



HALCYON CAPITAL LIMITED

11<sup>TH</sup> FLOOR

8 WYNDHAM STREET

CENTRAL  
HONG KONG

9 June 2022

*To the Independent Board Committee and the Independent Shareholders*

Dear Sirs,

**CONTINUING CONNECTED TRANSACTION IN RELATION TO  
THE NEW LABOR SUBCONTRACT FRAMEWORK AGREEMENT**

**INTRODUCTION**

We refer to our engagement as the independent financial adviser to the Independent

The Independent Board Committee, comprising Ms. Shen Lifeng, Ms. Chen Xin and Mr. Chan Ngai Sang Kenny, being the independent non-executive Directors, has been formed to advise the Independent Shareholders as to (i) the New Labor Subcontract Framework Agreement and its proposed annual caps (the “**Annual Caps**”) are conducted in ordinary and usual course of business of the Group, are on normal commercial terms which are fair and

and (ii) how the Independent Shareholders should vote on the relevant resolutions regarding

time they were made and continue to be so as at the date of the Circular, has been properly extracted from the relevant underlying accounting records (in the case of financial information) and made after due and careful inquiry by the Directors and/or the management of the Group. The Directors have confirmed in the Circular that, having made all reasonable enquiries, confirm that to the best of their knowledge and belief, the information contained in this 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 in this circular

misleading and we have further been confirmed by the Company that no material facts have been omitted from the information supplied and representations expressed to us. We have reviewed, among other documents, the Labor Subcontract Framework Agreement, the New Labor Subcontract Framework Agreement, the financial statements of the Company, the

*Principal business*

As stated in the 2021 Annual Report, the Group is a leading non-state owned construction group in the PRC and is principally engaged in construction contracting business and other businesses including service concession arrangements. The Group provides construction contracting services mainly as a contractor for building construction projects and

Financial statements for the period ended 31 December 2021

asset impairment losses of approximately RMB679 million and RMB976 million, respectively,

compared with that in 2020. The increase in impairment recorded was mainly attributable

to the deterioration in the credit standing of certain customers of property developers.

### Financial position

Set out below is the highlight of the financial position of the Group as at 31 December 2021 extracted from the 2021 Annual Report:

	<b>As at 31 December 2021</b>
	<i>RMB' mil</i>
Total assets	66,947
Total liabilities	61,075
Net assets	5,873

The Group recorded total assets of approximately RMB66,947 million as at 31

normal commercial terms in the ordinary and usual course of business of the Group, are fair and reasonable, and in the interests of the Group and its Shareholders as a whole.

also responsible for ensuring subcontractors in providing construction services and the labor

construction projects and infrastructure construction projects, for which Baoding Tianli  
will charge the Group total subcontract fees (including subcontract service fees, labor

fees and ancillary expenses, insurance, taxation, auxiliary materials and tools costs, etc. 1

The review panel will also take into consideration factors including, but not limited to,

historical results, as well as make reference to prevailing market terms and prices. The bidder with the highest score comprehensively determined by the review panel wins, and the bidding price offered by such bidder will be implemented.

Therefore, only in the event that Baoding Tianli and its associates win the bidding with the highest score determined by the review panel, the Group will enter into business agreements with Baoding Tianli under the New Labor Subcontract Framework Agreement.



- The Audit Committee of the Board, the office of the Board and various internal departments of the Company (including but not limited to the finance department and the legal department) will also regularly review the implementation of such framework agreement for the continuing connected transaction and the progress of the transaction

the pricing policy of such framework agreement for the continuing connected transaction on an annual basis;

We understand from the Management System and the management of the Group that

depending on the types and circumstances of connected transactions to be entered into, the  
pricing for connected transactions will not be fixed or determined by the management

relevant projects covered projects awarded to Baoding Tianli and Independent Third Parties during the two years ended 31 December 2021, we consider that these projects are

representative and the review of these projects is sufficient for the purpose of assessing

the composition of the review panels. Therefore, the risk for the awarding of contracts to be controlled by a few persons is reduced. Further, taking into account the composition of the review panel, which may involve the general managers and deputy general managers of the production safety department, operational management department, financial

based on the combined score of the two parts mentioned above. We consider that our findings is in line with the pricing policy and the Management System.

