BAOFENG MODERN INTERNATIONAL HOLDINGS COMPANY LIMITED
寶峰時尚國際控股有限公司

(Incorporated in the Cayman Islands with limited liability)
(Stock Code: 1121)

ANNUAL RESULTS ANNOUNCEMENT FOR THE YEAR ENDED 31 DECEMBER 2016

The board (the "Board") of directors (the "Directors") of Baofeng Modern International Holdings Company Limited (the "Company") announces the audited consolidated results of the Company and its subsidiaries (collectively referred to as the "Group") for the year ended 31 December 2016, together with the comparative figures for 2015 and the relevant explanatory notes as set out below.

CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

For the year ended 31 December 2016

	Notes	2016 RMB'000	2015 RMB'000
REVENUE	4	**215,831**	171,655
Cost of sales		**(140,529)**	(128,746)
GROSS PROFIT		**75,302**	42,909
Other net income and gains	4	**3,506**	13,091
Selling and distribution expenses		**(8,591)**	(11,968)
General and administrative expenses		**(51,916)**	(36,078)
Amortisation of intangible assets	10	**(105,401)**	(6,501)
Impairment loss on intangible assets	10	**(325,616)**	–
Finance costs	5	**(7,933)**	(7,848)
Fair value loss on convertible notes and warrants at fair value through profit or loss	14	**(31,173)**	(13,451)
Fair value gain on provision for contingent consideration at fair value through profit or loss	15	**141,915**	–
LOSS BEFORE TAX	6	**(309,907)**	(19,846)
Income tax expense	7	**(7,671)**	(5,823)
LOSS FOR THE YEAR AND TOTAL COMPREHENSIVE EXPENSES FOR THE YEAR ATTRIBUTABLE TO OWNERS OF THE COMPANY		**(317,578)**	(25,669)
LOSS PER SHARE	9		
– Basic (RMB)		**(0.29)**	(0.02)
– Diluted (RMB)		**(0.29)**	(0.02)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
As at 31 December 2016

	Notes	2016 RMB'000	2015 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment		**82,010**	87,341
Prepaid land lease payments		**32,640**	33,485
Intangible assets	*10*	**1,302,378**	1,476,616
		1,417,028	1,597,442
CURRENT ASSETS			
Inventories		**24,922**	31,366
Trade receivables	*11*	**76,132**	39,034
Prepayments, deposits and other receivables		**7,437**	7,451
Pledged deposits		**4,283**	2,723
Cash and bank balances		**4,789**	789,836
		117,563	870,410
CURRENT LIABILITIES			
Trade and bills payables	*12*	**53,889**	38,679
Deposits received, other payables and accruals		**33,518**	630,259
Interest-bearing bank borrowings	*13*	**124,000**	129,570
Warrants	*14*	**5,067**	21,590
Income tax payable		**8,285**	1,640
		224,759	821,738
NET CURRENT (LIABILITIES)/ASSETS		**(107,196)**	48,672
TOTAL ASSETS LESS CURRENT LIABILITIES		**1,309,832**	1,646,114
NON-CURRENT LIABILITIES			
Convertible notes	*14*	**194,824**	91,717
Provision for contingent consideration	*15*	**268,565**	422,285
Deferred tax liability		**3,071**	3,071
		466,460	517,073
NET ASSETS		**843,372**	1,129,041
EQUITY			
Share capital		**71,629**	70,555
Reserves		**771,743**	1,058,486
TOTAL EQUITY		**843,372**	1,129,041

NOTES:

1. CORPORATE INFORMATION

The Company is a limited liability company incorporated in the Cayman Islands. The registered office address of the Company is located at Cricket Square, Hutchins Drive, P.O. Box 2681, Grand Cayman KY1-1111, Cayman Islands. The Company's principal places of business are located in Huoju Industrial Zone, Jiangnan Town, Licheng District, Quanzhou City, Fujian Province, the People's Republic of China ("PRC") and Room 504, 5/F, OfficePlus @Sheung Wan, 93-103 Wing Lok Street, Sheung Wan, Hong Kong. The shares of the Company were listed on the Main Board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") on 28 January 2011.

The principal activity of the Company is investment holding. The Group is involved in the manufacture and sale of slippers, sandals, casual footwear and graphene-based ethylene-vinyl acetate ("EVA") foam material.

In the opinion of the Directors, the immediate holding company and the ultimate holding company of the Company is Best Mark International Limited, which was incorporated in the British Virgin Islands. Its ultimate controlling party is Mr. Sze Ching Bor.

2. BASIS OF PREPARATION

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs") issued by the International Accounting Standards Board ("IASB"). In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules") and by the Hong Kong Companies Ordinance.

As at 31 December 2016, the Group's current liabilities exceeded its current assets by approximately RMB107,196,000. The Group incurred a loss for the year of RMB317,578,000. These conditions indicate the existence of a material uncertainty which may cast significant doubt on the Group's ability to continue as a going concern and therefore, the Group may not be able to realise its assets and discharge its liabilities in the normal course of business.

In view of such circumstances, the Directors of the Company have given careful consideration to future liquidity and performance of the Group and its available sources of financing in assessing whether the Group will be able to finance its future working capital and finance requirements. Certain measures have been taken to manage its liquidity needs and to improve its financial position which include, but are not limited to, the following:

2. BASIS OF PREPARATION *(continued)*

1. The Group obtains facilities from financial institutions to extend existing borrowings upon their maturities. The Group will actively negotiate with the PRC banks for the renewal of the Group's PRC bank borrowings when they fall due to secure necessary facilities to meet the Group's working capital and financial requirements in the near future. The Directors have evaluated all the relevant facts available to them and are of the opinion that the Group has a good track record or relationship with the banks which will enhance the Group's ability to renew the Group's PRC bank borrowings upon expiry;

2. The Group will implement operation plans to control costs and generate adequate cash flows from the Group's operations; and

3. As detailed in note 16, the Group obtained a new facility of RMB40,000,000 from a financial institution.

The Directors have reviewed the Group's cash flow projections prepared by management. The cash flow projections cover a period of not less than twelve months from the end of the reporting period. The Directors are of the opinion that, taking into account the above-mentioned plans and measures, the Group would have sufficient working capital to finance its operations and to meet its financial obligations as and when they fall due within the next twelve months from the end of the reporting period. Accordingly, the Directors are of the opinion that it is appropriate to prepare the consolidated financial statements for the year ended 31 December 2016 on a going concern basis.

