SOMERLEY CAPITAL LIMITED
20/F., China Building, 29 Queen's Road Central, Hong Kong
Telephone: 2869 9090 Fax: 2526 2032 E-Mail: somerley@somerley.com.hk

24 October 2014

To the Independent Board Committee and the Independent Shareholders of Mongolia Energy Corporation Limited

Dear Sir or Madam,

(1) THE SUBSCRIPTIONS INCLUDING CONNECTED TRANSACTION IN RELATION TO SUBSCRIPTION OF THE 2014 GI CONVERTIBLE NOTE; AND (2) WHITEWASH WAIVER IN RELATION TO THE 2014 GI CONVERTIBLE NOTE AND THE 2014 CTF CONVERTIBLE NOTE

INTRODUCTION

We refer to our engagement to advise the Independent Board Committee and the Independent Shareholders in respect of the Subscriptions and the Whitewash Waiver, details of which are set out in the circular of the Company dated 24 October 2014 (the "**Circular**") to the Shareholders and, for information only, holders of the convertible notes of the Company, of which this letter forms part. Capitalised terms used in this letter shall have the same meanings as those defined in the Circular unless the context otherwise requires.

On 19 September 2014, the Company entered into the following:

(i) the 2014 GI Subscription Agreement pursuant to which the Company (as issuer) has conditionally agreed to issue and the GI Subscriber (as subscriber) has conditionally agreed to subscribe for the 2014 GI Convertible Note;

(ii) the 2014 CTF Subscription Agreement pursuant to which the Company (as issuer) has conditionally agreed to issue and the CTF Subscriber (as subscriber) has conditionally agreed to subscribe for the 2014 CTF Convertible Note; and

(iii) the 2014 SF Subscription Agreement pursuant to which the Company (as issuer) has conditionally agreed to issue and the SF Subscribers (as subscribers) have conditionally agreed to subscribe for the 2014 SF Convertible Notes.

As the GI Subscriber is a substantial Shareholder and its sole beneficial owner is an executive Director, the GI Subscriber is a connected person of the Company and the 2014 GI Subscription constitutes a connected transaction for the Company and is subject to reporting, announcement and the Independent Shareholders' approval requirements under the Listing Rules.

The Conversion Shares to be allotted and issued pursuant to the 2014 Convertible Notes are proposed to be issued pursuant to a specific mandate to be granted by the Independent Shareholders by way of poll at the SGM. Given that each of the Subscription Agreements is conditional to one another, all the transactions contemplated under the Subscription Agreements will be subject to the approval of the Independent Shareholders by way of poll at the SGM and the GI Subscriber, the CTF Subscriber, the SF Subscribers and their respective associates will abstain from voting on the proposed resolution to approve the Subscriptions at the SGM.

Completion of the 2014 GI Subscription Agreement and the 2014 CTF Subscription Agreement is conditional upon, among other things, the Whitewash Waiver being approved by the Independent Shareholders and granted by the Executive. The GI Subscriber, Mr. Lo and his spouse, the CTF Subscriber, Dragon Noble Group Limited, Dato' Dr. Cheng Yu Tung, Dr. Cheng Kar Shun, Henry and his spouse are parties acting in concert with each other in respect of the Company. As at the Latest Practicable Date, the Concert Group held an aggregate of 1,832,458,301 Existing Shares, representing approximately 27.12% of the aggregate voting rights of the Company. Upon full conversion of the aggregate amount of the 2014 GI Convertible Note and the 2014 CTF Convertible Note (based on the maximum respective principal amounts thereof to be issued and the accrued interest thereon) at the initial Conversion Price, it is expected that the aggregate voting rights of the Company held by the Concert Group will increase to approximately 77.21%, assuming no other change to the share capital and shareholding structure of the Company.

Under Rule 26 of the Takeovers Code, the acquisition of voting rights under such circumstances will trigger a mandatory general offer by the GI Subscriber and/or the CTF Subscriber for all the securities of the Company other than those already owned (or agreed to be acquired) by the Concert Group, unless an appropriate waiver is obtained.

An application has been made by the GI Subscriber and the CTF Subscriber to the Executive for the Whitewash Waiver. The Executive has indicated that the Whitewash Waiver will be granted subject to the approval of the Independent Shareholders by way of poll at the SGM. Members of the Concert Group and their respective associates and those Shareholders who are involved in or interested in the Subscriptions or the Whitewash Waiver will abstain from voting on the proposed resolution to approve the Whitewash Waiver at the SGM. If the Whitewash Waiver is not granted by the Executive or not approved by the Independent Shareholders, the 2014 GI Subscription Agreement and the 2014 CTF Subscription Agreement will not become unconditional and the Subscriptions will not proceed.

Pursuant to the Listing Rules and the Takeovers Code, the Independent Board Committee, comprising all independent non-executive Directors, namely Mr. Peter Pun, Mr. Tsui Hing Chuen, William and Mr. Lau Wai Piu, has been established to advise the Independent Shareholders as to whether the Subscriptions and the Whitewash Waiver are fair and reasonable and to advise the Independent Shareholders on how to vote on the proposed resolutions in respect thereof at the SGM. Mr. To Hin Tsun, Gerald, a non-executive Director, is not included in the Independent Board Committee as required under the Takeovers Code as Mr. To is currently an executive director of International Entertainment Corporation (stock code: 1009) and a non-executive director of NWS Holdings Limited (stock code: 659) (both of which are controlled by Dato' Dr. Cheng Yu Tung and family, and Dato' Dr. Cheng Yu Tung is the ultimate beneficial owner of the CTF Subscriber). We, Somerley Capital Limited, have been appointed as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in the same regards and our appointment has been approved by the Independent Board Committee.

BASIS OF OUR ADVICE

We are not connected with the Company, the Concert Group, SF Subscribers or any of their respective close associates, associates or core connected persons (all of which as defined in the Listing Rules) or any party acting, or presumed to be acting, in concert with any of them and accordingly, are considered suitable to give independent advice on the Subscriptions and the Whitewash Waiver. Apart from the normal professional fees payable to us in connection with this or similar appointments, no arrangement exists whereby we will receive any fees or benefits from the Company, the Concert Group, SF Subscribers or any of their respective close associates, associates or core connected persons or any party acting, or presumed to be acting, in concert with any of them.

During the past two years, Somerley Limited (presently known as "Somerley International Limited" and a fellow subsidiary of Somerley Capital Limited) issued an opinion letter as an independent financial adviser contained in the Company's circular dated 18 December 2012 in respect of the issues of the Existing 5% GI Convertible Note and the Existing 5% CTF Convertible Note. This past engagement was limited to providing independent advisory services to independent board committee and independent shareholders of the Company pursuant to the Listing Rules. In addition, Somerley Limited issued a certificate in respect of an independent determination of the adjustment on the conversion price of the Existing SF Convertible Notes (the "**Independent Determination**") as disclosed in the Company's announcement dated 9 January 2013. This past engagement was limited to providing the Independent Determination to the Company pursuant to the terms of the Existing SF Convertible Notes. Under the past engagements, Somerley Limited received normal professional fees from the Company. Notwithstanding the past engagements, as at the Latest Practicable Date, there were no relationships or interests with the Company that could reasonably be regarded as a hindrance to our independence as defined under Rule 13.84 of the Listing Rules to act as the independent financial adviser to the Independent Board Committee and the Independent Shareholders in respect of the Subscriptions and the Whitewash Waiver as detailed in the Circular.

