



TC Capital Asia Limited
天財資本亞洲有限公司

12 December 2012

*The Independent Board Committee and the Independent Shareholders
China Data Broadcasting Holdings Limited*

Dear Sirs,

- (1) **CONNECTED TRANSACTION AND VERY SUBSTANTIAL ACQUISITION;**
- (2) **REVERSE TAKEOVER INVOLVING A NEW LISTING APPLICATION;**
- (3) **PROPOSED GRANT OF SPECIFIC MANDATE TO ISSUE SHARES;**
- (4) **APPLICATION FOR WHITEWASH WAIVER; AND**
- (5) **CONTINUING CONNECTED TRANSACTIONS**

(I) INTRODUCTION

We refer to our appointment to act as the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders, relating to the Acquisition Agreement including the proposed grant of specific mandate to allot and issue the New Ordinary Shares, the New Convertible Preference Shares and the Conversion Shares, the application for the Whitewash Waiver and the Non-exempt Continuing Connected Transactions (including the related proposed annual caps). Details of the Acquisition Agreement, the Whitewash Waiver and the Non-exempt Continuing Connected Transactions are contained in the letter from the Board (the "**Board Letter**") in the circular to Shareholders dated 12 December 2012 (the "**Circular**"). Our letter is made for incorporation into the Circular. Capitalised terms used in this letter have the same meanings as those defined in the Circular unless the context otherwise requires.

Reference is made to the announcement dated 23 April 2012 published by the Company. On 28 March 2012, the Company as a purchaser, Fit Generation as vendor and Changhong (Hong Kong) Trading as guarantor entered into the Acquisition Agreement, pursuant to which the Company has conditionally agreed to purchase from Fit Generation, and Fit Generation has conditionally agreed to sell to the Company, the entire issued share capital of Target Co BVI, at a total consideration (the "**Consideration**") of HK\$2,012,868,000, to be settled in full by (i) as to HK\$135,000,000 by the allotment and issue of New Ordinary Shares at an issue price of HK\$1.00 per New Ordinary Share; and (ii) as to HK\$1,877,868,000 by allotment and issue of New Convertible Preference Shares at an issue price of HK\$1.00 per New Convertible Preference Share upon Completion. Changhong (Hong Kong) Trading, being the holding company of Fit Generation, has agreed to guarantee the obligations of Fit Generation under the Acquisition Agreement.

The transaction contemplated in the Acquisition Agreement constitutes a connected transaction for the Company under Chapter 20 of the GEM Listing Rules, as Fit Generation is an indirect wholly-owned subsidiary of Sichuan Changhong (which is a controlling shareholder of the Company) and hence a connected person of the Company.



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The transaction contemplated in the Acquisition Agreement also constitutes a very substantial acquisition by the Company under Chapter 19 of the GEM Listing Rules, as the calculation of the assets, profits, revenue and consideration ratios (as defined in the GEM Listing Rules) are all over 100%.

In addition, the transaction contemplated in the Acquisition Agreement constitutes a reverse takeover for the Company under Rule 19.06(6)(b) of the GEM Listing Rules, on the basis that such transaction constitutes a very substantial acquisition for the Company under Chapter 19 of the GEM Listing Rules and at the same time involve an acquisition of assets from Fit Generation (an indirect wholly-owned subsidiary of Sichuan Changhong) within 24 months of Sichuan Changhong gaining control (as defined under the Takeovers Code) of the Company.

Immediately following the allotment and issuance of the New Ordinary Shares to Fit Generation, the interest of Sichuan Changhong Concert Party Group in the Company will increase to approximately 52.53% of the enlarged issued ordinary share capital of the Company (after issuance of the New Ordinary Shares but before the conversion of any New Convertible Preference Shares).

Sichuan Changhong Concert Party Group has made an application to the Executive for and the Executive has indicated that it will grant the Whitewash Waiver from an obligation to make a general offer under Note 1 on the dispensations from Rule 26.1 of the Takeovers Code in respect of the Ordinary Shares of the Company not already owned or agreed to be acquired by Sichuan Changhong Concert Party Group. The Whitewash Waiver, if granted by the Executive, would be subject to, among other things, the approval of the Independent Shareholders at the SGM on a vote taken by poll.

Upon Completion, members of the Target Group will become subsidiaries of the Company. The Target Group has historically been involved and will continue to be involved in transactions with the Sichuan Changhong Group, which transactions after Completion will constitute continuing connected transactions for the Company under Chapter 20 of the GEM Listing Rules, as Sichuan Changhong will continue to be a connected person of the Company upon completion of the Acquisition. As certain percentage ratios under Rule 19.07 of the GEM Listing Rules in respect of the caps for the Non-exempt Continuing Connected Transactions do not fall under the exemptions in Rules 20.33 and 20.34 of the GEM Listing Rules, such Non-exempt Continuing Connected Transactions are subject to the approval of the Independent Shareholders under the GEM Listing Rules.

The Independent Board Committee, comprising all the Company's independent non-executive Directors, namely Mr. Chan Ming Sun, Jonathan, Mr. Ip Chun Chung, Robert, Mr. Sun Dongfeng and Mr. Cheng Yuk Kin, has been established to advise the Independent Shareholders on whether the terms of the Acquisition Agreement, the proposed grant of specific mandate to issue and allot the New Ordinary Shares, the New Convertible Preference Shares and the Conversion Shares, the Whitewash Waiver and the Non-exempt Continuing Connected Transactions, are fair and reasonable so far as the Independent Shareholders are concerned, and whether the entering into of the Acquisition Agreement and the Non-exempt Continuing Connected Transactions (including the related proposed annual caps) are in the interests of the Company and the Shareholders as a whole.



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In putting forth our opinion and recommendation, we have relied solely on the statements, information, opinions and representations contained in the Circular and the information and representations provided to us by the Company and its senior management. We have assumed that all such information, opinions, facts and representations, which have been provided by the Directors or representatives of the Company, for which they are fully responsible, are true, accurate and complete in all respects at the time they were made and given and continue to be true and valid as at the Latest Practicable Date. The Directors have also confirmed to us that no material facts have been omitted from the information supplied and we have no reason to suspect that any material information has been withheld by the Company or is misleading. We consider that we have sufficient information to reach an informed view and to provide a reasonable basis for our recommendation. We have not, however, for the purpose of this exercise, conducted any form of detailed investigation or audit into the businesses or affairs of the Group and Sichuan Changhong Concert Party Group nor have we carried out any independent verification of the information supplied.

We are not associated or connected with the Company, Sichuan Changhong Concert Party Group, Changhong IT, Fit Generation and their respective substantial shareholders or any party acting, or presumed to be acting, in concert with any of them and, accordingly, are considered eligible to give an independent advice on the terms of the Acquisition Agreement, the proposed grant of specific mandate to allot and issue the New Ordinary Shares, the New Convertible Preference Shares and the Conversion Shares, the Whitewash Waiver, the Non-exempt Continuing Connected Transactions and the transactions contemplated thereunder.

(II) THE ACQUISITION

Principal factors and reasons considered

In arriving at our opinion on the terms of the Acquisition, we have taken into consideration the following factors and reasons:

Background on the Group

Listed on the GEM of the Stock Exchange in January 2000, the Company is an investment holding company incorporated under the laws of Bermuda as an exempted company with limited liability on 22 September 1999. The principal business activities of the Group are (i) the trading and sales of electronic parts and components such as LCD screens, PDP screens, cathode ray tubes, integrated circuits, plugs and sockets primarily in the PRC; and (ii) the trading and sales of electrical appliances and consumer electronic products in non-PRC overseas markets.

As set out in the Company's 2011 annual report, the management of the Company will put more efforts to explore further business opportunities in related industries and will look for suitable investment opportunities to broaden the Group's business.



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Set out below is a summary of the financial results of the Group for each of the three years ended 31 December 2011 and for the nine months ended 30 September 2011 and 2012, and financial position of the Group as at 31 December 2009, 2010 and 2011 and as at 30 June 2012 extracted from “Appendix II – Financial Information of the Group” to the Circular and the Company’s 2012 third quarterly report.

Summary of financial results of the Group

	Year ended 31 December			For the nine months ended 30 September	
	2009	2010	2011	2011	2012
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	(audited)	(audited)	(audited)	(unaudited)	(unaudited)
Turnover	2,575,279	2,614,184	2,724,330	1,994,146	2,172,007
Gross profit	62,564	41,090	43,791	33,370	29,376
Profit/(loss) for the year/period	21,467	17,201	10,471	7,693	(4,364)
Profit/(loss) attributable to the owners of the Company	21,467	17,201	10,471	7,693	(4,364)
Earning/(losses) per share basic and diluted	6.75 cents	5.41 cents	3.19 cents	2.30 cents	(1.31) cents

From the above table, the turnover of the Group increased from approximately HK\$2,575 million in 2009 to approximately HK\$2,724 million in 2011, which represented an annual growth rate of approximately 1.5% and 4.2%, respectively. The turnover increased from approximately HK\$1,994 million for the nine months ended 30 September 2011 to approximately HK\$2,172 million for the nine months ended 30 September 2012, which represented a growth rate of approximately 8.9%.

For each of the three years ended 31 December 2011, the overall gross margin of the Group was 2.4%, 1.6% and 1.6%, respectively. For the nine months ended 30 September 2012, the overall gross margin was approximately 1.4%, which was dropped by approximately 0.3% comparing the corresponding period in 2011. As advised by the Company, the decrease in gross margin was mainly due to the fierce competitive in the industry as the results of global economy and politics’ instability.

The profit attributable to the owners of the Company has decreased by approximately 19.9% from approximately HK\$21.5 million in 2009 to approximately HK\$17.2 million in 2010. It was further decreased by 39.1% from approximately HK\$17.2 million in 2010 to approximately HK\$10.5 million in 2011. The profit attributable to the owners of the Company has decreased significantly from approximately HK\$7.7 million for the nine months ended 30 September 2011 to a loss of approximately HK\$4.4 million for the nine months ended 30 September 2012. Such decrease was mainly due to the payment of the professional fee for the acquisition project.



Summary of financial positions of the Group

	As at 31 December			As at
	2009	2010	2011	30 June
	HK\$'000	HK\$'000	HK\$'000	2012
	(audited)	(audited)	(audited)	(unaudited)
Total assets	803,376	566,370	516,615	509,581
Total liabilities	789,312	535,105	468,524	463,809
Total equity	14,064	31,265	48,091	45,772

As at 31 December 2010, the Group recorded total assets of approximately HK\$566.4 million (2009: HK\$803.4 million) and total liabilities of approximately HK\$535.1 million (2009: HK\$789.3 million). Total equity attributable to owners of the Company was approximately HK\$31.3 million (2009: HK\$14.1 million). Total equity amounted to approximately HK\$31.3 million (2009: HK\$14.1 million) which was attributable to the profit for the year of approximately HK\$17.2 million recorded for the year ended 31 December 2010.

As at 31 December 2011, the Group recorded total assets of approximately HK\$516.6 million (2010: HK\$566.4 million) and total liabilities of approximately HK\$468.5 million (2010: HK\$535.1 million). Total equity amounted to approximately HK\$48.1 million (2010: HK\$31.3 million) which was attributable to the profit for the year of approximately HK\$10.5 million recorded for the year ended 31 December 2011 and the increase in the share capital and share premium as a result of the issue and allotment of new Ordinary Shares to a subscriber in May 2011.

As at 30 June 2012, the Group recorded total assets of approximately HK\$509.6 million and total liabilities of approximately HK\$463.8 million. Total equity amounted to approximately HK\$45.8 million which was attributable to the loss of approximately HK\$2.3 million recorded for the six months ended 30 June 2012.

Background on the Target Group

As disclosed in the Board Letter, the Target Group is one of the top five IT distributors in the PRC, and ranked the fourth with a market share of 3.8% in terms of its sales revenue attributed to IT Hardware Products in 2011 according to the Euromonitor Report. It is principally engaged in the distribution of IT consumer products and IT corporate products in the PRC. The Target Group distributes a variety of enterprise and consumer hardware and software products in the PRC. IT consumer products distributed by the Target Group mainly include personal computers, digital products and IT accessories, while IT corporate products distributed by the Target Group mainly include storage products, minicomputers, networking products, PC servers, IBMS products, and UC & CC products. The Target Group also provides ancillary services in



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association with the distribution of IT corporate products to its customers including IT technical support services. Apart from IT consumer products and IT corporate products, it is also engaged in the distribution of smartphones and development of its self-developed products including but not limited to LBS products and provision of IT technical support services.