The Group has applied new and revised IFRSs, which include IFRS(s), International Accounting Standards ("IAS(s)") and Interpretations ("Int"), issued by the IASB for the first time in the current year.

Amendments to IFRS 10, IFRS 12 and IAS 28	Investment Entities: Applying the Consolidation Exception
Amendments to IFRS 11	Accounting for Acquisitions of Interests in Joint Operations
Amendments to IAS 1	Disclosure Initiative
Amendments to IAS 16 and IAS 38	Clarification of Acceptable Methods of Depreciation and Amortisation
Amendments to IAS 16 and IAS 41	Agriculture: Bearer Plants
IFRSs (Amendments)	Annual Improvements to IFRSs 2012-2014 Cycle

2. BASIS OF PREPARATION *(continued)*

The application of the new and revised IFRSs in the current year has had no material impact on the Group's financial performance and positions for the current and prior years and/or on the disclosures set out in these consolidated financial statements.

3. SEGMENT INFORMATION

Information reported to the Directors, being the chief operating decision maker (the "CODM"), for the purposes of resource allocation and assessment of segment performance focuses on types of goods or services delivered or provided. Specifically, the Group's reportable and operating segments are as follows:

(a) the Boree branded products segment manufactures and sells Boree branded slippers, sandals and casual footwear ("Boree Products");

(b) the Baofeng branded products segment manufactures and sells Baofeng branded slippers ("Baofeng Products");

(c) the Graphene-based products segment applied the technology know-how by applying graphene in the production of graphene-based EVA foam material with sterilizing, good elasticity and tear resistant functions ("Graphene-based Products"); and

(d) the Original Equipment Manufacturer ("OEM") segment produces slippers for branding and resale by others.

CODM monitors the results of the Group's operating segments separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on reportable segment result, which is a measure of adjusted result before tax.

The segment profit or loss represents the profit earned by or loss from each segment without allocation of interest income, other unallocated net income and gains, amortisation of intangible assets, impairment loss on intangible assets, fair value change on convertible notes, warrants and provision for contingent consideration at fair value through profit or loss ("FVTPL"), finance costs as well as corporate and other unallocated expenses.

Segment assets exclude property, plant and equipment, prepaid land lease payments, intangible assets, raw materials, work in progress, prepayments, deposits and other receivables, pledged deposits and cash and bank balances as these assets are managed on a group basis.

Segment liabilities exclude trade and bills payables, certain other payables and accruals, interest-bearing bank borrowings, convertible notes, warrants, income tax payable, deferred tax liability and provision for contingent consideration as these liabilities are managed on a group basis.

3. SEGMENT INFORMATION *(continued)*

Regarding the brand licensee business segment presented for the year ended 31 December 2015, it is not reported in the current year since it ceased operation in 2015.

Year ended 31 December 2016

	Boree Products *RMB'000*	Baofeng Products *RMB'000*	Graphene-based Products *RMB'000*	OEM *RMB'000*	Total *RMB'000*
Segment revenue					
Sales to external customers	**2,698**	**–**	**43,171**	**169,962**	**215,831**
Segment results	**(3,948)**	**–**	**27,133**	**43,526**	**66,711**
Reconciliation:					
Interest income					**1,072**
Other unallocated net income and gains					**2,434**
Corporate and other unallocated expenses					**(51,916)**
Amortisation of intangible assets					**(105,401)**
Impairment loss on intangible assets					**(325,616)**
Fair value loss on convertible notes and warrants at FVTPL					**(31,173)**
Fair value gain on provision for contingent consideration at FVTPL					**141,915**
Finance costs					**(7,933)**
Loss before tax					**(309,907)**
Segment assets	**1,497**	**–**	**33,011**	**48,340**	**82,848**
Reconciliation:					
Corporate and other unallocated assets					**1,451,743**
Total assets					**1,534,591**
Segment liabilities	**300**	**–**	**–**	**–**	**300**
Reconciliation:					
Corporate and other unallocated liabilities					**690,919**
Total liabilities					**691,219**

3. SEGMENT INFORMATION *(continued)*

Year ended 31 December 2015

	Boree Products *RMB'000*	Baofeng Products *RMB'000*	Graphene-based Products *RMB'000*	OEM *RMB'000*	Total *RMB'000*
Segment revenue					
Sales to external customers	27,849	–	–	143,806	171,655
Segment results	5,172	–	–	25,769	30,941
Reconciliation:					
Interest income					4,454
Other unallocated net income and gains					8,637
Corporate and other unallocated expenses					(36,078)
Amortisation of intangible assets					(6,501)
Fair value loss on convertible notes and warrants at FVTPL					(13,451)
Finance costs					(7,848)
Loss before tax					(19,846)
Segment assets	9,734	–	–	42,940	52,674
Reconciliation:					
Corporate and other unallocated assets					2,415,178
Total assets					2,467,852
Segment liabilities	150	150	–	–	300
Reconciliation:					
Corporate and other unallocated liabilities					1,338,511
Total liabilities					1,338,811

3. SEGMENT INFORMATION *(continued)*

Geographical information

(a) Revenue from external customers

	2016	2015
	RMB'000	*RMB'000*
PRC (principal place of operations)	**49,369**	27,561
United States of America ("US")	**162,750**	128,416
South America	**402**	800
Europe	**335**	1,087
South East Asia	**471**	10,111
Other countries	**2,504**	3,680
	215,831	171,655

The revenue information above is based on the locations of the customers.

