised by the Management, the "Retreat from the City and Enter into the Suburbs Project" (退城進郊

項目) and the transformation of old pipe network(s) project (老舊管網改造項目) for which the Loan will be utilized are anticipated to be completed in 2026 and 2028, respectively. Therefore, we concur with the Directors' view that the term of the Loan under the Loan Agreement is fair and reasonable so far as the Independent Shareholders are concerned.

According to the Letter from the Board, upon obtaining the Company's prior consent, Chuncheng Investment may repay the Loan or any part thereof at any time before the Maturity Date without penalty. Chuncheng Investment acknowledged that the Company has the right to require Chuncheng Investment to repay the Loan or any part thereof at any time before the Maturity Date due to the Company's business needs or capital market operation requirements. We have obtained a letter of undertaking issued by Chuncheng Investment, which confirms that the Company is entitled to the right to request early repayment, and Chuncheng Investment has undertaken to fully cooperate with the Company regarding the repayment.

Guarantee and pledge

As shown in the table above, out of the 17 Comparables, 3 loans were secured by personal or corporate guarantees and 5 were secured by asset or equity pledges. Thus, it is not uncommon in the market for listed companies in Hong Kong to grant unsecured loans to their controlling shareholder without guarantees. Furthermore, Chuncheng Investment is a state-owned enterprise with over 20 years of history. Therefore, we believe that it is justifiable for the Loan to be granted without guarantees or security.

Having considered (i) the interest rate of 4.5% per annum under the Loan Agreement is within the range of the Comparables and above the LPR quoted by the PBOC as well as the Group's funding cost, (ii) Chuncheng Investment's credibility as a state-owned company established on 28 April 1998 and wholly-owned by the State-owned Assets Supervision and Administration Commission of Changchun (長春市人民政府國有資產監督管理委員會), (iii) the financing needs and completion timelines of the projects for which the Loan will be utilized; and (iv) the stable returns the Loan will provide, we are of the view that the terms of the Loan Agreement and the transactions contemplated thereunder are on normal commercial terms and fair and reasonable so far as the Company and the Shareholders are concerned and is in the interests of the Company and the Shareholders as a whole.

4.2 *Reasons for and benefits of the provision of the Loan*

According to the Letter from the Board, the Loan is provided to Chuncheng Investment for the Retreat Project, the Transformation Project as well as for Chuncheng Investment Group's general working capital. Having taking into account the Company's current available cash balances, the Company considered it in the interests of the Company and its Shareholders as a whole to grant the Loan to Chuncheng Investment because the Loan could generate interest income to the Company on one hand and at the same time, the Group would be able to benefit from the improved heat supply efficiency brought by the Retreat Project and that neither the Retreat Project nor the Transformation Project would increase potential competition between the Group and Chuncheng Investment. In addition, given the interest rate to be charged by the Company in relation to the Loan (i.e. 4.5% per annum) is above the deposit interest rate offered by other banks (i.e. approximately 1.15% to 1.35% per annum), the Company is able to generate higher interest income through the provision of the Loan than depositing the cash with the banks.

According to with the Letter from the Board, the Group has been generating profits and maintains a relatively stable cash flow in recent years. Due to seasonable operating factors, the Group's cash balance is generally lower in the first half of the year because the heat supply period begins in October every year and the Group generally commences receiving heat fees from its customers in the second half of the year. Having considered the cash inflows generated during the heat supply period and taking into consideration the maximum amount of Loan to be provided to Chuncheng Investment, the Group still has sufficient working capital to support its daily operations.

According to the Letter from the Board, having considered Chuncheng Investment is a state-owned enterprise which is wholly-owned by Changchun State-owned Assets Supervision and Administration Commission, the Company is of the view that Chuncheng Investment has high debt repayment ability and operational stability. In particular, state-owned enterprises are the underpinning pillars in the socialist economy with Chinese characteristics and they play an irreplaceable economic role in maintaining national economic security and promoting high-quality development. The PRC Government has, from time to time, announced policies to support state-owned enterprises which are engaging in livelihood industries (such as heat supply) in the form of tax incentives, financial support, etc. to ensure that they continue to play the role as underpinning pillars in sustaining and stabilizing the growth of the national economy. In addition, based on the information provided by Chuncheng Investment to the Company, Chunchneg Investment has not defaulted any loans in recent years and certain large PRC banks have provided unsecured loans to Chuncheng Investment after their credit evaluation, which indicate Chuncheng Investment's good credit record. As such, the Company considered that it is common industry practice for loans provided to state-owned enterprises to be unsecured. Moreover, based on the information provided by Chuncheng Investment, Chuncheng Investment Group generated revenue of not less than RMB430 million for the year ended 31 December 2023 and had not less than RMB411 million cash balances and unutilized bank facilities in aggregate as at 30 June 2024. Based on the foregoing, while the Loan is unsecured, the Company still considered that the recoverability risk of the Loan is low and the terms of the Loan are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