In formulating our opinion and recommendation, we have reviewed, amongst others, the Announcement, the Subscription Agreements, the annual reports of the Company for the years ended 31 March 2014 (the "**2014 Annual Report**") and 31 March 2013, the working capital forecast of the Company, the existing convertible notes of the Company and the information contained in the Circular. We have also discussed with and reviewed the information provided by the management of the Group regarding the businesses and outlook of the Group.

We have relied on the information and facts supplied, and the opinions expressed, by the Directors and the management of the Group, which we have assumed to be true, accurate, complete and not misleading in all material aspects as at the date of this letter and will remain as at the date of the SGM. The Independent Shareholders will be informed as soon as possible if we become aware of any material change to such information up to the date of completion of the Subscriptions. We have sought and received confirmation from the Directors and the management of the Group that no material facts have been omitted from the information supplied and opinions expressed by them to us. We consider that the information which we have received is sufficient for us to reach our advice and recommendation as set out in this letter and to justify our reliance on such information. We have no reason to doubt the truth, accuracy or completeness of the information provided to us or to believe that any material information has been omitted or withheld. We have not, however, conducted any independent investigation into the business and affairs of the Group nor have we carried out any independent verification of the information supplied.

PRINCIPAL FACTORS AND REASONS CONSIDERED

In formulating our opinion, we have considered the following principal factors and reasons:

1. Business of and financial information on the Group

(a) Business and outlook of the Group

The Group is an energy and resources developer. The principal project of the Group is the coking coal mining project in Khushuut, Khovd Province, Western Mongolia (the "**Khushuut Coking Coal Project**", the mine site of which is known as the "**Khushuut Coal Mine**").

Despite the continual production halt of the Khushuut Coking Coal Project since October 2012 principally due to the dispute with the former sole mining contractor as well as the global economic downturn which had a negative bearing on the coking coal prices in the PRC, the Group has remained focused on optimising its coal production process and enhancing coal quality as well as appointing external contractors to prepare for the resumption of coal production in the fourth quarter of 2014.

Internally, key measures recently taken by the Group to improve the infrastructures of the Khushuut Coking Coal Project include completion and test run of (i) the dry processing plant in the Khushuut Coal Mine; and (ii) the main operative part of a coal washing plant in Xinjiang, the PRC. If the test runs are smooth, the Group expects these coal processing facilities to formally operate upon coal production in the fourth quarter of 2014. However, the coal production is subject to a number of factors including the successful test runs of its coal processing infrastructures in the Khushuut Coal Mine and in Xinjiang, satisfaction of the customer on coal quality, and market conditions. These infrastructures will complement the Group's coal production process and enhance its coal quality as and when it resumes production. Apart from the upgrade of the infrastructures, the Group appointed an overburden removal contractor in April 2014 to provide blasting, removal of topsoil and overburden covering the coal to be extracted for the subsequent coal mining to take place. The Group also appointed a coal extraction contractor in July 2014 to provide coal extraction services after the coal seam is exposed. The coal extraction contractor also provides loading and haulage of extracted coal services on the mine site. Both contractors are now working at the Khushuut Coal Mine. Apart from the field work contractors, the Group has also appointed external coal trucking companies to provide coal transportation services for its coal export.

Externally, as highlighted by the management of the Group in the 2014 Annual Report, there were encouraging signals released by the Mongolian government that a stable mining sector is being assured. It began with the Mongolian government making a number of amendments to its laws and regulations in order to regain the confidence of foreign investors. In order to enhance the economic growth by increasing export income and stabilising foreign currency rate, the Mongolian government adopted Resolution No.25 in January 2014 regarding "Plan on Measures for Increasing of Export Income". The said plan covers actions to be implemented in hopes of increasing and boosting minerals and coal export. The Group has entered into a co-operation agreement dated 6 March 2014 with the local government for the development of the Khushuut Coking Coal Project in order to obtain support from the local community for ensuring a stable operating environment of the Khushuut Coal Mine. During the year ended 31 March 2014, the Company was informed by its Mongolian legal adviser that the Khushuut Coal Mine was removed from the list of potential strategic deposits to be tabled for consideration at the Mongolian

Parliament. Accordingly, the uncertainty of the Mongolian government's participation in the Khushuut Coking Coal Project with unfavourable terms to the Company was eliminated.

In terms of market dynamics, the principal market of the Group's coking coal is the PRC. The prices and demand for coking coal in the Chinese market have been experienced downward trend as the Chinese economic model shifts from focusing on fixed asset investments to consumption and services. The Group remains confident and we concur that given the close proximity and a historical trade links between the PRC and Mongolia, China is anticipated to remain the largest market for the coking coal produced from the Khushuut Coking Coal Project.

(b) Financial information on the Group

(i) Financial results

The following are summaries of the consolidated statement of profit or loss of the Group for the years ended 31 March 2013 and 2014 as extracted from the 2014 Annual Report.

	For the year ended 31 March	
	2014	**2013**
	HK$'000	*HK$'000*
Revenue	498	11,792
Cost of sales	(4,632)	(261,863)
Gross loss	(4,134)	(250,071)
Impairment losses	(259,838)	(3,137,444)
Fair value gain on derivative component of convertible notes	42,392	302,987
Administrative expenses	(182,077)	(179,025)
Others	(262,440)	(39,137)
Finance costs	(372,027)	(388,743)
Loss before taxation	(1,038,124)	(3,691,433)
Income tax expenses	—	(7,385)
Loss for the year and loss for the year attributable to the Shareholders	(1,038,124)	(3,698,818)

During the year ended 31 March 2013, the Group sold 50,350 tonnes of raw coal to the customers in Xinjiang, the PRC, and Mongolia and generated approximately HK$11.8 million in revenue with an average selling price of approximately HK$234 per tonne. The low sales volume and revenue were attributable to (i) the halt of coal production since October 2012 due to the retreat of the sole mining contractor of the Khushuut Coking Coal Project; and (ii) inadequate screening capability on site at the Khushuut Coal Mine. In the following financial year, the coal production halt of the Khushuut Coking Coal Project continued while the Group mainly focused on the construction of coal production infrastructures. Due to the continual coal production halt, the revenue of the Group for the year ended 31 March 2014 was minimal and was mainly related to the sales of 15,300 tonnes of raw coal from the inventory stored at the coal washing plant at Xinjiang, the PRC.

The cost of sales was exceptionally high for the year ended 31 March 2013 as the mining activities carried out during the year failed to produce raw coal at optimum capacity. A total of approximately HK$90.3 million contractor fee was incurred despite the unsatisfactory production progress. The cost of sales for the year ended 31 March 2014 was approximately HK$4.6 million, which mainly comprised a write-down of inventory to net realisable value of approximately HK$4.1 million. As triggered by the coal production halt, all related expenses incurred in the Khushuut Coal Mine of approximately HK$55.7 million for the year ended 31 March 2014 were grouped under the "Others" category in the table above.