(b) Non-current assets

	2016	2015
	RMB'000	*RMB'000*
PRC (principal place of operations)	**1,417,018**	1,597,420

The non-current assets information above is based on the locations of the assets.

Information about major customers

Revenue from customers of the corresponding years contributing over 10% of the total sales of the Group are as follows:

	2016	2015
	RMB'000	*RMB'000*
Customer A	**69,330**	71,475
Customer B	**22,359**	19,798
Customer C	**32,717**	18,079
Customer D*	**51,185**	16,380

* Revenue from Customer D contributed less than 10% of the total sales of the Group for the year ended 31 December 2015.

Except Customer C in the Boree Products and Graphene-based Products segments, the Group's other major customers are in the OEM segment.

4. REVENUE, OTHER NET INCOME AND GAINS

Revenue, which is also the Group's turnover, represents the net invoiced value of goods sold, after allowances for returns and trade discounts.

An analysis of revenue, other net income and gains is as follows:

	2016	2015
	RMB'000	*RMB'000*
Revenue		
Manufacture and sale of goods	**215,831**	171,655
Other net income and gains		
Interest income	**1,072**	4,454
Sales of scrap material	**646**	1,912
Sales of semi-products	**–**	188
Rental income	**515**	462
Subsidy income*	**190**	500
Exchange gain	**917**	1,976
Others	**166**	3,599
	3,506	13,091

* *There are no unfulfilled conditions or contingencies relating to these subsidies.*

5. FINANCE COSTS

	2016	2015
	RMB'000	*RMB'000*
Interest on bank loans repayable within five years	**7,933**	7,848

6. LOSS BEFORE TAX

The Group's loss before tax is arrived at after charging/(crediting):

	2016	2015
	RMB'000	*RMB'000*
Cost of inventories sold*	**138,526**	134,156
Depreciation*	**7,922**	8,069
Amortisation of prepaid land lease payments	**845**	845
Amortisation of intangible assets	**105,401**	6,501
Minimum lease payments under operating leases in respect of land and buildings*	**475**	3,457
Employee benefit expenses (including directors' remuneration)*:		
Wages and salaries	**47,844**	44,490
Equity-settled share option expense	**20,712**	9,466
Staff welfares	**275**	314
Contributions to retirement benefits schemes	**1,478**	1,462
	70,309	55,732
Auditors' remuneration	**1,103**	1,467
Impairment loss on intangible assets	**325,616**	–
Impairment loss on other receivables	**165**	–
Impairment loss on trade receivables	**2,065**	218
Write-down/(reversal of write-down) of inventories	**2,003**	(5,410)
Loss on disposals of items of property, plant and equipment	**6**	1
Exchange gain, net	**(917)**	(1,976)
Research and development costs**	**5,436**	2,231

* *The cost of inventories sold for the year ended 31 December 2016 includes approximately RMB37,202,000 (2015: RMB38,607,000) relating to direct staff costs, depreciation of manufacturing facilities and operating lease payments in respect of land and buildings, which are also included in the respective total amounts disclosed above for each of these types of expenses.*

** *The research and development costs are included in "General and administrative expenses" in the consolidated statement of profit or loss and other comprehensive income.*

7. INCOME TAX EXPENSE

No provision for Hong Kong profits tax has been made as the Group's tax losses brought forward from prior years exceeded the assessable profits arising in Hong Kong for the year (2015: Nil). Taxes on profits assessable in the PRC have been calculated at the prevailing rates, based on existing legislation, interpretations and practices in respect thereof.

	2016	2015
	RMB'000	*RMB'000*
Current – PRC		
Charge for the year	**7,569**	3,399
Under-provisions in prior years	**102**	2,424
Total tax charge for the year	**7,671**	5,823

8. DIVIDEND

No dividend was proposed for the years ended 31 December 2016 and 2015 and since the end of the reporting period.

9. LOSS PER SHARE

The calculation of basic loss per share is based on the consolidated loss for the year attributable to owners of the Company and the weighted average number of ordinary shares of 1,080,827,914 (2015: 1,043,644,473) in issue during the year.

The weighted average number of ordinary shares used to calculate the basic loss per share for the year ended 31 December 2016 included the 1,067,579,608 ordinary shares in issue as at 1 January 2016, and 16,200,000 ordinary shares and 280,000 ordinary shares issued on 9 March 2016 and 17 October 2016 respectively in respect of the exercise of share options.

The weighted average number of ordinary shares used to calculate the basic loss per share for the year ended 31 December 2015 included the 1,013,720,833 ordinary shares in issue as at 1 January 2015, and 31,194,997 ordinary shares and 22,663,778 ordinary shares issued on 8 June 2015 and 18 June 2015 in respect of the exercise of the conversion rights attached to the convertible notes.

During the years ended 31 December 2016 and 2015, diluted loss per share does not assume the exercise of the Company's share options and convertible notes as the exercise of the Company's share options and convertible notes would result in a decrease in loss per share, and is regarded as anti-dilutive.