Funding needs of Chuncheng Investment

According to the Letter from the Board, the Retreat Project is a construction project undertaken by Chuncheng Investment which involves the provision of construction services by Chuncheng Investment to No. 2 Thermal Plant of Changchun City. As required by The Government of Changchun City, only wholly-owned stated-owned enterprises could undertake the construction work of the Retreat Project. As Chuncheng Investment is wholly-owned by the State-owned Assets Supervision and Administration Commission of Changchun (長春市人民政府國有資產監督管理委員會), it is eligible to undertake the construction work of the Retreat Project. As discussed with the Management, the Retreat Project is to construct (i) a long-distance heat supply pipeline network extending approximately 35 kilometers from the suburban area to the urban area of Changchun, (ii) a water pumping station covering about 1 hectare; (iii) a pressure-isolation heat exchanger spanning approximately 2.3 hectares; and (iv) a primary network connecting DN1400 heat supply pipeline to DN1000 heat supply pipeline. The capital funds for the Retreat Project are estimated to be RMB2.7 billion, which significantly exceeds Chuncheng Investment's current cash position. We conducted an online search and found news articles from Changchun Urban Planning & Research Center (the "**CUPR**"), indicating that leaders from the CUPR and Chuncheng Investment discussed the siting plan for the heating pipelines and facilities in response to the Retreat Project during a seminar held on 27 May 2024. On 2 June 2024, the CUPR and Chuncheng Investment carried on an on-site investigation to identify key points and challenges along the proposed heating pipeline route. Additionally, we noted that Chuncheng Investment released an announcement on 8 August 2024 regarding quotation on physical exploration for No. 2 thermal power plant's construction of supporting pipe network for the Retreat Project. The Transformation Project is currently in the information collation and feasibility study phase, with estimated capital funds of around RMB200 million.

According to the Letter from the Board and as advised by the Management, the Retreat Project aims to optimize the urban layout and enhance the urban environment by relocating the No. 2 thermal power plant from the city of Changchun to a suburban area. As the Group also procures heat from the No. 2 thermal power plant, the Group would be able to benefit from improved heat supply efficiency through the enhanced pipeline network while not incurring additional costs associated with constructing the pipeline infrastructure. For the Transformation Project, the relevant service area differs from that of the Group. Furthermore, as disclosed in the Company's global offering document dated 27 September 2019, the Company entered into a non-competition agreement with Chuncheng Investment, which shall continue to be effective until the earlier of the occurrence of the following situations: (i) the date on which Chuncheng Investment and its subsidiaries, in aggregate, directly or indirectly hold less than 30% of the entire issued share capital of the Company; or (ii) the date on which the H Shares cease to be listed on the Stock Exchange, except that trading in the H Shares is temporarily suspended for any reason. Therefore, it is considered that the Retreat Project and the Transformation Project would not increase potential competition between the Group and Chuncheng Investment.

Liquidity of the Group

According to the 2024 Interim Report, as at 30 June 2024, the Group had (i) current assets of approximately RMB1,019.5 million, primarily consisting of cash and cash equivalents of approximately RMB553.8 million, prepayments of approximately RMB176.2 million, trade receivables of approximately RMB155.2 million, and contract assets of approximately RMB53.5 million; (ii) a current ratio of 1.3 times, indicating that the Group has more current assets than current liabilities, thus ensuring sufficient liquidity to cover short-term obligations; and (iii) a negative gearing ratio as set out under sub-section headed "1.3 Financial position of the Group", indicating that cash and cash equivalents exceeded total interest-bearing liabilities and thus the Group's financial resources on hand is sufficient to cover its current borrowings.