The Target Group has been in a relationship with renowned brand suppliers as their authorised distributor of IT consumer products and IT corporate products in the PRC ranging from four months to eight years. As of 31 July 2012, the Target Group had 33 authorized distributorships of IT products in the PRC, mainly on a non-exclusive basis. These authorized distributorships enabled the Target Group to have a stable supply of IT products for its distribution to its customers.

The Target Group maintains a network of customers with business relationships ranging from five months to eight years. It distributes IT products to various types of customers. The Target Group's major customers are mainly sub-distributors, some of which are also engaged in system integration business during the Track Record Period. It also sells its IT products to end-users. The end-users of the IT corporate products sold by the Target Group include, enterprises, government authorities, financial institutions, health authorities, education institutions, railway companies, construction companies and electricity companies in the PRC.

Set out below is a summary of the financial results of the Target Group for the Track Record Period, as well as the financial position of the Target Group as at 31 December 2009, 2010 and 2011 and as at 31 July 2012 extracted from "Appendix I – Accountants' Report on the Target Group" to the Circular.

Summary of the financial results of the Target Group

	Year ended 31 December			For the seven months ended 31 July	
	2009	2010	2011	2011	2012
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	(audited)	(audited)	(audited)	(unaudited)	(audited)
Turnover	5,204,358	8,115,756	13,357,743	6,761,560	8,439,564
Gross profit	345,918	434,702	627,819	334,300	393,209
Profit for the year/period	135,091	142,600	208,634	139,577	137,545
Profit for the year/period attributable to the owners of the Target Co BVI	134,186	133,206	188,033	125,619	123,790



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From the above table, the turnover of the Target Group increased from approximately HK\$5,204 million for the year ended 31 December 2009 to approximately HK\$13,358 million for the year ended 31 December 2011, which represented an annual growth rate of approximately 55.9% and 64.6%, respectively. The turnover increased from approximately HK\$6,762 million for the seven months ended 31 July 2011 to approximately HK\$8,440 million for the seven months ended 31 July 2012, which represented a growth rate of approximately 24.8%. The significant increases in the total turnover were mainly due to the increase in product lines and sales volume of personal computers and digital products, and the increase in suppliers and sub-distributors of the Target Group.

For each of the three years ended 31 December 2011, the overall gross margin of the Target Group was approximately 6.6%, 5.4% and 4.7% respectively. The gross margins for the seven months ended 31 July 2011 and 2012 were 4.9% and 4.7% respectively. The decrease in gross margin for the year ended 31 December 2010 and the year ended 31 December 2011 was due to higher contribution of sales from products with lower gross profit margin for the year ended 31 December 2010 and the year ended 31 December 2011.

The profit attributable to the owners of the Target Co BVI slightly decreased by approximately 0.7% from approximately HK\$134.2 million in 2009 to approximately HK\$133.2 million in 2010, and increased by 41.1% from approximately HK\$133.2 million in 2010 to approximately HK\$188.0 million in 2011. The profit for the period attributable to the owners of the Target Co BVI decreased by approximately 1.5% from approximately HK\$125.6 million for the seven months ended 31 July 2011 to approximately HK\$123.8 million for the seven months ended 31 July 2012.

Summary of financial positions of the Target Group

	The Target Group			As at
	As at 31 December			31 July
	2009	2010	2011	2012
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	(audited)	(audited)	(audited)	(audited)
Total assets	1,293,280	2,154,680	2,865,748	2,951,566
Total liabilities	885,564	1,600,459	2,274,778	2,233,530
Total equity	407,716	554,221	590,970	718,036

As at 31 December 2010, the Target Group recorded total assets of approximately HK\$2,154.7 million (2009: HK\$1,293.3 million) and total liabilities of approximately HK\$1,600.5 million (2009: HK\$885.6 million). Total equity was approximately HK\$554.2 million (2009: HK\$407.7 million).



As at 31 December 2011, the Target Group recorded total assets of approximately HK\$2,865.7 million (2010: HK\$2,154.7 million) and total liabilities of approximately HK\$2,274.8 million (2010: HK\$1,600.5 million). Total equity was approximately HK\$591.0 million (2010: HK\$554.2 million).

PRC electronic information industry

Year	Sale revenue from the main businesses of the electronic information industry	Annual Growth	Sale revenue from the business of the sector of computer	Annual Growth
	(in RMB billion)	(%)	(in RMB billion)	(%)
2011	7,490.9	17.7%	2,167.6	15.2%
2010	6,364.5	24.1%	1,881.6	20.5%
2009	5,130.5	0.1%	1,561.7	-8.9%
2008	5,125.3	12.9%	1,713.4	7.3%
2007	4,540.0		1,596.9	

Source: The website of The Ministry of Industry and Information Technology (the "MIIT") of the PRC (www.miit.gov.cn)

Based on the information from the MIIT, we have calculated the compound annual growth rate (the "CAGR") of the sales revenue from the main businesses of the electronic information industry, which is approximately 13.3% between 2007 and 2011. According to the twelfth "Five-year plan", the PRC government has targeted to maintain the annual growth rate of the sales revenue from the main businesses of the electronic information industry at around 10% and such sales revenue will exceed RMB10 trillion by 2015. As illustrated in the above table, the sales revenue from the main businesses of the electronic information industry has maintained double-digit annual growth rates between 2007 and 2011, except during the global recession period in 2009.

The MIIT has further categorized the aforesaid PRC electronic information industry into 11 sub-sectors. Among these sub-sectors, there is a sub-sector, known as the "Computer", which is directly related to the principal businesses of both the Group and Target Group. We have also calculated the CAGR of the sales revenue from this sub-sector, which is approximately 7.9% between 2007 and 2011.

The twelfth "Five-year plan" also outlines that the PRC government has categorized the information industry as one of the strategic emerging industries for innovative development (戰略性產業創新發展工程). As forecasted by the Euromonitor Report as detailed in the section headed "Industry Overview" in the Circular, the IT product market in the PRC is expected to have a modest growth, to reach RMB421,313 million in terms of retail values in 2017, with a CAGR of 5.1% from 2012 to 2017, which will be mainly driven by the favourite PRC government's policy, the expanding market of sub-urban area and technology development.



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Although there is only a modest growth in the IT product market in the PRC as predicted by MIIT and Euromonitor, having considered the fierce competition in the industry and the Acquisition enables the Company to substantially increase its operating scale, we consider it is fair and reasonable and in the interests of the Company and its Shareholders as a whole.

Potential conflict of interest

We note that the Company, Sichuan Changhong and Sichuan Changhong Electric (the controlling shareholders of the Company) have been engaging in the similar trading and distribution business before the Acquisition. As a result, potential business competition amongst the parties had existed. As stated in the paragraph “Non-compete Undertakings”, under the section headed “Relationship with the Controlling Shareholders” in the Circular, in order to address any future competition between the respective trading and distribution business of Sichuan Changhong Group and the Enlarged Group, Sichuan Changhong, Sichuan Changhong Electric and Fit Generation, the controlling shareholders of the Company have entered into the Deed of Non-Competition in favour of the Company for itself and on behalf of its subsidiaries.

Under the Deed of Non-Competition, Sichuan Changhong Group will undertake that it shall not, directly or indirectly (whether as principal or agent, through any body corporate, partnership, joint venture or other contractual arrangement and whether for profit or otherwise) carry on, engage, invest or be interested or otherwise involved in the Restricted Business with the exceptions as stated in the paragraph “Non-compete Undertakings” under the section headed “Relationship with the Controlling Shareholders”.

Furthermore, as disclosed in the paragraphs “Independence from Controlling Shareholders” under the section headed “Relationship with Controlling Shareholders” in the Circular, with a view to further addressing the potential competition issues with the businesses among Sichuan Changhong Group, Sichuan Changhong Electric Group and the Enlarged Group, upon completion of the Acquisition, the Company and Sichuan Changhong Group will enter into arrangements such that, among other things:

- (1) Delineation of business – the principal businesses of the Enlarged Group will include the Group’s existing business comprising the CDB Component Business and the CDB Electronic Business, as well as the Target Group’s Target Existing Business comprising Target IT Business and the Target Mobile Business;
- (2) Geographical delineation – it has been agreed between the Company and Sichuan Changhong that they will segregate the current overlapping non-PRC overseas markets for the sales and distribution of electrical appliances and consumer electronic products. The Company will focus its CDB Electronic Business in CDB’s Markets. For the non-PRC overseas markets of the Changhong Electronic Business, the Sichuan Changhong Group will focus in Changhong’s Markets;



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Furthermore, pursuant to the Deed of Non-Competition, Sichuan Changhong has undertaken that it will cease its Changhong Electronic Business in CDB's Markets within 18 months upon Completion. The Company will also cease its CDB Electronics Business in Changhong's Markets within 18 months upon Completion. For the Market Opportunity, it has been agreed that the Enlarged Group shall have the right of first refusal to pursue such Market Opportunity. In deciding whether to pursue the Market Opportunity, the Company will seek approval from its independent non-executive Directors. The material terms relating to the Market Opportunity will be reviewed by the independent non-executive Directors.

- (3) Price segment and brand delineation – it has been agreed that any competition between the Changhong Mobile Business and the Target Mobile Business will be minimized upon Completion through price segment and brand delineation in mobile phones, pursuant to which the Sichuan Changhong Group and the Enlarged Group will focus on mobile products in different price segments. The Sichuan Changhong Group will continue to focus in own-branded products while the Enlarged Group will focus in smartphones of other brands.

Pursuant to the Deed of Non-Competition, after Completion, the Enlarged Group will focus in the distribution of smartphones with the unit retail price equal to or above RMB2,500 and the Sichuan Changhong Group (excluding the Enlarged Group) will focus in the distribution of mobile phones with the unit retail price equal to or below RMB1,500.

Sichuan Changhong Group's obligations under these arrangements are in addition to their obligation and reinforcement under the Deed of Non-Competition, and Sichuan Changhong Group will not interfere with any decision to be made by the Company under these arrangements. In addition to the above, as part of the Company's corporate governance measures, the Group has established its corporate governance practice manual that the Enlarged Group will adopt, review and update from time to time and pursuant to which an independent board committee will be established to deal with matters involving conflict of interests.

Given the above, we concur with the Director's view that the above arrangements would effectively reduce the potential competition issues between the Enlarged Group and Sichuan Changhong Group.

While the Deed of Non-Competition is in place, we believe that the interest of the Enlarged Group will be well protected even when the overlapping of directors and senior management exists between the two groups. In view of the adequate safeguard measures that are in place to protect the interests of the Enlarged Group, we are of the opinion that the Acquisition is fair and reasonable and in the interests of the Company and Shareholders as a whole.



Reasons for and benefits of the Acquisition

According to the Board Letter contained in the Circular, the Target Group is a key player in the IT products distribution business in the PRC, principally engaged in the distribution of IT consumer products and IT corporate products. The Group is expected to benefit from the Acquisition in the following principal aspects:

1. The Acquisition will benefit from the sustainable growth of the IT products industry in considering the following factors:
 - (i) the historical CAGR of approximately 13.3% of sales revenue from the main businesses of the electronic information industry in the PRC between 2007 and 2011 based on the MIIT information;
 - (ii) the twelfth “Five-year plan” in encouraging and supporting the development of electronic information industry with the target of around 10% annual growth rate;
 - (iii) the historical CAGR of approximately 7.9% of sales revenue from the sub-sector of computer in the PRC between 2007 and 2011 based on the MIIT information; and
 - (iv) the forecasted CAGR of 5.1% for the IT product market by Euromonitor Report between 2012 and 2017.
2. The Acquisition will create synergy to the Group’s existing business as it facilitates the Group to penetrate into the IT products industry. The overall competitiveness of the Group will also be strengthened as the Acquisition will:
 - (i) increase the scale of operations and strengthen its business and financial strength, thereby better positioning the Group for future business development and operations;
 - (ii) expand the business segments and products distributed by the Group to reach more diversified markets, in order to reduce its business fluctuations;
 - (iii) increase the Group’s competitiveness in the IT industry; and
 - (iv) share the expertise in the management team of the Target Group for the Enlarged Group’s IT products business.
3. Upon Completion, the Company’s operation scale will significantly increase. As reported in the unaudited pro forma financial information of the Enlarged Group contained in Appendix III to the Circular, assuming Completion has taken place on 1 January 2011, the turnover of the Group as an Enlarged Group for the year ended 31 December 2011 will be increased from HK\$2,724.3 million to HK\$16,082.1 million, representing approximately 4.9 times increase in the operation scale in term of the turnover.