10. INTANGIBLE ASSETS

	Technology Know-how (*note a,c*) *RMB'000*	O2O distribution vending system (*note b,c*) *RMB'000*	Deferred development costs (*note d*) *RMB'000*	Total *RMB'000*
Cost:				
At 1 January 2015	–	–	–	–
Addition during the year	1,483,117	–	–	1,483,117
At 31 December 2015 and 1 January 2016	1,483,117	–	–	1,483,117
Addition during the year	104,401	60,000	92,378	256,779
At 31 December 2016	1,587,518	60,000	92,378	1,739,896
Accumulated amortisation and impairment:				
At 1 January 2015	–	–	–	–
Provided for the year	6,501	–	–	6,501
At 31 December 2015 and 1 January 2016	6,501	–	–	6,501
Provided for the year	105,401	–	–	105,401
Impairment loss for the year	325,616	–	–	325,616
At 31 December 2016	437,518	–	–	437,518
Net carrying amount:				
At 31 December 2016	1,150,000	60,000	92,378	1,302,378
At 31 December 2015	1,476,616	–	–	1,476,616

Note:

(a) It represented certain technological know-how in respect of the application of graphene and includes one patent in the US ("US Patent"), four invention patent applications, three utility model patent applications and two utility model patents in the PRC (collectively as "PRC Patents"), relating to the manufacturing of graphene-based EVA foam material, graphene deodorizing and sterilizing chips and graphene-based pressure-sensitive sensors and the exclusive formula (collectively "Technology Know-how"), which was acquired from Bluestone Technologies (Cayman) Limited ("Bluestone"), an independent third party, in 2015.

10. INTANGIBLE ASSETS *(continued)*

Note: (continued)

(a) *(continued)*

The completion date of the transaction ("Completion Date") was 16 December 2015. The cost of the Technology Know-how was determined by the Directors and represented the sum of the cash consideration, the fair value of the convertible notes (note 14) and provision for contingent consideration at the acquisition date (note 15), and the capitalised transaction costs arising directly from the acquisition of the Technology Know-how. During the year, addition of the Technology Know-how represented the capitalisation of imputed interest of discounting the contingent consideration until the commencement of the use of the Technology Know-how. The Group's first graphene application products mass production line was completed and commenced trial production in late May 2016, and mass production has already been commenced in July 2016.

The Technology Know-how has definite useful lives and is amortised over 10 years using the straight-line method.

(b) In July 2016, the Group acquired the design of Online-to-Offline ("O2O") distribution vending system at the consideration of RMB60,000,000 from two independent third parties. Directors consider that the O2O distribution vending system would provide customers with an interactive and unique shopping experience, enhance the distribution channel of the products made by the Group and establish the core technical competitiveness of the Group.

(c) The Directors consider that the Technology Know-how and O2O distribution vending system belong to the O2O cash generating unit (the "Cash-generating Unit"), being the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets.

The Directors conducted an impairment assessment on the Cash-generating Unit and considered that provision for impairment to the carrying amount of the Cash-generating Unit of RMB325,616,000 was made as at 31 December 2016, with reference to a valuation of the value in use of the Cash-generating Unit conducted by an independent professional valuer, Ascent Partners Valuation Service Limited ("Ascent Partners"), using discounted cash flow approach. The discounted cash flow approach is based on a pre-tax discount rate of 31.21% and cash flow projections prepared from financial forecasts approved by the Directors. Since the business model for the Cash-generating Unit is changed from supplying of EVA foam materials in 2015 to retail of slippers through O2O distribution vending system and manufacturing EVA foam materials in 2016, assumption of budgeted sales was changed from the estimated sales order from shoes, slippers and luggage manufacturers to daily average sales of slippers from each O2O distribution vending system. Other key assumptions for the discounted cash flow approach relate to the estimation of cash inflows/outflows which include gross margin, such estimation is based on the expected and forecasted performance generated from the use of the Cash-generating Unit and management's expectations for the market development.

10. INTANGIBLE ASSETS *(continued)*

Note: (continued)

(d) In July 2016, the Group engaged several independent third parties in the research and development of manufacturing and application technology of graphene material on sterilizing chips, energy storage materials for batteries and pressure sensitive lighting devices for shoes. The Directors seek the opportunities in applying the graphene material in products other than shoes and plan to launch in the coming years.

The Directors estimated the value in use of the deferred development costs for impairment assessment purpose using discounted cash flow approach and concluded that no provision for impairment to the carrying amount of the deferred development costs was made at 31 December 2016.

11. TRADE RECEIVABLES

The Group's trading terms with its customers are mainly on credit. The credit period offered to its customers is generally for a period of three months. The Group seeks to apply strict control over its outstanding receivables and has a credit control department to minimise credit risk. Overdue balances are reviewed regularly by senior management. In view of the aforementioned and the fact that the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. The Group does not hold any collateral or other credit enhancements over its trade receivable balances. Trade receivables are non-interest-bearing.

An aged analysis of the Group's trade receivables, net of allowance for doubtful debts as at the end of the reporting period, based on the invoice date, is as follows:

	2016	2015
	RMB'000	*RMB'000*
Within 3 months	**38,208**	32,845
4 to 6 months	**33,063**	1,935
7 to 12 months	**4,861**	4,254
	76,132	39,034

12. TRADE AND BILLS PAYABLES

An aged analysis of the Group's trade and bills payables as at the end of the reporting period, based on the invoice date, is as follows:

	2016	2015
	RMB'000	*RMB'000*
Within 3 months	**36,998**	24,240
Over 3 months	**16,891**	14,439
	53,889	38,679

The trade and bills payables are non-interest-bearing and are normally settled on six months terms (2015: six months). The bills payable of RMB14,277,000 (2015: RMB7,825,000) were secured by the Group's pledged deposits amounting to RMB4,283,000 as at 31 December 2016 (2015: RMB2,723,000).