According to the "Financial Information of the Group" in the Appendix I of the Circular, the Group's bank borrowings amounted to RMB615,550,000 as of 31 October 2024. As advised by the Management, these bank borrowings bear an interest rate ranging from 3.2% to 3.4% per annum and were utilized to purchase heat sources prior to the commencement of heat supply period. Given the relatively low interest rates in the PRC, the Group tends to borrow from banks to capitalize on these favorable rates, bridging the time gap between receiving heat fees and procuring heat sources while maintaining a higher level of working capital. The Management believes relevant returns could exceed the funding cost. As stated in the sub-section headed "1.3 Financial position of the Group", the Group's cash and cash equivalents increased from approximately RMB1,030.2 million as at 31 December 2022 to approximately RMB1,111.0 million as at 31 December 2023, and subsequently decreased to RMB553.8 million as at 30 June 2024 mainly attributable to the seasonality of the heat supply business, as heat fees are generally collected in the second half of the year. Consequently, the Group usually records negative net cash flows from operating activities in the first half of the year. However, the Group has consistently realized positive cash flow from operating activities, ranging from approximately RMB124 million to RMB416 million annually since 2019. As advised by the Management, the Group's cash and cash equivalents amounted to approximately RMB1.5 billion as of 31 October 2024. Furthermore, based on the Company's cash flow and earnings forecast for 2024 and 2025, the projected net cash flows from operating activities for the year ending 31 December 2024 are expected to exceed RMB300 million, with cash and cash equivalents anticipated to be over RMB1 billion as of 31 December 2024.

Based on the above, the Management considered that the Group is in a healthy financial position with sufficient working capital for its daily operations. Furthermore, the grant of the Loan is contingent upon the Group maintaining sufficient working capital and the Company has absolute discretion in determining whether to accept any drawdown request from Chuncheng Investment. Therefore, the grant of the Loan by the Company to Chuncheng Investment will not materially impact on the Group's daily operations.

Generate interest income for the Company

The grant of the Loan will enable the Company to generate a stable revenue and cashflow stream. The terms of the Loan Agreement (including the interest rate) have been negotiated on an arm's length basis between the Company and Chuncheng Investment, taking into account the prevailing market interest rates and practices. In addition, as advised by the Management, the interest rate as quoted by local commercial banks for time deposits normally ranges from 1.15% per annum to 1.35% per annum, which are lower than the interest rate of 4.5% per annum specified in the Loan Agreement. We have also performed online checking on the official websites of major commercial banks in the PRC, namely Bank of China, Industrial and Commercial Bank of China, China Construction Bank Corporation, and Agricultural Bank of China, and noted that the interest rates for time deposit with terms ranging from 1 to 5 years vary from 0.8% to 1.25% for lump-sum deposits with installment withdrawals, and from 1.05% to 2.65% for lump sum deposits with full withdrawals. These rates are below the interest rate set in the Loan Agreement. Therefore, we are of the view that the Group will benefit from receiving interest income from the Loan at a rate higher than the prevailing interest rate for time deposits in the PRC.

Having considered that (i) the funding needs of Chuncheng Investment for the Retreat Project and Transformation Project, (ii) the Group's sound liquidity position, (iii) the grant of the Loan will not have material impact on the Group's daily operations while providing stable interest income; and (iv) the interest rate under the Loan Agreement is higher than the market rate for fixed deposits offered by major commercial banks in the PRC, we concur with the Directors' view that the provision of the Loan pursuant to the Loan Agreement is in the interests of the Company and the Shareholders as a whole.

RECOMMENDATION

Having considered the above principal factors and reasons, we are of the opinion that although the entering into of the Second Assets Transfer Agreement and the Loan Agreement was not in the ordinary and usual course of business of the Group, the terms of the Second Assets Transfer Agreement and the Loan Agreement are fair and reasonable and on normal commercial terms 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 recommend the Independent Board Committee to advise the Independent Shareholders to vote in favour of the relevant resolutions for approving (i) the Second Assets Transfer Agreement and the transactions contemplated thereunder; and (ii) the Loan Agreement and the transactions contemplated thereunder at the EGM.

Yours faithfully,
For and on behalf of
Giraffe Capital Limited

Johnson Chen
Managing Director

Mr. Johnson Chen is a licensed person registered with the Securities and Futures Commission and a responsible officer of Giraffe Capital Limited to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities and to undertake work as a sponsor. He has over 16 years of experience in the field of corporate finance advisory.