The Consideration will be fully settled by the issue of New Ordinary Shares and New Convertible Preference Shares, and will not result in any reduction in the Group's bank deposit and cash equivalent. Though there is a dilution effect to the existing public Shareholders brought about by the Acquisition, the Acquisition will create synergy for the Group's existing IT product industry as discussed above. The Group's income base will also be broadened through the Acquisition. As such, we are of the view that the dilution effect on the shareholdings of the public Shareholders is acceptable. The Directors also believe that the Acquisition will generate greater future income for the Enlarged Group that may compensate the dilution impact to the existing public Shareholders.

The details of the dilution effect will be further discussed under the section headed "Dilution effect of the issue of the New Ordinary Shares and Conversion Shares on the shareholding structure of the Company" below.

Having considered the above reasons and benefits, we are of the view that the Acquisition is in line with the Company's strategy to explore further business opportunities and broaden its business through participating in suitable investment opportunities in related industries as discussed above under the paragraph headed "Background on the Group". We concur with the Directors' view that the Acquisition is fair and reasonable so far as the Independent Shareholders are concerned and is in the interests of the Company and its Shareholders as a whole.

Principal terms of the Acquisition Agreement

Set out below is a summary of the salient terms of the Acquisition Agreement:

Date	:	28 March 2012
Parties	:	1. The Company, as purchaser; 2. Fit Generation, as vendor; and 3. Changhong (Hong Kong) Trading, as guarantor.
Subject matter	:	The Company has conditionally agreed to purchase from Fit Generation, and Fit Generation has conditionally agreed to sell to the Company, the entire issued share capital of Target Co BVI.
Guarantor	:	Changhong (Hong Kong) Trading, being the holding company of Fit Generation, has agreed to guarantee the obligations of Fit Generation under the Acquisition Agreement.
Consideration	:	The total Consideration is approximately HK\$2,012,868,000, which is to be settled in full (i) as to HK\$135,000,000 by the allotment and issue of New Ordinary Shares at an issue price of HK\$1.00 per New Ordinary Share; and (ii) as to HK\$1,877,868,000 by the allotment and issue of New Convertible Preference Shares at an issue price of HK\$1.00 per New Convertible Preference Share to Fit Generation upon Completion.



Conditions precedent : Completion of the Acquisition is conditional upon the satisfaction or waived (as the case may be) of the following conditions:

- (i) each of the covenants, agreements and obligations of Fit Generation to be performed and complied with on or prior to the Completion Date in accordance with the Acquisition Agreement having been duly performed or complied with in all respects on or before Completion Date;
- (ii) the warranties given by Fit Generation under the Acquisition Agreement being true and accurate and not misleading in all material respects on and as of the Completion Date, as though they had been given and made on such date by reference to the facts and circumstances then subsisting;
- (iii) the approval by the Independent Shareholders at the SGM by way of a poll of (i) the Acquisition; (ii) the proposal for grant of the specific mandate to allot and issue the New Ordinary Shares, the New Convertible Preference Shares and the Conversion Shares; (iii) the Whitewash Waiver; and (iv) the Non-exempt Continuing Connected Transactions and the proposed annual caps on the value of such transactions in accordance with the requirements of the GEM Listing Rules;
- (iv) if applicable, the approval of the transaction contemplated in the Acquisition Agreement being obtained from the sole shareholder of Changhong (Hong Kong) Trading in accordance with the applicable laws and the requirements of the Shanghai Stock Exchange or other supervisory or regulatory body to which Sichuan Changhong is subject;
- (v) in respect of the Target Group, all necessary licences, consents, approvals, authorisations, permissions, waivers, orders, exemptions or notifications (if any) which are required and appropriate for the execution and performance of the Acquisition Agreement and the transaction contemplated under the Acquisition Agreement having been obtained or made from or to relevant third parties and/or governmental or regulatory authorities or bodies, and not having been revoked prior to completion of the Acquisition;
- (vi) the approval in principle of the Listing Committee of the Stock Exchange of the New Listing Application and the grant of the Whitewash Waiver by the Executive being obtained by the Company;



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- (vii) the Listing Committee of the Stock Exchange agreeing to grant (subject to allotment) the listing of, and permission to deal in, the New Ordinary Shares and the Conversion Shares (and such permission and listing not subsequently being revoked);
- (viii) between the date of the Acquisition Agreement and Completion Date, no event or series of events shall have occurred which has had or would reasonably be expected to have a material adverse effect (as defined in the Acquisition Agreement on the Target Group); and
- (ix) no person having instituted or threatened any action or investigation to restrain, prohibit or otherwise challenge the transaction contemplated by the Acquisition Agreement.

The above conditions are required to be fulfilled (or, waived as the case may be) on or before the Long Stop Date. The Company may waive conditions (i), (ii) (in respect of the warranties given by Fit Generation only), (v) and (viii) and Fit Generation may waive condition (ii) (in respect of warranties given by the Company only). If the above conditions have not been satisfied or waived on or before such date, save as expressly provided in the Acquisition Agreement, the Acquisition Agreement shall lapse, and neither the Company nor Fit Generation shall have any claim against the other, save for any claim arising from the breach by any party of its obligation to fulfill the relevant conditions precedent.

On 27 September 2012, the Company and Fit Generation signed a letter for the extension of the Long Stop Date, pursuant to which the parties mutually agreed to extend the Long Stop Date from 28 September 2012 to 31 December 2012, or at such later date as may be mutually agreed between the Company and Fit Generation in writing.

On 6 December 2012, the Company and Fit Generation signed another letter for the further extension of the Long Stop Date, pursuant to which the parties mutually agreed to further extend the Long Stop Date from 31 December 2012 to 28 February 2013, or at such later date as may be mutually agreed between the Company and Fit Generation in writing.

As at the Latest Practicable Date, none of the above conditions precedent have been satisfied.



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Completion : Completion of the Acquisition is expected to take place on the fifth Business Day from and excluding the day set out in the condition precedents abovementioned have been satisfied or waived (as the case may be) or such time, date and place as may be mutually agreed by the Company and Fit Generation.

Evaluation of the Consideration

As disclosed in the Board Letter, the Consideration of approximately HK\$2,012,868,000 has been arrived at after arms' length negotiations between the parties having regard to, amongst others, the price-to-earnings ratio (the "**P/E Ratio**") of the average P/E Ratio of companies listed in Hong Kong whose principal activities are similar to the present business of the Group and the Target Group, based on the audited consolidated net profit of Changhong IT and its subsidiaries after taxation and extraordinary items for the financial year ended 31 December 2011, the financial and operational track record of the Target Group, the prospects of the industry in which the Target Group operates in, the rationale for the Acquisition, and the benefits to the Group following Completion.

In forming our opinion on the fairness and reasonableness of the Consideration, we have considered the commonly adopted comparable approaches used in determining a company's value, namely the P/E Ratio, price-to-book ratio (the "**P/B Ratio**") and price-to-sales ratio (the "**P/S Ratio**"). While P/E Ratio is a more accurate measurement and one of the most commonly used valuation ratio, it is unable to price loss-making companies, or companies experiencing unusually low profit which create exaggerated ratios. Therefore, P/B Ratio and P/S Ratio, while not as accurate as pricing mechanisms as they are meant for asset-heavy industries or start-ups respectively, they do provide a useful reference point to ensure the accuracy and reliability of the P/E Ratio. We have reviewed and compared the P/E Ratios, P/B Ratios and P/S Ratios of companies listed on the Stock Exchange, which the turnover generated from the distribution of electronic products and IT products in the PRC and Hong Kong representing more than half of their respective total turnover as reported in their respective latest annual reports.

On a best effort basis, we have identified 11 listed companies (including the Company) on the Stock Exchange (the "**Comparable Companies**"), being an exhaustive list, as at 28 March 2012, being the last trading day immediately prior to the suspension of trading in the Ordinary Shares (the "**Last Trading Day**") with their respective principal business of trading and distribution of electronic products and IT products in the PRC and Hong Kong. Although the Comparable Companies may have differences including principal business activities, stage of development, geographical location, market segment, operation scale and market capitalization as compared to the Target Group, we consider that the Comparable Companies, in general, serve as fair and representative samples. The business of trading and distribution of electronic products and IT products in the PRC and Hong Kong are somewhat similar in nature regardless of their individual uniqueness as this business activity is represented by low margins high volume, where distribution cost represents a major cost component aside from the cost of each products. Therefore, having a similar business structure, the Comparable Companies are able to provide a general landscape for evaluating the Target Group. We have excluded one company which has its share suspended for trading for more than two years and up to the Latest Practicable Date,



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as its prolonged suspended share price does not reflect the current market price. In calculating the average P/E Ratio, P/B Ratio and P/S Ratio, we have excluded the highest and lowest values of the P/E Ratio, P/B Ratio and P/S Ratio among the Comparable Companies, as these extreme values may be caused by the share price fluctuation, business cycle and/or accounting adjustment, which will distort the calculation. The following table sets forth certain details of the Comparable Companies.

Company	Stock code	Principal business	Market capitalisation (HK\$ million) (Note 1)	P/E Ratio (Note 2)	P/B Ratio (Note 3)	P/S Ratio (Note 4)
China Data Broadcasting Holdings Ltd.	8016	Trading of consumer electronic products and the related parts and components	581	54.5	12.1	0.2
Futong Technology Development Holdings Ltd.	465	Provision of IT solutions, distribution of enterprise IT products and provision of IT technical support services in the PRC	361	4.1	0.6	0.1
CIL Holdings Ltd.	479	Providing comprehensive solutions and distribution of server storage, multi-media and communication products	362	NA (Note 5)	21.4	1.3
SiS International Holdings Ltd.	529	Distribution of IT products; and property investment	936	1.4	0.5	0.7
EC-Founder (Holdings) Co. Ltd.	618	Distribution of information products	299	NA (Note 6)	0.9	0.1
Automated Systems Holdings Ltd.	771	IT products and information technology services	349	7.8	0.7	0.2
VST Holdings Ltd.	856	Distribution of information technology products and provider of enterprise systems and IT services	2,306	5.1	0.8	0.1
Digital China Holdings Ltd.	861	Sale and distribution of general information technology products and systems products; and provision of supply chain services and information technology services	16,719	15.9	2.5	0.3



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Company	Stock code	Principal business	Market capitalisation (HK\$ million) (Note 1)	P/E Ratio (Note 2)	P/B Ratio (Note 3)	P/S Ratio (Note 4)
Artel Solutions Group Holdings Ltd.	931	Distribution of computer components and information technology products and trading of securities	867	102.7	3.6	140.6
Mobicon Group Ltd.	1213	Trading and distribution of electronic parts, components and equipment, and computer products and accessories	138	11.9	0.7	0.2
Average				16.5	2.7	0.4
Median				9.8	0.9	0.2
Maximum				102.7	21.4	140.6
Minimum				1.4	0.5	0.1
Target Group at the Consideration (Note 7)			2,013	9.6	3.3	0.2

Sources: Bloomberg, www.hkex.com.hk and latest annual reports of the respective Comparable Companies

Notes:–

- The market capitalisation of the Comparable Companies is calculated based on the respective Comparable Companies' closing price sourced from the Bloomberg and number of issued shares of the respective Comparable Companies available from the website of the Stock Exchange as at the Last Trading Day.
- P/E Ratio is based on the market capitalisation of the respective Comparable Companies as at the Last Trading Day divided by the net profit of the respective Comparable Companies in their respective latest annual reports.
- P/B Ratio is based on the market capitalisation of the respective Comparable Companies as at the Last Trading Day divided by the latest published book value of the respective Comparable Companies in their respective latest annual reports.
- P/S Ratio is based on the market capitalisation of the respective Comparable Companies as at the Last Trading Day divided by the turnover of the respective Comparable Companies in their respective latest annual reports.
- CIL Holdings Ltd. has recorded net loss for the year ended 31 December 2011 and therefore the P/E Ratio is not available.
- EC-Founder (Holdings) Co. Ltd. has recorded net loss for the year ended 31 December 2011 and therefore the P/E Ratio is not available.
- The amount represents the valuation of the Target Group based on the Consideration of HK\$2,012,868,000.