During the year ended 31 March 2013, significant impairment losses of over HK$3.1 billion were recognised for assets related to the Khushuut Coking Coal Project due to (i) significant changes of estimate/assumptions made to the value-in-use calculation by the independent valuer in response to the cost structure of the potential coal extraction contractor at the time; (ii) decrease in estimated selling price of coking coals; and (iii) changes made in response to the suspension of coal production. Further impairment losses of approximately HK$259.8 million on assets related to the Khushuut Coking Coal Project were recognised for the year ended 31 March 2014. Such further impairment losses were largely due to the upward adjustments of the discount rate and estimated mining costs used in the value-in-use calculation by the independent valuer.

The derivative components of the existing convertible notes of the Company were initially recorded at fair value at their respective issue dates and re-measured at the end of each reporting period. As the Share price has declined since the respective issue dates of the existing convertible notes, fair value gains on derivative components of the existing convertible notes of approximately HK$303.0 million and HK$42.4 million were recognised for the years ended 31 March 2013 and 2014 respectively.

The Company was default on redemption of the Existing SF Convertible Notes and has triggered the potential early redemption obligation on the Company under the other existing convertible notes of the Company. The Group therefore re-measured the carrying amounts of the other existing convertible notes to their respective redemption amounts. As a result, a loss on re-measurement of the debt component of the existing convertible notes of approximately HK$219.8 million was recorded for the year ended 31 March 2014 under the "Others" category in the table above.

The administrative expenses of the Company mainly comprised (i) staff costs and benefits; (ii) legal and professional fees; and (iii) rental and utilities expenses. The Company recorded administrative expenses of approximately HK$179.0 million and HK$182.1 million for the years ended 31 March 2013 and 2014 respectively.

Finance costs represented interest on borrowings, majority of which were the interest expense on the existing convertible notes. Upon the re-measurement of the Existing 3% CTF Convertible Note, the Existing 5% GI Convertible Note and the Existing 5% CTF Convertible Note in November 2013, the interest expense on the existing convertible notes were charged at their respective coupon rates but not effective rates. As the respective coupon rates were lower than the effective rates, the finance costs for the year ended 31 March 2014 decreased despite the increase in borrowings.

The loss for the year attributable to the Shareholders dropped from approximately HK$3.7 billion for the year ended 31 March 2013 to approximately HK$1.0 billion for the year ended 31 March 2014. The decrease was mainly due to reduction of impairment losses associated with assets related to the Khushuut Coking Coal Project for the year ended 31 March 2014 as compared to the previous year.

(ii) Assets and liabilities

The following are summaries of the consolidated statements of the financial position of the Group as at 31 March 2013 and 2014 as extracted from the 2014 Annual Report.

	As at 31 March	
	2014	**2013**
	HK$'000	*HK$'000*
Non-current assets		
Property, plant and equipment	6,733,169	6,850,079
Other non-current assets	1,195,195	1,379,228
	7,928,364	8,229,307
Current assets	127,794	107,551
Current liabilities		
Convertible notes	2,454,535	741,279
Advances from a Director	780,210	470,013
Others	1,180,701	272,803
	4,415,446	1,484,095
Net current liabilities	(4,287,652)	(1,376,544)
Total assets less current liabilities	3,640,712	6,852,763
Non-current liabilities		
Convertible notes	—	2,206,661
Deferred income	12,665	—
	12,665	2,206,661
Net assets and equity attributable to the Shareholders	3,628,047	4,646,102

As at 31 March 2014, major assets of the Group were non-current assets including (i) property, plant and equipment mainly associated with the Khushuut Coking Coal Project of approximately HK$6,733.2 million; (ii) intangible assets chiefly representing exclusive right of use of paved road spanning from the Khushuut Coal Mine to the Yarant border crossing with Xinjiang, the PRC of approximately HK$852.8 million; and (iii) the exploration and evaluation assets associated with other mineral resources of approximately HK$285.7 million. The decrease in the non-current assets between 31 March 2013 and 31 March 2014 was a result of, among others, the impairment losses of approximately HK$259.8 million made in respect of the assets related to the Khushuut Coking Coal Project.

As at 31 March 2014, current assets of the Group mainly comprise cash and cash equivalents, other receivables, prepayments and deposits as well as held-for-trading investments. The increase in the current assets of the Group from approximately HK$107.6 million as at 31 March 2013 to approximately HK$127.8 million as at 31 March 2014 was mainly attributable to the increase in held-for-trading investments of approximately HK$29.8 million.

As at 31 March 2014, liabilities of the Group mainly comprised (i) the existing convertible notes of approximately HK$2,454.5 million; (ii) advances from Mr. Lo of approximately HK$780.2 million; and (iii) other financial liabilities of approximately HK$806.0 million. The balance of the existing convertible notes as at 31 March 2014 classified as current liabilities consisted of the outstanding amount of the principal and accrued interest of the Existing 3% CTF Convertible Note, the Existing 5% CTF Convertible Note and the Existing 5% GI Convertible Note. The aggregate balance of the existing convertible notes decreased from approximately HK$2,947.9 million as at 31 March 2013 to approximately HK$2,454.5 million as at 31 March 2014 was mainly due to the reclassification of the outstanding amount of the principal and accrued interest of the Existing 3.5% GI Convertible Note and the Existing SF Convertible Notes to other financial liabilities upon the expiries of the aforesaid two existing convertible notes on 6 September 2013 and 12 November 2013 respectively. Mr. Lo provided a standby facility of up to HK$1,900.0 million, of which approximately HK$1,119.8 million was unutilised as at 31 March 2014, with maturity date on 31 March 2016. The facilities are unsecured and carry an interest rate at Hong Kong prime lending rate plus 3% per annum. Set out below is a summary of the Group's principal liabilities as at 31 March 2014.

Convertible note/facility	Conversion price (per Share)	Principal amount (HK$ million)	Interest (per annum)	Maturity date	Status
Existing 3.5% GI Convertible Note	HK$4.00	300.0	3.5%	6 September 2013[1]	Expired[2]
Existing SF Convertible Notes	HK$2.68	466.8	3.5%	12 November 2013[1]	Expired[3]
Existing 3% CTF Convertible Note	HK$2.00	2,000.0	3.0%	15 June 2014[1]	Expired
Existing 5% GI Convertible Note	HK$0.36	200.0	5.0%	8 January 2016	Current
Existing 5% CTF Convertible Note	HK$0.36	200.0	5.0%	8 January 2016	Current
Mr. Lo's standby facility[4]	N/A	780.2	Hong Kong prime lending rate plus 3%	31 March 2016	Current

Notes:

1. Moratorium on repayment of the respective principals and interests due under the Existing 3.5% GI Convertible Note, the Existing SF Convertible Notes and the Existing 3% CTF Convertible Note was up to 19 September 2014, which had been further extended to the completion date of the 2014 Convertible Notes.

2. As at 31 March 2014, included in other financial liabilities was the Existing 3.5% GI Convertible Note of approximately HK$316.6 million, which was reclassified from convertible notes to other financial liabilities on its maturity. The loan is unsecured, bears interest at a fixed rate of 3.5% per annum and was repayable on 19 September 2014, which had been further extended to the completion date of the 2014 Convertible Notes.