## 5. Rationale for determining the Annual Caps

The table below sets out the historical transaction amounts between the Group and Baoding Tianli in respect of the labor subcontract services under the Labor Subcontract

Framework Agreement for each of the two years ended 31 December 2021, the annual caps under the Labor Subcontract Framework Agreement for each of the three years ending 31 December 2022 and the proposed Annual Caps for each of the three years ending 31 December 2025:

	For the year ended 31 December		For the four months
	2020	2021	ended 30 April 2022
	<i>RMB 'mil</i>	<i>RMB 'mil</i>	<i>RMB 'mil</i>
Actual amount	3,455	3,835	976
Annual cap	4,000	4,000	4,000 (Note 1)
Utilisation rate	86.4%	95.9%	73.2%(Note 2)

Notes:

1 The annual cap of RMB4,000 million represents the annual cap for the year ending 31

market nationwide, the Group's labor costs are expected to remain stable in the next

three years;

- (ii) The pandemic and supply-side reform in the PRC have led to an increase in the Group's supply chain risks. In order to enhance its resistance to the Group's overall business risks arising from supply chain risks, the Group will proactively control the operation of a single labor service provider in the overall labor costs and reduce its

To assess the fairness and reasonableness of the Annual Caps, we have discussed with the management of the Company and reviewed the calculation in relation thereto. We are given to understand that the proposed annual cap for the year ending 31 December 2023 was principally determined based on (i) the labor costs of the Group which is expected to remain stable; (ii) the Group's decision and consideration of supply chain safety which aims to proactively control the proportion of a single labor service provider in the overall labor costs and reduce its reliance on a single labor service provider; (iii) the estimated total

subcontracting fees to be paid to Baoding Tianli and its associates as a percentage of the Group's labor costs which is expected to be the same as will be determined by the (iv) the

yield real-estate bonds have become uninvestable for funds with strict mandates, and the dollar bond default rate hit a record high of 4.5% as of April 2022. The increase in

default rate of real estate developers would also increase the credit risk for receivables from real estate developers. Taking into account the continuous worsening of default rate of real estate developers in the PRC and the Group had recorded significant increase in individual provision for losses in relation to certain property developers in 2021, we are of the view that it is reasonable for the Group to take up less real estate development projects in the near future. Nevertheless, further taking into account the development focus and positioning of the Group, in particular, the large-scale construction of Xiong'an New Area

(as further elaborated below) which was consistent with the increase in new contract value

On the other hand, we noted the Group's decision and consideration of supply chain safety which aims to proactively control the proportion of a single labor service provider in the overall labor costs and reduce its reliance on a single labor service provider. In assessing the reasonableness for the implementation of such control, we have obtained and

recent years and noted that the growth rate for 2018 was approximately 6.7%, and was reduced to approximately 5.9% in 2019 and 2.3% in 2020. Although the PRC has recorded a rebound in real GDP growth for 2021 to approximately 8.1% following the low GDP



and also noted that certain areas of Dordrecht were subject to lockdown measures during

the four months ended 30 April 2022. Taking into account the facts that the relevant restrictions and controls have been subsequently eased, the utilisation rate for the four months ended 30 April 2022 still exceeded 70% and it is not feasible to forecast the possibility of further outbreak of COVID-19 if any, in connection with the management of

Yours faithfully,  
for and on behalf of  
**HALCYON CAPITAL LIMITED**



**Derek C.O. Chan**  
Chairman



**Barton Lai**  
Director

*Mr. Chan is a licensed person registered with the Securities and Futures Commission and a responsible officer of Halcyon Capital Limited, which is licensed under the SFO to carry out Type 6 (advising on corporate finance) regulated activities. Mr. Chan has participated in the execution of independent financial advisory services for*