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Based on the respective closing prices of the shares of the Comparable Companies as at the Last Trading Day, the P/E Ratios of the Comparable Companies range from approximately 1.4 times to approximately 102.7 times, with an average of approximately 16.5 times and a median of approximately 9.8 times. The implied P/E Ratio of the Acquisition of approximately 9.6 times is lower than the average as well as the median of the P/E Ratios of the Comparable Companies calculated based on the closing price of shares of the Comparable Companies as at the Last Trading Day.

Based on the respective closing prices of the shares of the Comparable Companies as at the Last Trading Day, the P/S Ratios of the Comparable Companies range from approximately 0.1 times to approximately 140.6 times with an average of approximately 0.4 times and a median of approximately 0.2 times. The implied P/S Ratio of the Acquisition is approximately 0.2 times which is lower than the average of the P/S Ratios of the Comparable Companies calculated based on the closing price of shares as at the Last Trading Day, while it is the same as the median of the P/S Ratios of the Comparable Companies.

As the ranges of the P/E Ratios and the P/S Ratios of the Comparable Companies are wide, main consideration has been given to the average P/E Ratio and P/S Ratio for our comparison and evaluation purposes. The medians of the P/E Ratio and P/S Ratio are also adopted such that the effect of the wide spread of discount and premium amongst the Comparable Companies would be minimized.

Accordingly, in light of (1) comparing with the P/E Ratios of the Comparable Companies, the P/E Ratio implied by the Consideration is lower than both of the average and median values; and (2) comparing with the P/S Ratios of the Comparable Companies, the P/S Ratio implied by the Consideration is lower than the corresponding average value and equal to the median value, we are of the view that the Consideration is fair and reasonable so far as the Independent Shareholders are concerned, and in the interests of the Company and Shareholders as a whole.

The issue price of the New Ordinary Shares and the New Convertible Preference Shares

Pursuant to the Acquisition Agreement, the total Consideration is approximately HK\$2,012,868,000, which is to be settled in full (i) as to HK\$135,000,000 by the allotment and issue of New Ordinary Shares at an issue price of HK\$1.00 per New Ordinary Share; and (ii) as to HK\$1,877,868,000 by the allotment and issue of New Convertible Preference Shares at an issue price of HK\$1.00 per New Convertible Preference Share to Fit Generation upon Completion. The issue price of HK\$1.00 per both the New Ordinary Share and New Convertible Preference Share represent:

- (i) a discount of approximately 42.53% to HK\$1.74, the closing price of the Ordinary Shares on the Stock Exchange on the Last Trading Day;
- (ii) a discount of approximately 42.53% to approximately HK\$1.74, the average closing price of the Ordinary Shares on the Stock Exchange for the last 10 full trading days prior to the suspension of trading in the Ordinary Shares;



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- (iii) a discount of approximately 42.86% to approximately HK\$1.75, the average closing price of the Ordinary Shares on the Stock Exchange for the last 30 full trading days prior to the suspension of trading in the Ordinary Shares;
- (iv) a premium of approximately 614.29% over approximately HK\$0.14, the audited consolidated net asset value of the Group per Ordinary Share as at 31 December 2011; and
- (v) a discount of approximately 39.76% to HK\$1.66, the closing price of the Ordinary Shares on the Stock Exchange on the Latest Practicable Date.

The price at which the New Ordinary Shares and the New Convertible Preference Shares to be issued was determined after arm's length negotiations between the Company and Fit Generation with reference to, among other factors, the financial position of the Group, the historical trading volume of the Ordinary Shares on GEM, the historical trading prices of the Ordinary Shares on GEM and the consolidated net asset value of the Group per Ordinary Share as at 31 December 2011. Based on the closing price of HK\$1.66 per Ordinary Share as at the Latest Practicable Date, the total market values of the New Ordinary Shares and the New Convertible Preference Shares are approximately HK\$224,100,000 and HK\$3,117,260,880, respectively.

The New Ordinary Shares will be issued as fully paid and will rank pari passu in all respects with the Ordinary Shares in issue at the Completion Date. The Conversion Shares will be issued upon conversion of the New Convertible Preference Shares as fully paid and will rank pari passu in all respects with the Ordinary Shares in issue as at the date of conversion.

In assessing the fairness and reasonableness of the issue price of both the New Ordinary Shares and New Convertible Preference Shares, we have conducted the analyses on the historical trading performance of the Ordinary Shares and compared the issue prices of the comparable transactions. Details of which are set forth below:

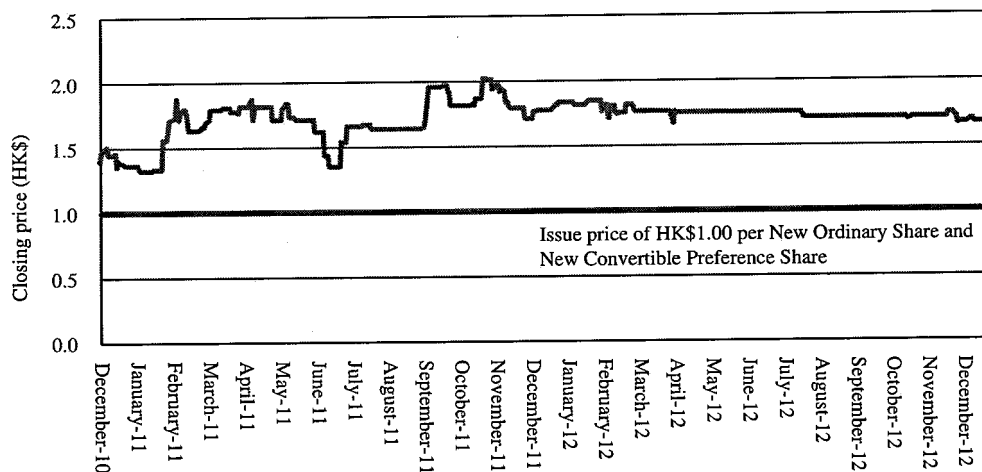
(a) *Share price performance and comparison with the issue price of the New Ordinary Shares and New Convertible Preference Shares*

The chart sets up below illustrates the movement of the closing price for the Ordinary Shares during the period from December 2010, up to and including the Latest Practicable Date (the "**Review Period**"). We consider such 24-month Review Period to be reasonable as it should be able to cover at least one fiscal year or the existence of any



12-month cyclical cycle. The Review Period can also capture the market price trend of the Ordinary Shares given the volatility of the general stock market during the Review Period:

Shares price performance of the Company



Source: Bloomberg

The trading in the Ordinary Shares has been suspended since 29 March 2012 and had resumed in the trading on 24 April 2012. The closing price of the Ordinary Shares has remained most of the time at HK\$1.74 after resumption, which was above the issue price of the New Ordinary Shares and the New Convertible Preference Shares with a few actual tradings in the Ordinary Shares during the period from 24 April 2012 (the first trading day after the publication of the Announcement dated 28 March 2012) to the Latest Practicable Date. The price of the Ordinary Share has remained relatively stable since 24 April 2012 up to the Latest Practicable Date. We are of the view that this relatively stable price is due to low trading volume of the Ordinary Shares since 24 April 2012.

During the Review Period, the Ordinary Shares were traded within the range of HK\$1.32 and HK\$2.00 per Ordinary Share, which compared to the issue price of both the New Ordinary Shares and New Convertible Preference Shares represent a discount of 24.24% to 50.00%. When compared to the closing price of the Ordinary Share as at the Latest Practicable Date, the discount is approximately 39.76%. We are of the view that the issue price of both the New Ordinary Shares and New Convertible Preference Shares represents a significant discount to the price of the Ordinary Shares.



(b) Analysis of the trading volume

The following table shows the highest and lowest daily trading volume, the average daily trading volume, the number of trading days with volume higher than 100,000 Ordinary Shares and the percentage of average daily trading volume over the total number of the Ordinary Shares in issue during the Review Period:

Month	Highest daily trading volume (in number of Ordinary Shares)	Lowest daily trading volume (in number of Ordinary Shares)	Average daily trading volume (in number of Ordinary Shares)	Number of trading days	Percentage of average daily trading volume
				in a month with trading higher than 100,000 Ordinary Shares (in days)	over total number of Ordinary Shares in issue (note 1) (%)
2012					
December (up to the Latest Practicable Date)	10,000	0	2,000	0	0.001%
November	170,000	0	13,455	1	0.004%
October	37,000	0	3,450	0	0.001%
September	0	0	0	0	0.000%
August	0	0	0	0	0.000%
July	6,000	0	345	0	0.000%
June	0	0	0	0	0.000%
May	0	0	0	0	0.000%
April	0	0	0	0	0.000%
March	10,000	0	1,818	0	0.001%
February	81,000	0	23,381	0	0.007%
January	22,260,000	0	1,243,760	1	0.372%
2011					
December	12,000	0	1,600	0	0.000%
November	226,000	0	33,500	1	0.010%
October	30,000	0	6,500	0	0.002%
September	68,000	0	17,950	0	0.005%
August	8,000	0	348	0	0.000%
July	44,000	0	2,500	0	0.001%
June	16,000	0	1,905	0	0.001%
May	128,000	0	11,900	1	0.004%
April	22,000	0	4,833	0	0.001%
March	80,000	0	11,130	0	0.003%
February	232,000	0	54,556	2	0.016%
January	408,000	0	22,238	1	0.007%



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Month	Highest daily trading volume <i>(in number of Ordinary Shares)</i>	Lowest daily trading volume <i>(in number of Ordinary Shares)</i>	Average daily trading volume <i>(in number of Ordinary Shares)</i>	Number of trading days in a month with trading higher than 100,000 Ordinary Shares <i>(in days)</i>	Percentage of average daily trading volume over total Ordinary Shares in issue <i>(note 1)</i> <i>(%)</i>
2010					
December	62,000	0	8,111	0	0.002%
Average			58,611		0.018%

Source: Bloomberg

Note:

1. Based on the total number of 334,000,000 Ordinary Shares as at the Latest Practicable Date.

As shown in the above table, the Ordinary Shares were thinly traded during the Review Period. The average daily trading volume was approximately 58,611 Ordinary Shares, representing approximately 0.018% of the issued share capital of the Company as at the Latest Practicable Date. In January 2012, the daily trading volume was significantly higher when comparing to other months during the Review Period. As disclosed in the announcement dated 20 January 2012, Mr. Ji Long Fen, a Director of the Company, traded 22,260,000 Ordinary Shares in the open market to a third party and therefore, resulted in the exceptional high average daily trading volume during the month within the Review Period.

We noted that that average daily trading volume by month of the Ordinary Shares during the Review Period accounted for only a small portion of the issued share capital of the Company, ranging from nil to approximately 1,243,760 Ordinary Shares. With January 2012 excluded, the average daily trading volume range from nil to 54,556. This average daily highest trading volume of Ordinary Shares represents only 0.016% of the issued share capital of the Company as at the Latest Practicable Date. Hence, liquidity issue will arise for anyone attempting to dispose of a large quantity of Ordinary Shares. This poor liquidity nature the Ordinary Shares represents a huge risk, particularly to owners of large quantity of Ordinary Shares, as any attempt to realise the value of the Ordinary Shares may drive down the Ordinary Share price significantly.

Therefore, in accepting the New Ordinary Shares and the New Convertible Preference Shares as consideration, Fit Generation has been given a discount on the issue price by the Company. We are of the view that providing a discount due to illiquid shares is fair and reasonable, as it is a common approach taken by the market. While providing a discount due to poor liquidity is a common practice, we are unable to ascertain if the amount of discount is fair and reasonable as explained in our analysis below.