3. As at 31 March 2014, included in other financial liabilities were the Existing SF Convertible Notes of approximately HK$489.4 million, which were reclassified from convertible notes to other financial liabilities on their maturity. The loans are unsecured, bear interest at a fixed rate of 3.5% per annum and were repayable on 19 September 2014, which had been further extended to the completion date of the 2014 Convertible Notes.

4. Mr. Lo has provided a standby facility of up to HK$1,900 million to the Company for its general working capital with maturity on 31 March 2016. As at 31 March 2014, a total of approximately HK$780.2 million was drawn by the Company. The loan is unsecured and repayable on demand. The interest expense charged by the standby facility is at the Hong Kong prime lending rate plus 3% per annum.

Based on the net asset value attributable to the Shareholders of approximately HK$3,628.0 million as at 31 March 2014 and 6,756,547,828 Existing Shares in issue as at the Latest Practicable Date, the net asset value attributable to the Shareholders per Existing Share or per New Share (as adjusted for the effect of the Capital Reorganisation) were approximately HK$0.5370 or HK$2.148 respectively.

In view of (i) the encouraging developments in the operation of the Khushuut Coking Coal Project; (ii) the positive outlook for the Group given the improving government policy in mining sector of Mongolia; (iii) the resumption of coal production in the fourth quarter of 2014 will be an opportunity of the Group to improve its financial performance in the long run; and (iv) the unsatisfactory working capital and gearing positions of the Group and the pressure of repayment of the expired existing convertible notes, we agree that a refinancing arrangement is necessary for the Group to refinance the expired existing convertible notes and to free up general working capital for the Group to further develop the Khushuut Coking Coal Project.

2. Reasons for and use of proceeds of the Subscriptions

As set out in the letter from the Board of the Circular, upon expiry of the Existing 3.5% GI Convertible Note, the Existing 3% CTF Convertible Note and the Existing SF Convertible Notes, the Company exercised its best endeavor to engage in negotiations with the Subscribers for the refinancing arrangement and finally reached a mutually acceptable debt restructuring plan by entering into the Subscription Agreements with the Subscribers.

The subscription price of the 2014 Convertible Notes will be used by the Company for (i) the full settlement of the outstanding principal amount and accrued interest of the existing expired convertible notes; and (ii) the early redemption of the outstanding principal amount and accrued interest of the existing unexpired convertible notes, on the respective completion dates of the Subscription Agreements. The maximum aggregate amount of the refinancing involved in the Subscriptions is approximately HK$3,470.1 million (being the total outstanding principal amount and accrued interest owing under the existing convertible notes calculated up to the Long Stop Date).

We note that the executive Directors are of the view that, after taking into account that: (i) the full settlement of the outstanding principal amounts and accrued interest of the Existing 3.5% GI Convertible Note, the Existing 3% CTF Convertible Note and the Existing SF Convertible Notes with the issue of the 2014 Convertible Notes will not exert immediate cash outflow burden on the Group; (ii) the early redemption of the Existing 5% GI Convertible Note and the Existing 5% CTF Convertible Note with the issue of the 2014 GI Convertible Note and the 2014 CTF Convertible Note bearing interest at 3% per annum will reduce the Group's payable interests; (iii) the Subscriptions will secure the continuing financial support from the Subscribers to the Group's business development and operation; (iv) the prevailing market prices and trading volume of the Shares and/or the current financial position of the Group may not be favourable to a fund raising exercise for substantial amount by way of issue of new Shares to independent third party(ies) or to existing Shareholders on a pro rata basis (e.g. rights issue and open offer) where considerable discount to the market prices of the Shares would be required after the Company's enquiry of certain brokerage houses with no favourable responses; and (v) the issue of the 2014 Convertible Notes will not lead to immediate dilution on the shareholding interests of the existing Shareholders, the issue of the 2014 Convertible Notes is an appropriate debt restructuring plan for the Company.

3. Financing alternatives available to the Group

We have reviewed whether there are other financing alternatives which were available to the Group other than the 2014 Convertible Notes and examined the reasons why they were not adopted.

As advised by the management of the Group, the Company has considered other forms of equity financing. The prevailing market prices and trading volume of the Shares and/or the current financial position of the Group may not be favourable to any fund raising exercises for substantial amount by way of issue of new Shares to independent third party(ies) (e.g. new share placement) or to existing Shareholders on a pro rata basis (e.g. rights issue or open offer) where considerable discount to the market prices of the Shares would be required after the Company's enquiry of certain brokerage houses with no favourable responses, whereas the initial Conversion Price of HK$0.230 per Conversion Share was set at a premium of approximately 1.32% over the closing price of the Shares on the Last Trading Day. Furthermore, fund raising by way of new share placement will create immediate dilution on the shareholding of the existing Shareholders. On the other hand, fund raising through rights issue or open offer will attract higher transaction costs (such as underwriting and other fees) and dilution effects on those non-participating Shareholders will usually be greater as compared to new share placement and issue of convertible notes. We understand that the current debt restructuring proposal was arrived at after due and careful consideration of various alternatives by the executive Directors. The executive Directors consider and we concur with the executive Directors' view that the issue of the 2014 Convertible Notes is an appropriate debt restructuring plan for the Company.

4. Principal terms of the 2014 Convertible Notes

(a) Subject

On 19 September 2014, the Company entered into the 2014 GI Subscription Agreement pursuant to which the Company (as issuer) has conditionally agreed to issue and the GI Subscriber (as subscriber) has conditionally agreed to subscribe for the 2014 GI Convertible Note at the subscription price which will be used for full settlement of the outstanding principal amount and accrued interest of the Existing 3.5% GI Convertible Note due and owing by the Company to the GI Subscriber on the GI Completion Date and for early redemption of the outstanding principal amount and accrued interest of the Existing 5% GI Convertible Note on the GI Completion Date. The GI Subscriber has, subject to the terms and conditions of the 2014 GI Subscription Agreement, agreed to extend the date of repayment of the aggregate outstanding amount owing under the Existing 3.5% GI Convertible Note to the GI Completion Date. The GI Subscriber agrees not to exercise the conversion right under the Existing 5% GI Convertible Note until the GI Completion Date. The aggregate outstanding amount under the Existing 3.5% GI Convertible Note and the Existing 5% GI Convertible Note was approximately HK$538.8 million as at the date of the 2014 GI Subscription Agreement and will be approximately HK$542.9 million as at the Long Stop Date.

On 19 September 2014, the Company entered into the 2014 CTF Subscription Agreement pursuant to which the Company (as issuer) has conditionally agreed to issue and the CTF Subscriber (as subscriber) has conditionally agreed to subscribe for the 2014 CTF Convertible Note at the subscription price which will be used for full settlement of the outstanding principal amount and accrued interest of the Existing 3% CTF Convertible Note due and owing by the Company to the CTF Subscriber on the CTF Completion Date and for early redemption of the outstanding principal amount and accrued interest of the Existing 5% CTF Convertible Note on the CTF Completion Date. The CTF Subscriber has, subject to the terms and conditions of the 2014 CTF Subscription Agreement, agreed to extend the date of repayment of the aggregate outstanding amount owing under the Existing 3% CTF Convertible Note to the CTF Completion Date. The CTF Subscriber agrees not to exercise the conversion right under the Existing 5% CTF Convertible Note until the CTF Completion Date. The aggregate outstanding amount under the Existing 3% CTF Convertible Note and the Existing 5% CTF Convertible Note was approximately HK$2,413.1 million as at the date of the 2014 CTF Subscription Agreement and will be approximately HK$2,426.9 million as at the Long Stop Date.