13. INTEREST-BEARING BANK BORROWINGS

	2016	2015
	RMB'000	*RMB'000*
Secured bank loans repayable within one year	**124,000**	129,570

(a) At 31 December 2016, the bank loans were denominated in Renminbi (2015: Renminbi and US dollars) and bore fixed interest rates ranging from:

Year ended 31 December 2016	4.60% – 6.25% per annum
Year ended 31 December 2015	1.51% – 7.57% per annum

(b) At 31 December 2016, the secured bank loans of the Group were secured by a pledge of the Group's buildings and land use right, amounting to approximately RMB15,680,000 (2015: RMB18,945,000) and approximately RMB33,456,000 (2015: RMB34,301,000) respectively. In addition, the bank loans were guaranteed by an independent third party and Mr. Zheng Jingdong and his spouse.

14. CONVERTIBLE NOTES AND WARRANTS

Valuation of the Convertible Notes and the Warrants

The movements of the Convertible Notes and the Warrants were as follows:

	2012 Convertible Notes	**2015 Convertible Notes** *(note a)*	**2016 Convertible Notes** *(note a)*	**2012 Warrants** *(note b)*	**2015 Warrants** *(note b)*	**Total**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Fair value at 1 January 2015	53,123	–	–	4,137	–	57,260
Issued during the year	–	91,717	–	–	4,880	96,597
Converted during the year	(54,001)	–	–	–	–	(54,001)
Fair value loss charged to profit or loss during the year	878	–	–	7,009	5,564	13,451
Fair value at 31 December 2015 and 1 January 2016	–	91,717	–	11,146	10,444	113,307
Issued during the year	–	–	55,411	–	–	55,411
Fair value loss charged/(gain credited) to profit or loss during the year	–	25,177	22,519	(6,079)	(10,444)	31,173
Fair value at 31 December 2016	–	116,894	77,930	5,067	–	199,891
Represented by:						
Current portion	–	–	–	5,067	–	5,067
Non-current portion	–	116,894	77,930	–	–	194,824
	–	116,894	77,930	5,067	–	199,891

Note:

(a) In connection with the acquisition of the Technology Know-how as explained in note 10, the Company issued zero-coupon unsecured convertible notes (the "2015 Convertible Notes") with principal amount of HK$110,880,000 as part of the initial consideration on 16 December 2015. As a settlement of part of contingent consideration, the Company also issued zero-coupon unsecured convertible notes (the "2016 Convertible Notes") with principal amount of HK$73,920,000 on 2 February 2016.

The 2015 Convertible Notes and 2016 Convertible Notes (collectively as the "Convertible Notes") entitle the holder to convert them into the ordinary shares of the Company (the "Shares") at any time from the date of issue of the 2015 Convertible Notes and 2016 Convertible Notes to the date immediately prior to the maturity date on 16 December 2018 and 2 February 2019 respectively, being the third anniversary of the date of issue, in multiples of HK$1,000,000 at a conversion price of HK$0.84 per conversion share subject to adjustments in certain events. The shares to be allotted and issued upon conversions shall rank pari passu in all respects among themselves and with all other ordinary shares in issue by the Company on the date of such allotment and issue. Also, the Company has a right to redeem the Convertible Notes at any time before the maturity date of the Convertible Notes.

14. CONVERTIBLE NOTES AND WARRANTS *(continued)*

Valuation of the Convertible Notes and the Warrants *(continued)*

Note: (continued)

(a) *(continued)*

During the years ended 31 December 2016 and 2015, the Convertible Notes holder did not convert any Convertible Notes.

The Convertible Notes included a debt instrument with embedded derivatives. Upon initial recognition, the Convertible Notes are designated as financial liabilities at FVTPL since it contains embedded foreign exchange derivatives. The fair values of the Convertible Notes are remeasured at the end of each reporting period and any gains or losses arising from changes in fair value are recognised in the statement of profit or loss.

Valuation

As at 31 December 2016 and 2015, the fair values of the Convertible Notes were based on the valuations performed by Ascent Partners and calculated using the binomial model and the inputs into the model were as follows:

	2016	2015
2015 Convertible Notes		
Stock price (HK$)	**0.99**	0.77
Principal amount (HK$'000)	**110,880**	110,880
Coupon rate (%)	**0**	0
Conversion price (HK$)	**0.84**	0.84
Volatility (%)	**81.76**	74.08
Risk-free rate (% per annum)	**1.07**	0.74
Expected life (years)	**1.96**	3.00
Expected dividend yield (%)	**0**	0
2016 Convertible Notes		
Stock price (HK$)	**0.99**	N/A
Principal amount (HK$'000)	**73,920**	N/A
Coupon rate (%)	**0**	N/A
Conversion price (HK$)	**0.84**	N/A
Volatility (%)	**80.88**	N/A
Risk-free rate (% per annum)	**1.10**	N/A
Expected life (years)	**2.09**	N/A
Expected dividend yield (%)	**0**	N/A

14. CONVERTIBLE NOTES AND WARRANTS *(continued)*

Valuation of the Convertible Notes and the Warrants *(continued)*

Note: (continued)

(b) Pursuant to a subscription agreement entered into with Asia Equity Value Ltd (the "Subscriber") on 8 June 2012 (the "Subscription Agreement"), the Company issued a 7% senior guaranteed convertible notes with a principal amount of HK$176,000,000 (i.e. RMB143,470,000) (the "2012 Convertible Notes") to the Subscriber on 21 June 2012 (the "Issuance Date"). No 2012 Convertible Notes remained outstanding as at 31 December 2015. In addition, pursuant to the Subscription Agreement, the Company also issued to the Subscriber warrants (the "2012 Warrants") which carry the rights to subscribe for 62,026,431 new ordinary shares of the Company as a condition to the issuance of the 2012 Convertible Notes.