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(c) *Comparison with the listed companies which issued new shares and/or convertible preference shares*

The following summary table illustrates an exhaustive list of 7 comparable companies listed on the Stock Exchange, which (i) issued circular regarding very substantial acquisition under the Listing Rules; (ii) the transaction involved application for the Whitewash Waiver; (iii) shareholders' approval has been obtained at the shareholders' meeting; and (iv) issued new shares and/or convertible preference shares as consideration (the "Comparable Shares"), during the Review Period with the issue price of new shares and/or convertible preference shares, compared to their respective closing price on the last trading day. We consider such Review Period to be reasonably long and any extended period over the Review Period may include older data which may not reflect on the current market conditions. As the Consideration involves the issuance of both the New Ordinary Shares and New Convertible Preference Shares, we believe that the Comparable Shares would provide a benchmarking comparison for our analysis in determining the issue price of the New Ordinary Shares and New Convertible Preference Shares. Although each of the Comparable Shares may be subjected to different principal activities, transaction terms, financial standings, business performance, issuance scale and dilution impact, we consider that the premium or discount of the Comparable Shares, serve as fair and representative samples because these approved transactions involve the issuance of shares or convertible securities under a very substantial acquisition and a Whitewash Waiver, which raise liquidity issues for the vendors of the transactions for each of the Comparable Shares. These reasons, coupled with the approval of shareholders, make the transactions of the Comparable Shares representative of the market in general.

Date of circular	Company	Stock code	Premium over/ (discount to) the closing share price on the last trading day (Note 1) (%)	Liquidity (Note 2) (%)
16 November 2012	EC-Founder (Holdings) Company Limited	618	(0.0)%	0.6%
29 December 2011	China Daye Non-Ferrous Metals Mining Limited	661	(15.3)%	6.1%
31 October 2011	Shanghai Industrial Urban Development Group Limited	563	(3.8)%	2.3%
25 May 2011	Madax International (Holdings) Limited	231	1.9%	3.3%
25 February 2011	Golden Resorts Group Limited (Note 3)	1031	(3.6)%	2.4%
31 December 2010	Tianjin Tianlian Public Utilities Company Limited (Note 4)	8290	(15.0)%	1.9%
14 December 2010	Lumena Resources Corporation (Note 5)	67	7.5%	27.3%
Average			(4.0)%	6.3%
Median			(3.6)%	2.4%
Maximum			7.5%	27.3%
Minimum			(15.3)%	0.6%
12 December 2012	The Company	8016	(42.5)%	0.3%

Sources: www.hkex.com.hk and Bloomberg



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Notes:

1. Last trading day refers to the respective last trading day for the Comparable Shares specified in their respective circulars.
2. The liquidity is calculated by the average monthly trading volume during the Review Period divided by the total number of issue shares as at the respective latest practicable dates of each Comparable Shares.
3. Golden Resorts Group Limited has changed its company name to Kingston Financial Group Limited with effect from 6 May 2011 and its stock code remains unchanged.
4. Tianjin Tianlian Public Utilities Company Limited had transferred the listing of its shares from the GEM to the Main Board of the Stock Exchange on 18 October 2011 under the stock code of 01265. Tianjin Tianlian Public Utilities Company Limited has changed its company name to Tianjin Jinran Public Utilities Company Limited with effect from 21 September 2012 and its stock code remains unchanged.
5. Lumena Resources Corporation has changed its company name to China Lumena New Materials Corporation with effect from 8 December 2010 and its stock code remains unchanged.
6. Companies in distress and suspended for prolonged period of time have been excluded from the table.

As indicated from the table above, we note that the issue price of the Comparable Shares have an average discount of approximately 4.0% and a median of approximately 3.6%. When compared to the discount of the New Ordinary Shares and the New Convertible Preference Shares, the discounts of Comparable Shares are much lower, implying that the discount on the New Ordinary Shares and the New Convertible Preference Shares is higher than usual. While the discount on the New Ordinary Shares and the New Convertible Preference Shares is on the high end, it should also be noted that the liquidity of the Shares is at the extreme low end. Liquidity of the Comparable Shares average is about 6.3% with the lowest being 0.6% and the highest being 27.3%. These low and high percentages represent approximately 6,300,000 and 529,000,000 shares of the Comparable Shares traded on a monthly basis, respectively. The Company's liquidity, on the other hand, average about 0.32% with approximately 1,000,000 Ordinary Shares traded per month. If the trade of 22,260,000 Shares executed by Mr. Ji Long Fen to an independent third party is to be excluded from the calculation, the liquidity of the Company would drop to 0.05% with average monthly volume of approximately 183,000. This is equivalent to daily trading volume of approximately 9,145 Shares or 0.003% of the Ordinary Shares issued in total. Trading of the Shares is so low that there are many days in a month where the Ordinary Shares were never traded.

Given the analysis of the comparison set out above, the issue prices of the New Ordinary Shares and New Convertible Preference Shares, which is at a discount of 42.5% to the closing price of the Ordinary Shares on the Last Trading Day, is not fair and reasonable compared to the Comparable Shares when taken solely on a pricing discount basis. However, in considering the liquidity of the Ordinary Shares, which is unusually



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low and the size of the issue of the New Ordinary Shares and the New Convertible Preference Shares, which could result in 2,012,868,000 Shares to be issued, we are of the opinion that on the basis of low liquidity and the sheer size of the New Ordinary Shares and the New Convertible Preference Shares, a discount should be given to compensate the party accepting the New Ordinary Shares and the New Convertible Preference Shares as a consideration. While the pricing discount on the New Ordinary Shares and the New Convertible Preference Shares is substantial, we could not confirm or deny if such discount is within market standard.

Based on the Comparable Shares table above, there is no precedent case whereby a company whose shares have minimal to no liquidity, issues substantial number of shares or instruments convertible in to shares as consideration for acquisition. Therefore, the Comparable Shares are only useful as a reference and not a comparable, and there is no direct comparable that could be used to determine the fairness and reasonableness of the discount of the New Ordinary Shares and the New Convertible Preference Shares. We have, for the purpose of determining this fairness and reasonableness, discussed the discount and its determination with the Company. According to the Company, the discount was determined after arm's length negotiations between the Company and Sichuan Changhong, taking into account various factors, including but not limited to liquidity and size of the transaction. Having considered (i) the poor liquidity of the Ordinary Shares; (ii) the large number of Ordinary Shares to be issued or convertible relative to its trading volume; and (iii) there is a lack of comparable market information for shares with low liquidity, we are unable to form an opinion if the price and the discount on the price determined based on an arm's length negotiation, after taking into consideration the aforementioned factors, is fair and reasonable, and in the interests of the Company and Shareholders as a whole. However, having considered that upon Completion, the pro forma earnings per Ordinary Share and the pro forma net asset value per Ordinary Share will be significantly improved as discussed in the section headed "Financial effects of the Acquisition on the Group" below, we are of the view that the discount on the New Ordinary Shares and New Convertible Preference Shares is fair and reasonable, and in the interests of the Company and Shareholders as a whole.

Settlement of Consideration

The Consideration for the Acquisition will be satisfied by the allotment and issuance of New Ordinary Shares and New Convertible Preference Shares to Fit Generation, details of which is contained within the Board Letter. While settling the Consideration in other forms, such as cash or borrowings, would provide no dilution impact to the Company, it will not be easy for the Company to raise HK\$2,012,868,000 in cash. As disclosed in the 2012 interim report, the cash and bank balance of the Group is HK\$176,196,000, which is unable to settle the full Consideration, as a result, utilising internally generated cash would on the other hand put significant stress onto the operating cashflow of the Company. As such, settlement of the Consideration by way of issuing the New Ordinary Share and the New Convertible Preference Shares is fair and reasonable and in the interests of the Company and Shareholders as a whole.



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Dilution effect of the issue of the New Ordinary Shares and Conversion Shares on the shareholding structure of the Company

The interests of the existing Independent Shareholders will be diluted from approximately 35.15% to approximately 25.02% upon issue of the New Ordinary Shares but before conversion of any of the 1,877,868,000 New Convertible Preference Shares. As the full conversion of the New Convertible Preference Shares will bring the Company's public float down to 5% and result in the Company failing to meet the minimum public float requirement of the GEM Listing Rules, Fit Generation has undertaken to the Company that they will only exercise the conversion rights as to such number of New Convertible Preference Shares if, upon conversion, the percentage of the Ordinary Shares held by the public will still meet the minimum public float requirement of the GEM Listing Rules of 25%. We consider the level of dilution to the existing Independent Shareholders (i) upon issue of the New Ordinary Shares but before conversion of any New Convertible Preference Shares; and (ii) upon issue of the New Ordinary Shares and full conversion of the New Conversion Preference Shares significant and not in the interests of Independent Shareholders.

However, in consideration of the following reasons:

(a) *Opportunity to participate in a much larger business*

Given the proven track record and the historical growth in profitability of the Target Group, the Independent Shareholders will be able to participate in a much larger business with significantly greater revenue base, improved earnings capability and growth prospects.

(b) *Synergistic growth opportunities of the Group and Target Group*

With the merger of the Group and the Target Group, the Enlarged Group can obtain the assistance from the each other in strategically expanding (i) the current sales network and coverage; (ii) the supply and procurement networks for the consumer electronic products, IT products and electronic parts and components in order to increase its bargaining power and competitive advantage; and (iii) the product range and scope of business, which will not only broaden the revenue bases of the Group, but will also allow the Group to strength and further widen its offering of consumer electronic products, IT products and related business and consequently its reputation in the PRC.

(c) *Ease of funding for the Acquisition*

The allotment and issue of the New Ordinary Shares and the New Convertible Preference Shares to satisfy the Consideration is an easier way to fund the Acquisition. This method is favourable to the Company as it enables the Group to make an acquisition of a very significant size without a large outlay of cash, but involves the issue of a substantial number of New Ordinary Shares and New Convertible Preference Shares with dilution consequence to the Independent Shareholders.



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(d) Difficulty in raising cash for the Acquisition

Dilution to the Independent Shareholders could be avoided if a rights issue or an open offer is conducted to raise capital for the Acquisition. However, having considered the extremely low trading volume and the size of the offer needed to fully settle the Consideration, it is unlikely that arm's length underwriters and the Independent Shareholders would be attracted to participate in a rights issue or an open offer on the same quantum and terms as the New Ordinary Shares and New Convertible Preference Shares based on our experience and discussions with various independent brokerage firms.

(e) Cheaper alternative to raise cash

In view of the difficulty in raising cash to settle the Acquisition as mentioned above, the cost of funds from any attempts to raise cash would be prohibitively high, hence rendering the Acquisition impossible or very costly.

Based on the above reasons, we are of the view that it is inevitable but acceptable for the Company to issue the New Ordinary Shares and New Convertible Preference Shares as the Consideration. Upon considering the benefits of an Enlarged Group from all perspectives, we are of the opinion that the Acquisition and the dilution effect to the existing Independent Shareholders (i) upon issue of the New Ordinary Shares but before conversion of any New Convertible Preference Shares; and (ii) upon issue of the New Ordinary Shares and full conversion of the New Conversion Preference Shares are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

Financial effects of the Acquisition on the Group

(a) Net profit

Following Completion, the Target Co BVI will become a directly wholly-owned subsidiary of the Company, and the assets, liabilities and financial results of the Target Co BVI will be consolidated into the financial statements of the Group. Based on the unaudited pro forma financial information of the Enlarged Group contained in the Appendix III to the Circular prepared based on the income statement of the Group and the Target Group for the year ended 31 December 2011, the Enlarged Group's consolidated total comprehensive income attributable to the Shareholders would be substantially increased from approximately HK\$10.5 million to approximately HK\$201.8 million, representing an increase of approximately 18 times, as if the completion of the Acquisition has taken place on 1 January 2011.

Independent Shareholders should note that the aforesaid pro forma statement is prepared based on the historical financial figures of the Target Group. Therefore, there is no assurance that the future performance of the Target Group will be similar to those historical figures as reported in the unaudited pro forma financial information of the Enlarged Group contained in Appendix III to the Circular. Shareholders are advised to read the section headed "Risk Factors" contained in the Circular which describes the risks relating to the Acquisition, the Enlarged Group, the Target Group's business and the industry in which the Target Group operates.