On 19 September 2014, the Company entered into the 2014 SF Subscription Agreement pursuant to which the Company (as issuer) has conditionally agreed to issue and the SF Subscribers (as subscribers) have conditionally agreed to subscribe for the 2014 SF Convertible Notes at the subscription price which will be used for full settlement of all outstanding principal amount and accrued interest of the Existing SF Convertible Notes due and owing by the Company to the SF Subscribers on the SF Completion Date. The SF Subscribers have, subject to the terms and conditions of the 2014 CTF Subscription Agreement, agreed to extend the date of repayment of the aggregate outstanding amount owing under the Existing SF Convertible Notes to the SF Completion Date. The aggregate outstanding amount under the Existing SF Convertible Notes was approximately HK$497.1 million as at the date of the 2014 SF Subscription Agreement and will be approximately HK$500.3 million as at the Long Stop Date.

The 2014 GI Subscription, the 2014 CTF Subscription, the 2014 SF Subscription and the Whitewash Waiver are part and parcel to the whole debt restructuring plan under the Subscriptions. The Subscription Agreements are inter-conditional on one other and completion of the Subscription Agreements shall take place simultaneously. Shareholders' attention are also drawn to the conditions precedent set out in the paragraph headed "Conditions precedent" in each of the sections headed "2014 GI Subscription Agreement", "2014 CTF Subscription Agreement" and "2014 SF Subscription Agreement" in the letter from the Board of the Circular.

The principal terms of the 2014 Convertible Notes are set out in the letter from the Board of the Circular. Our analyses of each of them are set out below.

(b) Conversion Price

The initial Conversion Price (subject to adjustments as set out in the section headed "Principal terms of the 2014 Convertible Notes" in the letter from the Board in the Circular), being HK$0.230 per Existing Share (for illustration purpose, approximately HK$0.920 per New Share), represents:

(i) a premium of approximately 1.3% over the adjusted closing price of HK$0.908 per New Share (based on the closing price of HK$0.227 per Existing Share as quoted on the Stock Exchange on the Last Trading Day and adjusted for the effect of the Capital Reorganisation);

(ii) a premium of approximately 1.8% over the adjusted average closing price of approximately HK$0.904 per New Share (based on the average closing price of approximately HK$0.226 per Existing Share as quoted on the Stock Exchange for the 5 consecutive trading days up to and including the Last Trading Day and adjusted for the effect of the Capital Reorganisation);

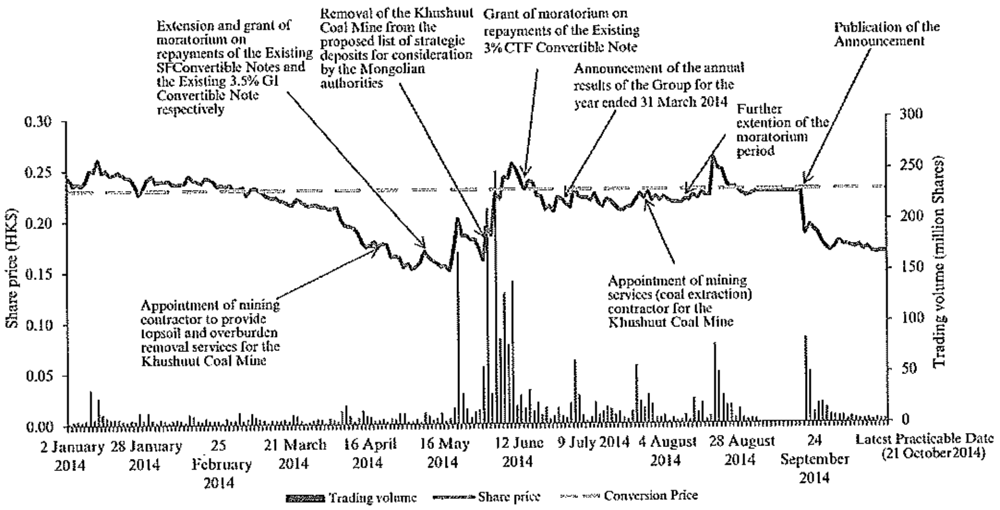
(iii) a discount of approximately 1.3% to the adjusted average closing price of approximately HK$0.932 per New Share (based on the average closing price of approximately HK$0.233 per Existing Share as quoted on the Stock Exchange for the 10 consecutive trading days up to and including the Last Trading Day and adjusted for the effect of the Capital Reorganisation);

(iv) a premium of approximately 36.9% over the adjusted closing price of HK$0.672 per New Share (based on the closing price of HK$0.168 per Existing Share as quoted on the Stock Exchange on the Latest Practicable Date and adjusted for the effect of the Capital Reorganisation); and

(v) a discount of approximately 57.2% to the adjusted audited consolidated net assets value of approximately HK$2.148 per New Share (based on the audited consolidated net assets value of approximately HK$0.537 per Existing Share (calculated from the audited consolidated net assets value of Company attributable to the Shareholders of approximately HK$3,628.0 million as at 31 March 2014 and 6,756,547,828 Existing Shares in issue as at the Latest Practicable Date) and adjusted for the effect of the Capital Reorganisation).

We understand that the initial Conversion Price was determined after arm's length negotiation between the Company and the Subscribers after taking into account the prevailing market price of the Existing Shares, the Capital Reorganisation, the operation and financial performance of the Group and the current market conditions.

In order to assess the fairness and reasonableness of setting the initial Conversion Price at HK$0.230 per Conversion Share, we have analysed the recent Share price performance. Set out in the chart below are the historical closing price and trading volume of the Existing Shares from the beginning of 2014 and up to and including the Latest Practicable Date (the "**Review Period**"). We consider that the 10-month Review Period a reasonable period of time within which the prevailing market price of the Existing Shares can be illustrated. As set out in the discussion below, the Company announced a number of developments during the Review Period which we consider to be crucial in shaping the market price of the Existing Shares.



Source: Bloomberg

During the Review Period, the closing prices of the Existing Shares ranged from the lowest of HK$0.151 per Share to the highest of HK$0.260 per Share. During the Review Period, the Share price fell from the aforesaid highest price level in middle of January 2014 and oscillated downwards continuously. The Share price reached a trough in early to middle of May 2014 and rebounded since early June 2014 after the announcements of a couple of positive developments of the Company including the appointment of a mining services (removal of topsoil and overburden) contractor, extension and grant of moratorium on repayments of certain outstanding convertible notes of the Company and the removal of the Khushuut Coal Mine from the proposed list of strategic deposits for consideration by the Mongolian Parliament in late April 2014 to middle of June 2014. On 11 June 2014, the Share price was closed almost at par with the previous height of HK$0.260 per Share where the Existing Shares closed at HK$0.255 apiece. Thereafter and until the publication of the Announcement, the Existing Shares traded at a narrower band between HK$0.208 per Share and HK$0.260 per Share but were unable to break through the HK$0.260 per Share mark following the releases of announcements of the annual results of the Group for the year ended 31 March 2014 and the appointment of another mining services (coal extraction) contractor. Since the publication of the Announcement and up to and including the Latest Practicable Date, the share price of the Existing Shares slid downwards and the closing prices were in-between HK$0.167 per Share and HK$0.194 per Share with an average of approximately HK$0.175 per Share.