The 2012 Warrants initially give the holder of the 2012 Warrants (the "Warrants Holder") the rights to subscribe for 62,026,431 new Shares. The initial subscription price of the 2012 Warrants is HK$1.53 per share (the "Subscription Price"), subject to anti-dilution adjustment for stock dividends, stock splits, dilutive securities issuances and other customary adjustment events from time to time in accordance with the terms and conditions of the 2012 Warrants. The subscription period of the 2012 Warrants commences from 6 months after the Issuance Date (i.e. 22 December 2012) (the "Warrants Subscription Date"), and will mature on the fifth anniversary from the Warrants Subscription Date (i.e. 22 December 2017).

Upon the occurrence of any events of defaults or certain events as mentioned in the Subscription Agreement, the Warrants Holder may elect to require the Company to redeem or repurchase all or a portion of its 2012 Warrants at a price equal to the Black Scholes Value in respect of the relevant 2012 Warrants as mentioned in the Subscription Agreement.

On 7 February 2013, the Company had entered into a supplemental instrument with the Subscriber to amend certain major terms and conditions of the 2012 Warrants (the "Supplemental Warrants Instrument"). The Supplemental Warrants Instrument had been approved by the Subscriber as the sole holder of the 2012 Warrants in accordance with the terms and conditions of the 2012 Warrants. In accordance with the Supplemental Warrants Instrument, the Company and the Subscriber agreed that any adjustments to the Subscription Price should take effect if the adjustment is HK$0.01 or more. As a result of the above, the Subscription Price had been adjusted from HK$1.53 to HK$1.49 with effect from 12 October 2012 as a result of the distribution of the 2012 interim dividend of HK2.5 cents per ordinary share by the Company.

According to the agreement amongst the Subscriber and three independent third parties (the "Transferees") on 29 October 2014, the 2012 Warrants were also transferred from the Subscriber to the Transferees on 29 October 2014.

On 13 March 2015, the Company entered into a new warrants subscription agreement (the "2015 Warrants Subscription Agreement") with two warrants subscribers (the "2015 Warrants Subscribers") in relation to the issue of a total of 88,000,000 warrants (the "2015 Warrants") to the 2015 Warrants Subscribers at the issue price of HK$0.07 per 2015 Warrant. The subscription rights attaching to the 2015 Warrants was expired on 20 October 2016.

14. CONVERTIBLE NOTES AND WARRANTS *(continued)*

Valuation of the Convertible Notes and the Warrants *(continued)*

Note: (continued)

(b) *(continued)*

No warrants have been exercised during both years ended 31 December 2015 and 2016.

The 2012 Warrants and 2015 Warrants (collectively as the "Warrants") are classified as derivatives and are accounted for as financial liabilities at FVTPL upon initial recognition since it contains embedded foreign exchange derivatives. The fair values of the Warrants are remeasured at the end of each reporting period and any gains or losses arising from changes in fair value are recognised in the statement of profit or loss.

Valuation

As at 31 December 2016 and 2015, the fair values of the 2012 Warrants and 2015 Warrants were based on the valuations performed by Asset Appraisal Limited, which is an independent firm of professionally qualified valuers and calculated using the binomial model and the inputs into the model were as follows:

	2016	2015
2012 Warrants		
Stock price (HK$)	**0.99**	0.78
Exercise price (HK$)	**1.49**	1.49
Volatility (%)	**55.71**	82.61
Risk-free rate (% per annum)	**0.85**	0.36
Expected life (years)	**0.98**	1.98
Expected dividend yield (%)	**0**	0
2015 Warrants		
Stock price (HK$)	**N/A**	0.78
Exercise price (HK$)	**N/A**	1.50
Volatility (%)	**N/A**	105.99
Risk-free rate (% per annum)	**N/A**	0.11
Expected life (years)	**N/A**	0.81
Expected dividend yield (%)	**N/A**	0

15. PROVISION FOR CONTINGENT CONSIDERATION

In connection with the acquisition of the Technology Know-how as explained in note 10, provision for contingent consideration as at 31 December 2015 represented the acquisition-date fair value of contingent consideration of i) a maximum of approximately RMB1,289,409,836 in cash ("Cash Consideration"); and ii) the contingent convertible notes ("Contingent CNs") with principal amount of HK$73,920,000 (equivalent to approximately RMB60,590,164), which will be issued by the Company after fulfillment of certain conditions specified in the acquisition agreement signed on 14 October 2015 ("Acquisition Agreement"), as part of the consideration for the acquisition of the Technology Know-how.

The settlement of Cash Consideration and the Contingent CNs is subject to the following conditions:

"Second Instalment Conditions" refer to (a) the registration of the transfer of the PRC Patents and the US Patent having been completed in the State Intellectual Property Office of the PRC and the United States Patent and Trademark Office respectively, such that the Company having become the applicant of the PRC Patents (or if the PRC Patents are granted, the Company having become the PRC Patents owner) under the record of the State Intellectual Property Office of the PRC, and the Company having become the US Patent owner under the record of the United States Patent and Trademark Office; and (b) the training provided by Bluestone to the technicians of the Group and its contracted parties having been completed, such that the Group and its contracted parties having been able to produce graphene-based EVA foam material and graphene deodorizing and sterilizing chips based on the Technology Know-how independently, and the graphene-based EVA foam material and graphene deodorizing and sterilizing chips produced having been certified by an independent technical organisation at provincial level or above to meet the inspection standard as stipulated under the Acquisition Agreement.

Upon fulfilment of the Second Instalment Conditions, the second instalment in the amount of RMB450,000,000 shall be payable by the Company, of which (a) RMB389,409,836 shall be paid in cash within 6 months after fulfilment of the Second Instalment Conditions; and (b) RMB60,590,164 shall be satisfied by issuing the convertible notes with principal amount of HK$73,920,000 to Bluestone or its nominee(s) within 15 business days after the fulfillment of the Second Instalment Conditions.