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(b) Earnings per share

Assuming Completion has taken place on 1 January 2011, the pro forma earnings per Ordinary Share of the Enlarged Group would become HK\$0.38 per Ordinary Share (based on a total of 469,000,000 Shares after the issuance of the New Ordinary Shares following the Acquisition and assuming no New Convertible Preference Shares have been converted), and approximately HK\$0.08 per Ordinary Share (based on a total of 2,346,868,000 Shares after the issue of the New Ordinary Shares and full conversion of all New Convertible Preference Shares), as compared to the earnings per Ordinary Share of the Group of approximately HK\$0.03 for the year ended 31 December 2011 (based on 334,000,000 Ordinary Shares in issue). Adjustment has been made to take into consideration of the professional fees of the Acquisition incurred. Shareholders are advised to note that the pro forma earnings per Ordinary Share of the Enlarged Group was prepared for illustrative purpose and may not reflect the actual financial positions and results of the operation of the Group.

(c) Net assets

Upon Completion, the financial results of the Target Group will be consolidated into the Group's account. As shown in the unaudited pro forma financial information of the Enlarged Group as set out in Appendix III to the Circular, assuming the Completion had taken place on 30 June 2012, the net asset value attributable to the Shareholders will be substantially increased from approximately HK\$45.8 million to approximately HK\$744.9 million. The pro forma net asset value per Ordinary Share will be increased from approximately HK\$0.14 to approximately HK\$0.32 as at 30 June 2012 (based on a total of 2,346,868,000 Shares after the issuance of the New Ordinary Shares and full conversion of all New Convertible Preference Shares). The above shows that the Acquisition is likely to have a positive impact on the Group's net assets base per Ordinary Share, as if Completion has taken place on 30 June 2012.

(d) Gearing and working capital

Upon Completion, the Enlarged Group's equity base would be enlarged by the issuance of the New Ordinary Shares and the New Convertible Preference Shares. According to the unaudited pro forma financial information of the Enlarged Group as set up in Appendix III to the Circular, the Group's total assets would increase from HK\$509.6 million to HK\$3,442.2 million, while the total liabilities would increase from HK\$463.8 million to HK\$2,697.3 million. Gearing ratio as at 30 June 2012, calculated as the total liabilities divided by the total assets, would decrease from approximately 91.0% to approximately 78.4% as if the Completion has taken place on 30 June 2012.



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(III) WHITEWASH WAIVER

Immediately upon Completion, the interest of Sichuan Changhong Concert Party Group in the Company will increase from approximately 33.34% to approximately 52.53% of the enlarged issued share capital of the Company (excluding the Conversion Shares to be issued by the Company upon the conversion of the New Convertible Preference Shares) and approximately 90.51% of the enlarged issued ordinary share capital of the Company (including the Conversion Shares to be issued by the Company upon the full conversion of the New Convertible Preference Shares). Accordingly, Sichuan Changhong Concert Party Group will be obligated to make an unconditional mandatory general offer for all the issued Shares of the Company not already owned by them and persons acting in concert with them under Rule 26.1 of the Takeovers Code. An application has been made to the Executive for the Whitewash Waiver. The Whitewash Waiver, if granted by the Executive, would be subject to, among other things, the approval of the Independent Shareholders at the SGM on a vote taken by poll.

As discussed in the paragraph headed “Principal terms of the Acquisition Agreement” above, the Acquisition is conditional on, among other things, the approval of the Whitewash Waiver by the Independent Shareholders at the SGM. If the Whitewash Waiver is not approved, the Acquisition will not proceed and no general offer obligation will be triggered. In the event the Acquisition cannot proceed, the Group and the Shareholders will not be able to enjoy the benefits that would arise from the Acquisition and the possible enhancement in the Group’s net asset value and earnings capability as discussed above.

Given the aforementioned potential benefits of the Acquisition to the Group and the terms of the Acquisition being fair and reasonable so far as the Independent Shareholders are concerned, we are of the opinion that the approval of the Whitewash Waiver, which is a prerequisite for the completion of the Acquisition, is in the interests of the Company and the Shareholders as a whole.

Shareholders should note that upon Completion, Sichuan Changhong Concert Party Group will hold more than 50% of the enlarged issued share capital of the Company. Accordingly, Sichuan Changhong Concert Party Group may increase its shareholdings in the Company without incurring any further obligation under Rule 26 of the Takeovers Code to make a general offer.

(IV) CONTINUING CONNECTED TRANSACTIONS

(a) Beijing Lease

Introduction

According to the Circular, on 16 May 2012, Changhong IT entered into the Beijing Lease, which was supplemented by a supplement agreement on 6 July 2012 with Beijing Changhong, pursuant to which Beijing Changhong has leased the Beijing Property to Changhong IT for a term of five years, with an option to terminate by Changhong IT upon three years after its commencement on 1 June 2012. Upon Completion, the above lease arrangement will constitute a continuing connected transaction of the Company.



Pursuant to Rule 20.35 of the GEM Listing Rules, the duration of the agreement must not exceed three years, except in special circumstances which are limited to cases where the nature of the transactions requires the agreement to be of duration longer than three years. We are required to explain on why leasing longer period for the Beijing Lease is required to exceeding three years, and to confirm that it is normal business practice for these types of leasing contracts to be of such duration.

Reasons for The Beijing Lease with a Duration Exceeding Three Years

As set out in the Circular, the Beijing Property will be used as Changhong IT's headquarters office in Beijing. We have discussed with the management of Changhong IT the rationale for the duration of the Beijing Lease, and were given to understand the following factors and reasons for such duration as follows:

- (1) the five-year duration of Beijing Lease for the office premise will enable the Changhong IT to prevent the frequent recurrence of expensive initial set-up costs such as renovation and interior decoration, which the Enlarged Group will invest on the Beijing Property in order to occupy the said premises;
- (2) the supplement agreement entered on 6 July 2012 provides an option for Changhong IT to terminate the Beijing Lease upon three years after its commencement on 1 June 2012. This option may allow greater flexibility for the Enlarged Group to choose other offices if better opportunities arisen in the future; and
- (3) the ability for Changhong IT to lock in the rental rates of the Beijing Property for a period of five years is in the interest of the Company and Shareholders a whole, as the rental rates within the city of Beijing and the vicinity of the Beijing Property has been rising in the last few years. Based on the information presented within the "Global Market Perspective – First Quarter 2012", a quarterly publication by Jones Lang LaSalle, the rental price for office property in Beijing is in a rising trend and is expected to continue growing over the next few years. Furthermore, availability ratio of grade A office space is expected to drop, due to the limited supply, and will lead to an increase in rent and shifting some of the demand into secondary locations. In view of the demand of office space in Beijing and the potential increase in rent, we are of the view that the entering into of a long-term leasing agreement will allow the Changhong IT to lock in the current rental rates and prevent further increase in rental rates over the next five years.

In considering whether it is normal business practice for the leasing agreements of office to have duration longer than three years, we have reviewed a comparable transaction involving the lease of office space in the same building as the Beijing Property. We noted that the lease under the aforesaid comparable transaction was also for a term of five years. We have also confirmed with the building management office of the Beijing Property that it is their normal business practice to enter into tenancy agreement with tenure exceeding 3 years.



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The following table illustrates the comparisons between the Beijing Lease and the comparable lease we have reviewed:

	Beijing Lease	Comparable lease
Duration of the leasing (years)	5	5
Leasing area (sq.m.)	6,348	550
Leasing price (RMB/sq.m.)	828	1,008
Leasing floor	7-12	5

Save for the above, the remaining terms of the leasing agreement under the aforesaid comparable transaction is about the same to the Beijing Lease.

Having considered the principal factors and reasons referred in the above, we are of the view that the Beijing Lease with duration of more than three years is required, and is normal business practice for these types of leasing contracts to be of such duration, and the entering into of the Beijing Lease is fair and reasonable so far as the Independent Shareholders are concerned, and is in interests of the Company and Shareholders as a whole.

(b) Framework Agreements

Introduction

The Group and the Target Group have historically been involved and will continue to be involved in transactions with the Sichuan Changhong Group. Upon Completion, members of the Target Group will become subsidiaries of the Company and the Enlarged Group will continue to have certain transactions that constitute connected transactions within the meaning of the GEM Listing Rules.

On 7 December 2012, the Company (on behalf of the Enlarged Group) has entered into the Framework Agreements with Sichuan Changhong for a term from Completion to 31 December 2015, in order to set out the basis upon which members of the Enlarged Group will, after Completion, continue to engage in transactions with the Sichuan Changhong Group as part of the Enlarged Group's business.

Based on the applicable percentage ratios (under Rule 19.07 of the GEM Listing Rules), the transactions contemplated under the Framework Agreements for a term ending 31 December 2015 constitute continuing connected transactions of the Company under the Rules 20.45 to 20.54 of the GEM Listing Rules, which are subject to reporting, announcement and Independent Shareholders' approval requirements.



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Principal factors and reasons considered

In arriving at our opinion and recommendations to the Independent Board Committee and Independent Shareholders in relation to the Non-exempt Continuing Connected Transactions under the Framework Agreements, we have taken into consideration the following factors and reasons:

Background of the Framework Agreements

(i) Background of the relevant parties

a. Sichuan Changhong Group

As set out in the Circular, the Sichuan Changhong Group is currently one of the largest PRC consumer electronics products providers specialising in research & development, manufacturing and marketing of consumer electronic products.

b. The Group

Please refer to the section headed "Background on the Group" above within the letter of TC Capital.

c. The Target Group

Please refer to the section headed "Background on the Target Group" above within the letter of TC Capital.

(ii) Background of and reasons for entering into the Framework Agreements

The Group has been carrying out transactions with the Sichuan Changhong Group under the Framework Agreements and previous supply and purchase agreements since 2007. On 20 November 2009, the Company entered into the Existing Master Supply Agreement with Sichuan Changhong in respect of the supply of the Group Supply Products to certain members of the Sichuan Changhong Group. On the same date, the Company had entered into the Existing Master Purchase Agreement in relation to the purchase of the Group Purchase Products from certain members of the Sichuan Changhong Group on an ongoing basis, which the agreements will expire on 31 December 2012.

Under the Existing Master Purchase Agreement, the Group has purchased certain consumer electronic products such as televisions, air-conditioners and fridges from the Sichuan Changhong Group. As discussed with the Group, the Group is the preferential agent for Sichuan Changhong Group's Changhong Electronic Business in overseas markets and all the consumer electronic products purchased were used for re-selling purpose as the Group is in the business of trading of consumer electronic products. The Group is able to use its own bankable assets, such as developed overseas networks, to become the preferential agent of Sichuan Changhong Group for overseas markets, which is in line with the interests of the Company and Shareholders.



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Under the Existing Master Supply Agreement, the Group has supplied electronic products and components such as LCD screens, PDP screens, integrated circuits, cathode ray tubes, voltage regulators, plugs and sockets to the Sichuan Changhong Group.

The Existing Master Purchase Agreement, the Existing Master Supply Agreement and the relevant annual caps for the period from 1 January 2010 to 31 December 2012 were approved by the Independent Shareholders at SGM that held on 29 December 2009. Further details of the Existing Master Purchase Agreement, the Existing Master Supply Agreement as contemplated thereunder are set out in the circular of the Company dated 10 December 2009.

The Target Group has supplied various consumer electronic products and IT products such as servers, notebooks, storage devices and network equipment to certain members of the Sichuan Changhong Group, who are in the businesses of trading of consumer electronic and IT products. On the other hand, the Target Group has purchased from the Sichuan Changhong Group consumer electronic products such as LBS Products manufactured at its specific request from time to time as part of its own-brand products division of its business for sales in the PRC. As the Target Group does not manufacture these products, the Target Group has to purchase them from Sichuan Changhong Group. As disclosed by the Target Group, approximately 80.4% of products purchased from Sichuan Changhong Group were used for re-selling and the remaining 19.6% were for self-use as of 2011.

As discussed with the Target Group, the followings are the reasons and benefits of the Target Group in the sales and purchases with the Sichuan Changhong Group:

- (1) in light of the long-established and close working relationship between the Target Group and the Sichuan Changhong Group, and the understanding of each other's operations and practices, it lowers the counter-party risk in supplying and purchasing materials and services to and from any independent third parties;
- (2) the Target Group is able to obtain a favorable pricing condition with satisfied quality of products from the Sichuan Changhong Group; and
- (3) the reliability of the supply of products to and from the Sichuan Changhong Group has been established. Accordingly, the New Master Supply Agreement ensures the continuity and stability of the Company's production and operation, which has a positive impact in terms of operational integration and geographical convenience.