The Share price level in the Review Period appears to have already reflected all the sentiments revolved around the challenges faced by the Company in 2014. The average closing price of an Existing Share during the Review Period was approximately HK$0.213 while the initial Conversion Price of HK$0.230 per Conversion Share represents a premium of approximately 8.0% over the average closing price per Share for this period.

Based on the above factors, we consider the initial Conversion Price to be fair and reasonable and in the interests of the Company and the Shareholders as a whole.

(c) Maturity

The maturity of the 2014 Convertible Notes is the fifth anniversary from the date of their issue and the Company shall redeem 100% of the respective outstanding principal amounts of the 2014 Convertible Notes at par together with all interest accrued thereon on the maturity date.

As discussed with the management of the Group, the coal production of the Khushuut Coal Mine was planned to commence in the fourth quarter of 2014 and the business activities of the Group will, upon resolving the technical issues associated with coal processing, enhancing coal quality and appointment of the external contractors, expand considerably relative to what was achieved in the past few years. The five-year term of the 2014 Convertible Notes shall provide the Group with adequate time to build up its full-scale mining operation before the repayment of the 2014 Convertible Notes falls due. It also relieves the Group's financial pressure during this period before the Khushuut Coal Mine comes to a full scale coal production.

(d) Conversion, repurchase and redemption

Holders of the 2014 Convertible Notes have the right to convert, with a minimum aggregate amount of HK$1 million and HK$1,000 integral multiples thereof, during the term of the 2014 Convertible Notes, all or any part of the outstanding principal amount and any accrued but unpaid interest of the 2014 Convertible Notes into Conversion Shares at the Conversion Price (subject to adjustments).

The Company or any of its subsidiaries may at any time and from time to time repurchase the 2014 Convertible Notes or any part thereof at any price, in the open market or otherwise, as may be agreed between the Company or such subsidiary and the holder(s) of the 2014 Convertible Note(s). The 2014 Convertible Note(s) or any part thereof so repurchased shall forthwith be cancelled by the Company.

The Company also has the right to redeem the whole or any part (in denomination of HK$1,000) of the outstanding principal amount of the 2014 GI Convertible Note and/or the 2014 CTF Convertible Note together with all interest accrued thereon during their respective term.

We consider the above terms of the 2014 GI Convertible Note and the 2014 CTF Convertible Note to be favourable to the Company as these options provide more flexibility to the Company for retirements of the 2014 GI Convertible Note and the 2014 CTF Convertible Note.

(e) Interest rate

The 2014 Convertible Notes carry an interest rate of 3% per annum on the principal amount from time to time outstanding which is payable in arrears on the maturity date of the 2014 Convertible Notes.

Having taken into account the fact that (i) the refinancing requirement of the Group as discussed in the section headed "2. Reasons for and use of proceeds of the Subscriptions" above in this letter; (ii) the issue of the 2014 Convertible Notes is the preferred method of financing in light of prevailing market prices and trading volume of the Shares and the current financial position of the Group as discussed in the section headed "3. Financing alternatives available to the Group" above in this letter; (iii) the interest rate of 3% per annum of the 2014 Convertible Notes is close to the average interest rates charged by the Comparable Transactions (as defined below) as discussed in the section headed "5. Comparable Transactions" below in this letter and is lower than (a) the interest rates of the existing unexpired convertible notes of the Company (i.e. the Existing 5% GI Convertible Note and the Existing 5% CTF Convertible Note); and (b) the interest rate charged on the advances from Mr. Lo; and (iv) the unsecured nature of the 2014 Convertible Notes, we consider that the 3% interest rate attached to the 2014 Convertible Notes to be acceptable.

(f) Other terms of the 2014 Convertible Notes

The 2014 Convertible Notes are freely transferable, in whole or in part (in authorised denomination of HK$1,000 or its multiples) of the outstanding principal amount, to any person, subject to the respective terms of the 2014 Convertible Notes, the Listing Rules and all applicable laws and regulations. We consider the availability of such terms provides protection to the Company for the purposes of general regulatory compliance and such terms are generally in line with market practice.

5. Comparable Transactions

In assessing the terms of the 2014 Convertible Notes, we have also reviewed a number of comparable transactions took place during the Review Period (up to 4:00 p.m. on the Latest Practicable Date) which involved the issue of convertible bonds/notes (the "**Comparable Transactions**"). The Comparable Transactions are selected based on the following criteria: (i) the issuers are listed on the Stock Exchange and such transactions are publicly announced by way of announcement pursuant to the Listing Rules; (ii) the market capitalisation of each issuer is comparable to that of the Company (i.e. within the range between 0.5 time to 2 times of the market capitalisation of the Company as at the Latest Practicable Date); and (iii) the convertible bonds/notes have a duration of 3 to 5 years. The Comparable Transactions were considered an exhaustive list of transactions based on the aforesaid criteria.

We note that although the business activities, financial positions, business performances and future prospects of the issuers engaging in the Comparable Transactions vary from company to company, we consider that the terms of the Comparable Transactions were determined under similar market conditions and sentiments as the 2014 Convertible Notes and the Comparable Transactions serve as a reasonable proxy of the recent trend in convertible bonds/notes issues in the Hong Kong market. Furthermore, as there were 19 Comparable Transactions in the 10-

month review period, representing a reasonable number for our comparison purpose, we consider the selection of the 10-month review period appropriate for our analysis and the Comparable Transactions are a fair and representative sample.

The Comparable Transactions are set out in the table below.