15. PROVISION FOR CONTINGENT CONSIDERATION *(continued)*

"Third Instalment Conditions" refer to (a) the accumulated turnover of a special purpose vehicle ("SPV") to be established by the Group for the sales of graphene-based EVA foam material, graphene deodorizing and sterilizing chips and graphene-based wearable devices manufactured using the Technology Know-how and/or any other companies (other than companies of the Group) authorised to use the Technology Know-how having reached RMB40,000,000; and (b) the sales volume of graphene-based EVA foam material having reached 20,000 cubic meters, each within 9 months after the Completion Date (or such later date as the Company may agree).

Upon fulfilment of the Second Instalment Conditions and the Third Instalment Conditions, the third instalment in the amount of RMB270,000,000 shall be payable by the Company in cash to Bluestone or its nominee(s) within 15 business days after the fulfillment of the Third Instalment Conditions.

Second Instalment Conditions and Third Instalment Conditions have been fulfilled and the Company has paid RMB389,409,836 by way of cash and RMB60,590,164 by way of issuing the 2016 Convertible Notes (refer to note 14) and RMB270,000,000 by way of cash on 2 February 2016 and 8 September 2016 respectively.

Pursuant to the Acquisition Agreement, upon fulfilment of the Second Instalment Conditions and the Third Instalment Conditions, Bluestone is entitled to share 35% of the earnings before interests, taxes, depreciation and amortisation ("EBITDA") of the SPV for the 6-month period ended 30 June or 31 December of each year ("Interim Financial Period") during which the Second Instalment Conditions and the Third Instalment Conditions are fulfilled and each subsequent Interim Financial Period (until the end of the sixth financial year ending 31 December from the Completion Date), subject to a maximum sharing amount of RMB630,000,000 (the "EBITDA Sharing Mechanism").

For the avoidance of doubt, the financial year in which the Completion Date ending on would be considered as the first financial year for the purpose of the EBITDA Sharing Mechanism. During the period under the EBITDA Sharing Mechanism, for each Interim Financial Period, the Company should appoint an independent auditor to issue a certificate for the EBITDA of the SPV during the relevant Interim Financial Period within 4 months from the end of such Interim Financial Period, and the sharing amount shall be paid by the Company in cash to Bluestone or its nominee(s) within 15 business days after the issuance of such certificate. Any license fees for the Technology Know-how payable by the SPV to the Group will be disregarded in the calculation of the EBITDA.

If the accumulated EBITDA of the SPV during the period under the EBITDA Sharing Mechanism is less than RMB1,800,000,000 (for the purpose, if the SPV records a loss in any Interim Financial Period, the EBITDA of the SPV of that Interim Financial Period would be regarded as zero in calculating the accumulated EBITDA), the total sharing amount under the EBITDA Sharing Mechanism will be less than RMB630,000,000 and the Company is not obligated to pay the shortfall between RMB630,000,000 and 35% of the actual accumulated EBITDA of the SPV during the period under the EBITDA Sharing Mechanism.

15. PROVISION FOR CONTINGENT CONSIDERATION *(continued)*

Provision for contingent consideration as at 31 December 2016 represented the contingent cash consideration payable to Bluestone or its nominee(s) under the EBITDA Sharing Mechanism.

The movements of the provision for contingent consideration were as follows:

	2016	2015
	RMB'000	*RMB'000*
As at the beginning of the year	**1,029,203**	–
Acquired on acquisition of the Technology Know-how during the year	**–**	1,029,203
Settlement during the year	**(610,420)**	–
Fair value gain credited to profit or loss during the year	**(141,915)**	–
As at the end of the year	**276,868**	1,029,203
Current portion included in deposits received, other payables and accruals	**(8,303)**	(606,918)
Non-current portion	**268,565**	422,285

The fair value of the provision for contingent consideration is calculated using the binomial model. The inputs into the model as at 31 December 2016 and 2015 were as follows:

	2016	2015
Stock price (HK$)	**N/A**	0.77
Coupon rate (%)	**N/A**	0
Conversion price (HK$)	**N/A**	0.84
Expected dividend yield (%)	**N/A**	0
Expected volatility (%) *(note a)*	**N/A**	70.14
Expected life (years) *(note b)*	**N/A**	3.54
Risk free rate (% per annum) *(note c)*	**N/A**	0.83
Discount rate	**12.15% – 12.69%**	18.78%

15. PROVISION FOR CONTINGENT CONSIDERATION *(continued)*

Note:

(a) Expected volatility was determined by calculating the historical volatility of the Company's share price.

(b) Expected life was the expected remaining life of the Contingent CNs.

(c) The risk free rate for the Contingent CNs is determined by reference to the yield of the Hong Kong Generic Bond.

(d) All Contingent CNs have already been issued as at 31 December 2016.

The provision for contingent consideration is classified as a financial liability which will then be measured at fair value and any changes in fair value will be recognised in the consolidated statement of profit or loss.

The Directors conducted a fair value assessment of the provision for contingent consideration as at 31 December 2016, with reference to a valuation conducted by Ascent Partners.

16. EVENT AFTER FINANCIAL REPORTING DATE

The Group obtained a facility of RMB40,000,000 from a financial institution in June 2017 which was guaranteed by a subsidiary of the Group.

EXTRACT OF INDEPENDENT AUDITOR'S REPORT

The following is an extract from the report issued by Pan-China (H.K.) CPA Limited ("Pan-China"), the Company's auditor, on the consolidated financial statements of the Group for the year ended 31 December 2016:

We do not express an opinion on the consolidated financial statements of the Group. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, we are unable to form an opinion as to whether the consolidated financial statements give a true and fair view of the financial position of the Group as at 31 December 2016 and of the Group's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRSs") issued by the International Accounting Standards Board (the "IASB"). In all other respects, in our opinion the consolidated financial statements have been properly prepared in compliance with the disclosure requirements of the Hong Kong Companies Ordinance.