To conclude, with reference to the reasons and benefits mentioned above, we are of the view that the necessity for the counter-parties sales and purchases between the Target Group and the Sichuan Changhong Group is fair and reasonable and in the best interests of the Shareholders.



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Upon Completion, members of the Target Group will become subsidiaries of the Company. In order to regulate the relationship between the Enlarged Group and the Sichuan Changhong Group with respect to the supply of products by the Enlarged Group to the Sichuan Changhong Group and the purchase of products by members of the Enlarged Group from members of the Sichuan Changhong Group in the future after Completion, the Company and Sichuan Changhong have entered into the New Master Supply Agreement and the New Master Purchase Agreement, collectively known as Framework Agreements, on 7 December 2012.

The New Master Supply Agreement shall replace the Existing Master Supply Agreement (with effect from the Completion Date) and prescribes the framework terms upon which the Company shall and shall procure the relevant members of the Enlarged Group to provide, and Sichuan Changhong shall and shall procure the relevant members of the Sichuan Changhong Group to purchase the Enlarged Group Supply Products and such other products as the Company and Sichuan Changhong may agree from time to time commencing on the Completion Date and ending on 31 December 2015.

The New Master Purchase Agreement shall replace the Existing Master Purchase Agreement (with effect from the Completion Date) and prescribes the framework terms upon which Sichuan Changhong shall and shall procure the relevant members of the Sichuan Changhong Group to provide, and the Company shall and shall procure the relevant members of the Enlarged Group (which includes Changhong IT) to purchase the Enlarged Group Purchase Products and such other products as the Company and Sichuan Changhong may agree from time to time commencing on the Completion Date and ending on 31 December 2015.

In arriving at our view, we have considered the following factors in regard of entering into the Framework Agreements:

a. Major customer and supplier of the Group

As disclosed in the Company's 2011 annual report, during the year ended 31 December 2011, the five largest customers were Sichuan Changhong and its subsidiaries accounted for approximately 67.47% of the total sales, while two of the five largest suppliers were the Sichuan Changhong and its subsidiaries which accounted for 32.22% of the total purchases.

b. Lower counter-party risk

The Group has been carrying out transactions with the Sichuan Changhong Group under the Existing Master Supply Agreement and previous supply agreement since 2007. In light of the long-term established and solid relationship between the Enlarged Group and various suppliers of products that are required by the Sichuan Changhong Group, and the understanding of each other's operations and practices, it lowers the counter-party risk in supplying to and from any Independent Third Parties.



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As advised by the Company, based on the previous experiences under the Existing Master Purchase Agreement, the Sichuan Changhong Group is able to deliver quality products in a timely manner. Having reliable and cooperative suppliers through the New Master Purchase Agreement will enable the Enlarged Group to be able to source for more customer orders, improve its sales orders and expand its business.

c. Established network by the Enlarged Group

As of 31 December 2011, the Sichuan Changhong Group imported more than US\$1 billion worth of electronic parts and components from overseas via independent agents, and purchased more than HK\$20 million worth of IT products such as computers, servers, notebooks, storage devices and network equipment etc. from other independent suppliers. The Enlarged Group has established long term and solid relationships with various suppliers of products that are required by the Sichuan Changhong Group, and therefore, the Enlarged Group will be able to capitalize on such established relationships to procure the products required by the Sichuan Changhong Group and in turn increase the income of the Enlarged Group with a committed source of purchase orders from the Sichuan Changhong Group through the New Master Supply Agreement.

d. Risk associated with the reliance on few customers

Although the Sichuan Changhong Group is the largest customer and one of the major suppliers of the Group, the Group will continue to source its products from other suppliers and distribute its products to various customers to avoid over-reliance on the Sichuan Changhong Group. As the Group will from time to time consider further acquisitions of companies should suitable opportunities arise, such acquisitions will further increase the Target Group's customer and supplier bases and hence reduce the risk of reliance on few customers and suppliers.

For further details of the risks faced by the Target Group, please refer to the section headed "Risk Factors" in the Circular.

Having considered the aforesaid factors and the business nature of the Company and the Sichuan Changhong Group, we are of the view that the Framework Agreements are entered in the ordinary and usual course of business of the Company, and in the interests of the Company and its Shareholders as a whole.



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(1) Supply of consumer electronic products, IT products and electronic parts and components by the Enlarged Group to the Sichuan Changhong Group

Principal terms of the New Master Supply Agreement

Pursuant to the terms of the New Master Supply Agreement, the Enlarged Group will supply the Enlarged Group Supply Products between the Enlarged Group and Sichuan Changhong. Details of the principal terms of the New Master Supply Agreement are set out in the Circular.

Pricing

As advised by the Company that the prices of the Enlarged Group Supply Products under the New Master Supply Agreement shall be determined and negotiated based on normal commercial terms and with reference to the prevailing fair market prices of comparable products, and such prices shall be no less favourable to the Enlarged Group than that available from Independent Third Parties. There should be no minimum orders and it is not necessary for the Enlarged Group to supply the Sichuan Changhong Group products unless orders are made by members of the Sichuan Changhong Group.

Payment terms

Pursuant to the New Master Supply Agreement, payment by Sichuan Changhong depends on the products to be supplied and volume, and the time of delivery for each transaction. It is generally expected to be made by telegraphic transfer payable within 35 to 45 days from the date of delivery or irrevocable letter of credit.

In this regard, we have obtained and reviewed a number of the contracts and invoices in respect of the historical transactions between the Group and Sichuan Changhong, and the Group and Independent Third Parties. We note that the terms of the contracts with Sichuan Changhong, in particular the pricing and settlement terms are no less favourable to the Group than the terms offered to Independent Third Parties, which we consider are fair and reasonable, on normal commercial terms and are in the interests of the Company and its Shareholders as a whole.

Settlement

We have reviewed the 2009, 2010 and 2011 annual reports of the Company and the information provided by the Group in respect of subsequent settlement. The ratio of delay in settlement by Sichuan Changhong was approximately 0.79% as of 31 December 2011, and no bad debt provision has been made. Accordingly, we consider that the settlement term by Sichuan Changhong is acceptable, fair and reasonable and in the interests of the Company and its Shareholders as a whole.



Basis of determination of the proposed annual caps ending 31 December 2015 regarding the New Master Supply Agreement

As disclosed in the Circular, the proposed aggregate annual caps for the three years ending 31 December 2015 under the New Master Supply Agreement are determined with reference to:

- (i) the historical transactions conducted and transaction amounts in respect of the Target Group's and the Group's supply of products to the Sichuan Changhong Group;
- (ii) the Target Group's estimated approximate 10% year-on-year increase in annual sales of IT products to the Sichuan Changhong Group based on the Sichuan Changhong Group's expected needs and projected increase in revenue and growth of its business in view of the increase in demand and the expansion of customer base in the consumer electronics and IT products markets in the PRC; and
- (iii) the value of the actual supply by the Group to the Sichuan Changhong Group in 2010 and 2011 under the Existing Master Supply Agreement, and the anticipated increase in demand by the Sichuan Changhong Group assuming that the supply of electronic components and products to the Sichuan Changhong Group by the Enlarged Group in the three years ending 31 December 2015 will have an increase of approximately 10% per year.

In determining the fairness and the reasonableness of the proposed aggregate annual caps for the three years ending 31 December 2015 under the New Master Supply Agreement, we have considered the following factors:

– *Historical transactions conducted and the transaction amounts*

The table below sets forth (i) the historical aggregate transaction amounts and historical annual caps under the Existing Master Supply Agreement for the Track Record Period; and (ii) the proposed annual caps of the aggregated transactions contemplated under the New Master Supply Agreement ending 31 December 2015:

	Historical transaction amounts				Historical annual caps for			Annual caps for the year		
	for the year ended 31 December			for seven months	the year ended 31 December			ending 31 December ^(Note 1)		
	2009	2010	2011	ended 31 July	2009	2010	2011	2013	2014	2015
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Supply of the Target Group Supply Products	12,958	23,305	18,598	26,946	-	-	-	22,504	24,754	27,230
Supply of the Group Supply Products	1,776,680	1,553,588	1,991,262	987,076	2,184,000	2,090,000	2,299,000	2,409,427	2,650,370	2,915,407
Total	1,789,638	1,576,893	2,009,860	1,014,022	2,184,000	2,090,000	2,299,000	2,431,931	2,675,124	2,942,637



Note:—

1. The proposed annual caps for the three years ending 31 December 2015 represent the “Supply of the Enlarged Group Supply Products” under the New Master Supply Agreement.

The utilization rates of the annual caps for the year 2009, 2010 and 2011, are calculated based on the historical transaction amounts divided by the annual caps of the respective years. These rates range from approximately 74% to 87% indicating that these historical annual caps have been determined and utilised to a reasonable level. The CAGR of the total historical transactions between 2009 and 2011 is approximately 6%. The Company estimates the annual growth rate for the year ending 2013 is expected to be approximately 10% and continues to maintain steadily at 10% in 2014 and 2015.

– *Expected business growth of the Sichuan Changhong Group*

As discussed with the Company, the estimated increases in the annual sales of IT products and the electronic components and products by the Target Group and the Group, respectively, to the Sichuan Changhong Group have been determined with reference to the Sichuan Changhong Group’s expected business growth. As disclosed in the Sichuan Changhong Group’s 2007, 2008, 2009, 2010 and 2011 annual reports, the CAGR of its turnover between 2007 and 2011 is 22.5%, while the CAGR of its IT products segment alone during the same period is 40.5%.

– *Prospects of the PRC’s electronic information industry*

As discussed in the section headed “PRC electronic information industry” before, we have reviewed the Electronic Information Industry Statistical Bulletins 2007-2011 (2007-2011年電子資訊產業統計公報) published by the MIIT, the calculated CAGR of the sales revenue from the main businesses of the electronic information industry as well as the sub-sector of “Computer”, which are approximately 13.3% and 7.9% between 2007 and 2011, respectively. Moreover, the PRC government has targeted to maintain the annual growth rate of the sales revenue from the main businesses of the electronic information industry at around 10% until 2015 according to its twelfth “Five-year plan”. Euromonitor has also forecasted the IT product market with the CAGR of 5.1% between 2012 and 2017.

Having considered the factors and discussed above, in particular, (i) the historical growth rates and the transaction amounts; (ii) the expected business growth of the Sichuan Changhong Group; and (iii) the continuous growth of the consumer electronics and IT products markets of the PRC, we are of the view that the aggregate annual caps contemplated under the New Master Supply Agreement, and the expected annual supply value growth of 10% in determining the 2013, 2014 and 2015 aggregate annual caps, are fair and reasonable so far as the Independent Shareholders are concerned, and in the interests of the Company and Shareholders as a whole.



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(2) Purchase of consumer electronic products by the Enlarged Group from the Sichuan Changhong Group

Principal terms of the New Master Purchase Agreement

Pursuant to the terms of the New Master Purchase Agreement, the Enlarged Group will purchase the Enlarged Group Purchase Products and such other products from the Sichuan Changhong Group. Details of the principal terms of the New Master Purchase Agreement are set out in the Circular.

Pricing

As advised by the Directors that the prices of the Enlarged Group Purchase Products under the New Master Purchase Agreement shall be determined and negotiated based on normal commercial terms and with reference to the prevailing fair market prices of comparable products, and such prices shall be no less favourable to the Enlarged Group than that available from the Independent Third Parties.

Payment terms

Pursuant to the New Master Purchase Agreement, payment by the Company depends on the products to be purchased and volume, and the time of delivery for each transaction. It is generally expected to be made by telegraphic transfer payable within 35 to 45 days from the date of delivery or by transferable letter of credit.

In this regard, we have obtained and reviewed a number of the contracts, purchasing orders and invoices of the Company for the purchases from Sichuan Changhong and the Independent Third Parties for the purchase of similar electronic components and products. We note that the terms of the contracts with Sichuan Changhong, in particular the pricing of materials and payment terms are no less favourable to the Company than the terms available from the Independent Third Parties, which we consider are fair and reasonable, on normal commercial terms and in the interests of the Company and its Shareholder as a whole.