Date of announcement	Name of company	Stock code	Market capitalisation (HK$' million)	Interest rate (per annum)	Duration (number of years)	Premium/(discount) of conversion price over/(to) the share price of last trading day prior to the publication of the relevant announcement	Premium/(discount) of conversion price over/(to) the share price of last 5 trading days prior to the publication of the relevant announcement	Redemption on maturity
14 January 2014	Green International Holdings Limited	2700	756	(1) 5.0%	3	(9.09)%	(6.72)%	100.00%
21 January 2014	Ping Shan Tea Group Limited	364	1,246	4.0%	3	5.00%	(7.49)%	100.00%
28 January 2014	Hong Kong Resources Holdings Company Limited ("HK Resources")	2882	708	3.0%	5	(2) (2.17)%	(2) 3.45%	100.00%
30 January 2014	Sunway International Holdings Limited	58	570	0.0%	3	(14.29)%	9.73%	(3) Not applicable
1 April 2014	Crosby Capital Limited	8088	608	5.0%	3	12.68%	12.36%	Not stated
4 April 2014	Sheen Tai Holdings Group Company Limited	1335	643	3.0%	3	(14.09)%	(3.38)%	Not stated
17 April 2014	Kiu Hung Energy Holdings Limited	381	1,073	0.0%	3	(27.54)%	(23.08)%	Not stated
30 April 2014	Cosmopolitan International Holdings Limited	120	816	2.5%	3	(4) 29.63%	(4) 29.31%	100.00%
30 April 2014	Cosmopolitan International Holdings Limited ("Cosmopolitan")	120	816	3.5%	Up to 3	(4) 48.15%	(4) 47.78%	100.00%
5 May 2014	China Print Power Group Limited	6828	1,806	0.0%	3	(12.92)%	(14.31)%	Not stated
14 May 2014	China Ocean Shipbuilding Industry Group Limited	651	1,928	7.5%	3	(33.33)%	(21.20)%	100.00%
5 June 2014	China Investments Holdings Limited	132	925	2.0%	5	18.75%	22.19%	100.00%
13 June 2014	National United Resources Holdings Limited	254	599	0.0%	5	(6.54)%	(8.17)%	100.00%
18 June 2014	China Putian Food Holding Limited	1699	952	(5) 10.5%	3	(8.45)%	(7.80)%	115.00%
5 August 2014	Beijingwest Industries International Limited	2339	957	0.0%	5	(11.36)%	(9.72)%	100.00%
14 August 2014	South Sea Petroleum Holdings Limited ("South Sea Petroleum")	76	1,874	0.0%	Up to 4.25	(1.19)%	0.00%	Not stated
30 September 2014	Blue Sky Power Holdings Limited	6828	1,806	8.0%	3	1.55%	3.36%	104.00%
7 October 2014	Blue Sky Power Holdings Limited	6828	1,806	0.0%	3	(10.19)%	(6.23)%	Not stated
20 October 2014	ZMFY Automobile Glass Services Limited	8135	624	1.0%	3	(20.00)%	(10.61)%	100.00%
			Average	2.89%	(6) 3.49	(2.92)%	0.58%	101.58%
			Median	2.50%	3.00	(8.45)%	(6.23)%	100.00%
			Maximum	10.50%	5.00	48.15%	47.78%	115.00%
			Minimum	0.00%	3.00	(33.33)%	(23.08)%	100.00%
19 September 2014	The Company — The 2014 Convertible Notes	276	1,122	3.0%	5	1.32%	1.95%	100.00%

Sources: Website of the Stock Exchange and Bloomberg

Notes:

1. The interest payment is payable upon maturity and no interest payment is required if the relevant convertible bonds/notes are previously redeemed or converted.

2. The price comparisons of the issue of the convertible bonds by HK Resources are made with reference to closing prices of HK Resources on and prior to 1 November 2013, being the last trading date immediate before the publication of the joint announcement of HK Resources and Luk Fook Holdings (International) Limited dated 5 November 2013 in relation to a memorandum of understanding regarding, among other things, the issue of the convertible bonds by HK Resources.

3. The convertible notes issued by Sunway is subject to mandatory conversion upon maturity.

4. The price comparisons of the issue of the convertible bonds by Cosmopolitan are made with reference to closing prices of Cosmopolitan on and prior to 30 April 2014 after adjusted for an open offer conducted by Cosmopolitan before the issue of the convertible bonds by Cosmopolitan.

5. The interest rate includes an administrative fee of 1.0% per annum.

6. For the purpose of computation of the average duration, the convertible bonds/notes of Cosmopolitan and South Sea Petroleum with duration of up to 3 years and up to 4.25 years are assumed to be 3 years and 4.25 years respectively.

7. Chun Wo Development Holdings Limited ("**Chun Wo**", stock code: 711) announced the issue of convertible bonds on 20 October 2014. The statistics of the convertible bonds proposed to be issued by Chun Wo are considered not applicable for our analysis as such issue is part of a takeover transaction involving Chun Wo and therefore such issue is not included in the table above.

As set out in the table above, the interest rate of the 2014 Convertible Notes of 3% per annum is close to the average of 2.89% and higher than the median of 2.50% of that of the Comparable Transactions.

The premium of the initial Conversion Price over the closing price of the Shares on the Last Trading Day for the 2014 Convertible Notes is 1.32%, which is higher than the average of 2.92% discount and the median of 8.45% discount of that of the Comparable Transactions. When compared to a 5-day average share price prior to the entering into the relevant issue of the convertible notes/bonds, the premium of the initial Conversion Price over the 5-day average closing price of the Shares for the 2014 Convertible Notes increases slightly to 1.95%, which is also higher than the average of 0.50% premium and the median of 6.23% discount of that of the Comparable Transactions.

Based on our analyses in section headed "4. Principal terms of the 2014 Convertible Notes" and this section, we concur with the executive Directors' view that the terms of the Subscription Agreements are on normal commercial terms and fair and reasonable, and the transactions contemplated under the Subscription Agreements are in the interests of the Company and the Shareholders as a whole.

6. Financial effects of the Subscriptions on the Group

(a) Net asset value

As advised by the management of the Company and based on the accounting policies of the Group, the 2014 Convertible Notes to be issued by the Company will contain both debt and conversion option components, both being accounted for as liabilities, and will be classified separately on initial recognition. As the subscription prices of the 2014 Convertible Notes will be used by the Company for settlement and early redemption of the existing convertible notes of the Company, it is anticipated that, save for the relevant transaction costs, the impact of the Subscriptions on the net asset value of the Company will not be significant upon completion of the Subscriptions.

(b) Earnings

As advised by the management of the Company and based on the accounting policies of the Group, the debt component of the 2014 Convertible Notes will be carried at amortised cost using the effective interest method in subsequent periods. The effective interest expenses of the 2014 Convertible Notes will be charged to the consolidated statement of profit or loss of the Group subsequent to the issue of the 2014 Convertible Notes. The finance costs which are calculated based on effective interest of the 2014 Convertible Notes will continuously be incurred by the Group until conversion and/or redemption of the 2014 Convertible Notes in full. In addition, the conversion option (i.e. derivative) component of the 2014 Convertible Notes will be measured at fair value with changes in fair value recognised in the consolidated statement of profit and loss of the Group.

Although the finance costs and the changes in fair value of the conversion option component of the 2014 Convertible Notes may create negative impact on the future earnings of the Group, the issue of the 2014 Convertible Notes is considered necessary in order to allow the Group to facilitate its mining operation in the Khushuut Coking Coal Project and the refinancing requirement of the Group as discussed in section headed "2. Reasons for and use of proceeds of the Subscriptions" above in this letter.

(c) Working capital

As at 31 March 2014, the Group had net current liabilities of approximately HK$4,287.7 million. Upon completion of the Subscriptions, the subscription price of the 2014 Convertible Notes (being a maximum of approximately HK$3,470.1 million based on the total outstanding principal amount and accrued interest owing under the existing convertible notes calculated up to the Long Stop Date) will be used for the settlement of all the existing convertible notes of the Company, all of which are current liabilities. As the duration of the 2014 Convertible Notes will be 5 years, the 2014 Convertible Notes will be initially classified as non-current liabilities. This effectively refinances the aforesaid current liabilities with non-current liabilities. Accordingly, the working capital position of the Group are expected to be improved upon completion of the Subscriptions.