Basis of determination of the annual caps ending 31 December 2015 regarding the New Master Purchase Agreement

As disclosed in the Circular, the proposed aggregate annual caps ending 31 December 2015 under the New Master Purchase Agreement are determined with reference to:

- (i) the historical transactions conducted and transaction amounts in respect of the Enlarged Group's purchase of the Enlarged Group Purchase Products from the Sichuan Changhong Group;
- (ii) the Enlarged Group's overall projected demand for products from the Sichuan Changhong Group based on its business expansion plans; and



- (iii) the value of the actual purchase by the Group from the Sichuan Changhong Group in 2010 and 2011 under the Existing Master Purchase Agreement, and the anticipated increase in demand by the Group's customers assuming that the purchase of electronic products from the Sichuan Changhong Group by the Enlarged Group in the three years 31 December 2015 will have an increase of approximately 10% per year.

In determining the fairness and the reasonableness of the annual caps, we have considered the following factors:

– *Historical annual caps under the Existing Master Purchase Agreement*

The table below sets forth (i) the historical aggregate value of purchase of products and historical annual caps under the Existing Master Purchase Agreement for the Track Record Period; and (ii) the proposed aggregate annual caps under the New Master Purchase Agreement ending 31 December 2015:

	Historical transaction amounts for				Historical annual caps for			Annual caps for the year		
	the year ended 31 December		the seven months ended 31 July		the year ended 31 December			ending 31 December ^(Note 1)		
	2009	2010	2011	2012	2009	2010	2011	2013	2014	2015
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Purchase of the Target Group Purchase Products	4,570	4,121	495	19	-	-	-	599	659	725
Purchase of the Group Purchase Products	1,160,050	1,323,062	924,262	492,387	1,250,000	1,375,000	1,512,500	1,118,357	1,230,193	1,353,212
Total	1,164,620	1,327,183	924,757	492,406	1,250,000	1,375,000	1,512,500	1,118,956	1,230,852	1,353,937

Note:—

- The proposed annual caps for the three years ending 31 December 2015 represent the "Purchase of the Enlarged Group Purchase Products" under the New Master Purchase Agreement.

The utilization rates of the annual caps for the years 2009, 2010 and 2011, are calculated based on the historical transaction amounts divided by the annual caps of the respective years. These rates range from approximately 61% to 96% indicating that these historical annual caps have been determined and utilised to a reasonable level. While the CAGR of the total historical transaction amounts between 2009 and 2011 shows a negative growth rate, the historical transaction amounts fluctuated to a high of HK\$1,327.2 million in 2010 and a low of HK\$924.8 million in 2011. We note that the proposed 2013, 2014 and 2015 aggregate annual caps of the New Master Purchase Agreement are higher than the historical transactions in 2009,



2010 and 2011. Having considered the factors and discussed above, in particular, (i) the transaction amounts where a buffer is required to meet the possibility of large fluctuations; (ii) the historical transaction amounts under the Existing Master Purchase Agreement; (iii) the expected business growth under the Enlarged Group's future business plan; (iv) the approximately 13.3% historical CAGR of the sales revenue from the main businesses of the electronic information industry; and (v) the approximately 10% targeted growth rate of the consumer electronics and IT products markets of the PRC under the twelfth "Five-year Plan", we are of the view that it is fair and reasonable to determine the 2013, 2014 and 2015 aggregate annual caps based on the historical transaction amounts incorporating buffers and expected business growth. Consequently, we are of the view that the 2013, 2014 and 2015 aggregate annual caps contemplated under the New Master Purchase Agreement, and the expected annual purchase value growth of 10% in determining the 2013, 2014 and 2015 aggregate annual caps, are fair and reasonable so far as the Independent Shareholders are concerned, and in the interests of the Company and Shareholders as a whole.

– *Expected business growth of the Enlarged Group*

As discussed with the Company regarding the future plan of the Enlarged Group, the Company decides to expand the product varieties and the business, including expansion of the PDP products and IT products services businesses through the Acquisition. The Company also seeks for the opportunities for the development of IT products and consumer electronic products business in the developing regions, such as the South East Asia, South America and Africa.

– *Prospects of the PRC's electronic information industry*

After reviewing the Electronic Information Industry Statistical Bulletins 2007-2011 (2007-2011年電子資訊產業統計公報) published by the MIIT, we have calculated the CAGR of the sales revenue from the main businesses of the electronic information industry, which is approximately 13.3% between 2007 and 2011. Moreover, the PRC government has targeted to maintain the annual growth rate of the sales revenue from the main businesses of the electronic information industry at around 10% till 2015 according to the twelfth "Five-year plan".

We also notice that there is a decrease of approximately 30% in the historical transaction amount in 2011 when compared to that of 2010. As discussed with the Company, the decrease was mainly due to the weak global economy, the unstable atmosphere brought by the European debt crisis and the unstable political environment in the Middle East region. These resulted in the reducing of the purchasing orders by the end-users and consumers, as well as weakening the customers' confidence. The Company estimates the annual growth rate for the year ending 2013 is expected to be approximately 10% and continue to maintain steadily at 10% in 2014 and 2015. The management of the Company is of the view that the general economy will start picking up in 2012 and 2013 and the



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expansion of business as discussed above. As such, the demand and the sales will restore gradually. Furthermore, a reasonable buffer should be allocated to meet the fluctuations under the New Master Purchase Agreement. We have also calculated that the CAGRs of the turnover of the Group and the Target Group are approximately 2.9% and 60.2% between 2009 and 2011, respectively, and having taken the consideration of the benefits of the Acquisition discussed in the section headed "Reasons for and benefits of the Acquisition", we are of the view that the Company's estimation on the 10% annual business growth rate of the Enlarged Group between 2013 and 2015 is fair and reasonable.

(V) DISCUSSION AND CONCLUSION

The Acquisition is in line with the strategy of the Group to further develop the IT products market through mergers and acquisitions and will broaden the Group's revenue base, which we consider the Acquisition will likely bring positive impact to the Group's turnover.

The total Consideration of HK\$2,012,868,000 for the Acquisition will be satisfied in full by (i) as to HK\$135,000,000 by the allotment and issue of New Ordinary Shares at an issue price of HK\$1.00 per New Ordinary Share; and (ii) as to HK\$1,877,868,000 by the allotment and issue of New Convertible Preference Shares at an issue price of HK\$1.00 per New Convertible Preference Share to Fit Generation upon Completion. This settlement method allows the Group to acquire significant assets without stretching its financial positions. For the Consideration, the P/E Ratio implied by the Consideration is lower than the average as well as the median of the Comparable Companies, and for the P/S Ratio implied by the Consideration is lower than the average of the Comparable Companies, but is equal to the median value. Accordingly, we are of the view that the Consideration when compared to the Comparable Companies is fair and reasonable so far as the Independent Shareholders are concerned, and in the interests of the Company and the Shareholders as a whole.

The allotment and issue of the New Ordinary Shares and New Convertible Preference Shares at a price of HK\$1.00, representing a discount of approximately 42.5% to the closing price of the Ordinary Shares on the Stock Exchange on the Last Trading Day, which is higher than the average discount of the issue prices of the new shares and/or preference shares to the Comparable Shares on the respective last trading days. Taking into account (i) the poor liquidity of the Ordinary Shares, (ii) the large number of Ordinary Shares to be issued or convertible relative to its trading volume, and (iii) there is a lack of comparable market information for shares with low liquidity, accordingly, we are unable to form a view if the issue price at HK\$1.00 is fair and reasonable so far as the Independent Shareholders are concerned and in interests of the Company and the Shareholders as a whole. However, having considered that upon Completion, the pro forma earnings per Ordinary Share and the pro forma net asset value per Ordinary Share will be significantly improved as discussed in the section headed "Financial effects of the Acquisition on the Group" above, we are of the view that the discount on the New Ordinary Shares and New Convertible Preference Shares is fair and reasonable, and in the interests of the Company and Shareholders as a whole.



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The shareholding interest in the Company of the public Shareholders of Ordinary Shares will be diluted from 35.15% to 25.02% after Completion and the allotment and issue of the New Ordinary Shares (but before conversion of any New Convertible Preference Shares), and further diluted to 5.00% after allotment and issue of the New Ordinary Shares and the full conversion of the New Convertible Preference Shares if the public float requirement is not met by the Company. We consider that the dilution is inevitable in the case of a substantial acquisition of this type which is being financed without incurring any cash outlay or additional liabilities to satisfy the Consideration.

The Acquisition will result in the interests of the Sichuan Changhong Concert Party Group and associates being increased from approximately 33.34% to approximately 52.53% of the issued share capital of the Company as enlarged by the New Ordinary Shares (but before conversion of any New Convertible Preference Shares) and further to 90.51% upon full conversion of the New Convertible Preference Shares and the issue of the New Ordinary Shares (in the assumed scenario that the New Convertible Preference Shares are fully converted without subject to the minimum public float requirement), thus triggering an obligation to make an unconditional mandatory general offer for all the issued Ordinary Shares. Sichuan Changhong Concert Party Group has made the application for the Whitewash Waiver, which is subject to the Independent Shareholders' approval. If the Whitewash Waiver is not granted, the Acquisition will not proceed. In the light of the benefits of Acquisition mentioned above, we consider it is in the interests of the Independent Shareholders that the Whitewash Waiver be granted to Sichuan Changhong.

Assuming Completion has taken place on 1 January 2011, the unaudited pro forma net profit of the Enlarged Group would be increased to approximately HK\$201.8 million, representing an increase of approximately 18 times from the audited net profit of the Group for the amount of HK\$10.5 million for the year ended 31 December 2011. Besides, the Acquisition would enhance the pro forma net asset value per Ordinary Share from HK\$0.14 to HK\$0.32 as if the Completion has taken place on 30 June 2012 based on the unaudited pro forma financial information of the Enlarged Group set out in Appendix III to the Circular (and based on a total of 2,346,868,000 Shares after the issuance of the New Ordinary Shares and full conversion of all New Convertible Preference Shares). Given that the proven track record of the turnover generated by the Target Group and the experience of the Group's management in operating the business of distribution of IT products in the PRC, we expect that there will not any material adverse factor as disclosed in the section headed "Risk Factors" in the Circular on the net profit of the Enlarged Group. Nevertheless, Shareholders are advised to read the section headed "Risk Factors" contained in the Circular which describes the risks relating to the Acquisition, the Enlarged Group, the Target Group's business and the industry in which the Target Group operates.

The supply and purchase arrangements between the Enlarged Group and the Sichuan Changhong Group will continue after the Completion and will constitute continuing connected transactions for the Company under the GEM Listing Rules. The proposed annual caps have been determined with reference to the historical transactions conducted, the historical transaction amounts and the future expected growth of the Sichuan Changhong Group after the Acquisition, which we are of the view that the bases for determining the proposed annual caps under the Framework Agreements are fair and reasonable so far as the Independent Shareholders are concerned.



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(VI) ADVICE

Having considered the principal reasons and factors referred to above, we are of the view that:

- (a) the Acquisition, while not in the ordinary and usual course of business of the Company, is on normal commercial terms, fair and reasonable so far as the Independent Shareholders are concerned and in the interests of the Company and the Shareholders as a whole;
- (b) the potential benefits of the Acquisition to the Group and the terms of the Acquisition being fair and reasonable so far as the Independent Shareholders are concerned, we are of the opinion that the approval of the Whitewash Waiver, which is a prerequisite for the Completion, is fair and reasonable so far as the Independent Shareholders are concerned and in the interests of the Company and the Shareholders as a whole; and
- (c) the Framework Agreements are entered in the ordinary and usual course of business. In addition, the terms of the Framework Agreements and their respective proposed annual caps are on normal commercial terms, fair and reasonable so far as the Independent Shareholders are concerned and in the interests of the Company and its Shareholders as a whole.

Accordingly, we advise the Independent Board Committee to advise, and we also recommend, the Independent Shareholders to vote in favour of the resolutions to be proposed at the forthcoming SGM to approve the Acquisition Agreement, the proposed grant of specific mandate to allot and issue the New Ordinary Shares, the New Convertible Preference Shares and the Conversion Shares, the application for the Whitewash Waiver, the Framework Agreements and the transactions contemplated thereunder, and to approve the proposed related aggregate annual caps.

Yours faithfully,
For and on behalf of
TC Capital Asia Limited

Edward Wu
Managing Director