7. Potential dilution effect on the shareholdings of the Independent Shareholders

Assuming that the Capital Reorganisation has become effective and there is no other change to the issued share capital and shareholding structure of the Company from the Latest Practicable Date up to the date when all the 2014 Convertible Notes are converted, the full conversion of the 2014 Convertible Notes will result in an allotment and issue of no more than approximately 17,350.6 million Conversion Shares (before the Capital Reorganisation becoming effective) approximately or 4,337.6 million Conversion Shares (after the Capital Reorganisation becoming effective), which represents approximately 256.80% of the entire issued share capital of the Company at the Latest Practicable Date and approximately 71.97% of the entire issued share capital of the Company as enlarged by the issue of the Conversion Shares. Dilution effect on the existing public Shareholders is approximately 52.37% (from approximately 72.77% to approximately 20.40%). We consider the aforesaid dilution effect acceptable in light of (i) the low level of cash holdings of the Group of approximately HK$48.6 million as at 31 March 2014; (ii) the pressing need to refinance the existing liabilities of the Group as most of them have fallen due or about to; and (iii) the other forms of equity financing are limited, means the existing public Shareholders may suffer from a greater degree of dilution.

8. Whitewash Waiver

Upon full conversion of the aggregate amount of the 2014 GI Convertible Note and the 2014 CTF Convertible Note (based on the maximum respective principal amounts thereof to be issued and the accrued interest thereon) at the initial Conversion Price, it is expected that the aggregate voting rights of the Company held by the Concert Group will increase to approximately 77.21%, assuming no other change to the share capital and shareholding structure of the Company. Under Rule 26 of the Takeovers Code, the acquisition of voting rights under such circumstances will trigger a mandatory general offer by the GI Subscriber and/or the CTF Subscriber for all the securities of the Company other than those already owned (or agreed to be acquired) by the Concert Group, unless an appropriate waiver is obtained. An application has been made by the GI Subscriber and the CTF Subscriber to the Executive for the Whitewash Waiver. The Executive has indicated that the Whitewash Waiver will be granted subject to the approval of the Independent Shareholders by way of poll at the SGM. Members of the Concert Group and their respective associates and those Shareholders who are involved in or interested in the Subscriptions or the Whitewash Waiver will abstain from voting on the proposed resolution to approve the Whitewash Waiver at the SGM.

Independent Shareholders should note that the 2014 GI Subscription and the 2014 CTF Subscription are conditional on, among others, the granting of the Whitewash Waiver by the Executive and the approval of the Whitewash Waiver by the Independent Shareholders by way of poll at the SGM. Such condition cannot be waived under the terms of the 2014 GI Subscription Agreement and the 2014 CTF Subscription Agreement. If the Whitewash Waiver is not granted by the Executive or if the Whitewash Waiver is not approved by the Independent Shareholders, the 2014 GI Subscription Agreement and the 2014 CTF Subscription Agreement will lapse. In such circumstances, the SF Subscription Agreement will also lapse given the Subscription Agreements are inter-conditional on one other. Based on the principal factors and reasons as set forth above, we do not see the merit to be gained by the Independent Shareholders for not voting in favour of the resolution to approve the Whitewash Waiver. Failure to approve the resolution in relation to the Whitewash Waiver would cause the Subscription Agreements to lapse.

DISCUSSION AND ANALYSIS

The Khushuut Coking Coal Project, being the principal project of the Group, has experienced significant operational difficulties in the last few years and has been in continual production halt since October 2012. Nevertheless, there were encouraging developments in the operation of the Khushuut Coking Coal Project and the outlook has become more favourable given the improving government policy in the mining sector of Mongolia since the last financial year. It is currently expected that the coal production of the Khushuut Coking Coal Project will be resumed in the fourth quarter of 2014.

Due to the operational difficulties and the continual production halt of the Khushuut Coking Coal Project since October 2012, the Group recorded substantial losses in the last few years. The financial positions, in particular working capital and gearing levels, were unsatisfactory. To make matters worse, a substantial amount of the existing liabilities of the Group, mostly the existing convertible notes, have fallen due or about to. Accordingly, we agree that a refinancing arrangement is necessary for the Group to refinance the existing expired convertible notes and to free up general working capital for the Group to further develop the Khushuut Coking Coal Project.

The terms of the 2014 Convertible Notes, including but not limited to the Conversion Price, maturity, repurchase, redemption and interest rate, are considered to be favourable or acceptable to the Company. In particular, the comparison of the initial Conversion Price of the 2014 Convertible Notes against the recent closing price of the Shares is considered to be favourable to the Company when compared with that of the Comparable Transactions. In addition, the interest rate of the 2014 Convertible Notes of 3% per annum is close to the average of that of the Comparable Transactions.

The financial impact of the Subscriptions on the Group is considered to be favourable in general having taken into account the working capital position of the Group will be significantly enhanced upon completion of the Subscriptions. The improvement of the Group's working capital position is necessary to facilitate the mining operation in the Khushuut Coking Coal Project.

Assuming no other change to the issued share capital and shareholding structure of the Company from the Latest Practicable Date up to the date when all the 2014 Convertible Notes are converted, dilution effect resulting from full conversion of the 2014 Convertible Notes on the existing public Shareholders is approximately 52.37% (from approximately 72.77% to approximately 20.40%). We consider the aforesaid dilution effect acceptable in light of (i) the low level of cash holdings of the Group; (ii) the pressing need to refinance the existing liabilities of the Group as most of them have fallen due or about to; and (iii) the other forms of equity financing are limited, means the existing public Shareholders may suffer from a greater degree of dilution.

The 2014 GI Subscription and the 2014 CTF Subscription are conditional on, among others, the approval of the Whitewash Waiver by the Independent Shareholders at the SGM. If the Whitewash Waiver is not approved by the Independent Shareholders, the 2014 GI Subscription Agreement and the 2014 CTF Subscription Agreement will lapse. In such circumstances, the SF Subscription Agreement will also lapse given the Subscription Agreements are inter-conditional on one other. Based on the principal factors and reasons as set forth above, we do not see the merit to be gained by the Independent Shareholders for not voting in favour of the resolution to approve the Whitewash Waiver.

OPINION AND RECOMMENDATION

Having considered the abovementioned principal factors and reasons, we consider that the Subscriptions, though not entered into in the ordinary and usual course of business of the Group, are on normal commercial terms, and the terms of the Subscription Agreements and the transactions contemplated thereunder and the Whitewash Waiver are fair and reasonable as far as the Independent Shareholders are concerned and are in the interests of the Company and the Shareholders as a whole. We therefore advise the Independent Board Committee to recommend, and we ourselves recommend, the Independent Shareholders to vote in favour of the resolutions approving the Subscriptions and the Whitewash Waiver at the SGM.

Yours faithfully,
for and on behalf of
SOMERLEY CAPITAL LIMITED

Kenneth Chow
Managing Director — Corporate Finance

Danny Cheng
Director

Mr. Kenneth Chow is a licensed person registered with the SFC and as a responsible officer of Somerley to carry out Type 6 (advising on corporate finance) regulated activities under the SFO and has over 15 years of experience in corporate finance industry.

Mr. Danny Cheng is a licensed person registered with the SFC and as a responsible officer of Somerley to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities under the SFO and has over 10 years of experience in corporate finance industry.