Basis for disclaimer of opinion

Limitation of Scope – Recognition of certain of the Group's intangible assets in accordance with International Accounting Standard 38 (IAS 38), "Intangible Assets" issued by the International Accounting Standard Board (the "IASB")

As disclosed in note 17 to the consolidated financial statements, the Group had incurred certain amount of costs of RMB92,378,000 during the year ended 31 December 2016 and capitalized these costs as intangible assets (labelled as "deferred development costs" in note 17 to the consolidated financial statements) (the "Deferred Development Costs"). The management of the Company represented to us that the Deferred Development Costs were incurred in relation to the research and development of manufacturing and application technology of graphene material on sterilizing chips, energy storage materials for batteries and pressure sensitive lighting devices for shoes and that the payments made in respect of these costs were made during the year ended 31 December 2016 to parties not considered as related parties in accordance with IAS 24 Related Parties Disclosures.

During the course of our audit of the consolidated financial statements of the Group for the year ended 31 December 2016, we were not provided with sufficient appropriate documentary evidence to satisfy ourselves about the bona fide nature of the costs incurred and details of the related development projects for which the costs were incurred. We were not provided with satisfactory explanations about the commercial substance of why such development costs were necessary to be incurred and the nature of the related development projects. Furthermore, IAS 38 requires a number of criteria to be satisfied before an entity can recognise development costs as an intangible asset (e.g. technical feasibility of completing the related project and how the costs incurred will generate probable future economic benefits etc.). Due to the lack of supporting documentary evidence, we were not provided with sufficient appropriate evidence regarding how the specified criteria set out in IAS 38 to justify the recognition of the Deferred Development Costs as an intangible asset had been satisfied and hence were not able to justify whether the Deferred Development Costs should be recognised as an intangible asset in accordance with IAS 38. There were no alternative audit procedures to satisfy ourselves concerning these matters.

Any adjustments that might have been found necessary in respect thereof would have a consequential effect on the net assets of the Group as at 31 December 2016, the results of the Group for the year ended 31 December 2016 and the related disclosures thereof in the consolidated financial statements.

Limitation of scope – Impairment assessment of the Group's intangible assets under International Accounting Standard 36 (IAS 36), "Impairment of assets" issued by the IASB

During the year ended 31 December 2016, an impairment loss of approximately RMB325,616,000 in respect of technology know-how intangible assets was recognised by the Group. The recoverable amounts of the Technology Knowhow and O2O distribution vending system intangible assets were determined based on the management's estimate of the value-in-use of the cash generating unit in which the technology knowhow and O2O distribution vending system intangible assets belonged, taking into account a valuation using a discounted cash flow approach. The recoverable amount of the Deferred Development Costs was determined based on the management's own estimate of the value-in-use of the Deferred Development Costs, as described in note 17 to the consolidated financial statements. After the impairment loss recognised by the Group, the aggregate carrying amount of the Group's intangible assets (labelled as "technology know-how", "O2O distribution vending system" and "Deferred Development Costs") as at 31 December 2016 amounted to RMB1,302,378,000 with the impairment loss of RMB325,616,000 being fully allocated by the management of the Company to the technology know-how.

During the year ended 31 December 2016, as represented by the management of the Company, the business models on how to realise the technology knowhow intangible assets had been changed from manufacturing and supplying of EVA foam materials to shoes, slippers and luggage manufacturers, to manufacturing and sales of plastic slippers through O2O distribution vending machines. We have not been able to obtain sufficient appropriate audit evidence to satisfy ourselves that the key assumptions (e.g. bases regarding the related forecasted revenue including the estimated sales prices and estimated sales quantity) adopted in the valuation of the cash generating unit referred to above were reasonable and supportable. The forecasted revenue was based on limited market data and in our view the other key assumptions used in the valuation did not adequately take into account the challenges in the operating environment that the Group will be facing in the future. Also, details on feasibility aspects of the marketing plans of the Intangible Assets provided to us were very limited.

Any deficit of recoverable amount compared to carrying amount would represent an impairment loss in accordance with IAS 36. However, in the absence of sufficient appropriate evidence regarding whether the key assumptions adopted were reasonable and supportable, we were unable to satisfy ourselves as to the appropriateness and sufficiency of the amount of impairment loss made in the consolidated financial statements as well as the allocation of the impairment losses to different classes of intangible assets. Any adjustments that might have been found necessary in respect thereof would have a consequential effect on the net assets of the Group as at 31 December 2016, the results of the Group for the year ended 31 December 2016 and the related disclosures thereof in the consolidated financial statements.

In addition, as the Intangible Assets as stated above were held by various subsidiaries of the Company, any adjustment on the carrying amounts of these assets found to be necessary would also affect the carrying amounts of the Company's interests in subsidiaries, which amounted to RMB893,338,000 as at 31 December 2016 as disclosed in note 39 to the consolidated financial statements and the amount of the Company's loss for the year then ended as disclosed in the Company's statement of changes in equity disclosed in note 39 to the consolidated financial statements.

Material uncertainty in relation to going concern

We draw attention to note 3 to the consolidated financial statements which indicates that the Group incurred a net loss of approximately RMB317,578,000 for the year ended 31 December 2016 and, as of that date, the Group's current liabilities exceeded its current assets by approximately RMB107,196,000. As explained in note 3 to the consolidated financial statements, these conditions indicate that a material uncertainty exists that may cast significant doubt on the Group's ability to continue as a going concern. Our opinion is not disclaimed on this matter.

MANAGEMENT DISCUSSION AND ANALYSIS

During the year, the Group focused on the graphene technology application and the development of graphene application products and successfully launched Graphene-based Products in June 2016. As the Graphene-based Products have received the market recognition, the sales performance of the Group has improved in the second half of 2016 and the revenue of the Graphene-based Products amounted to approximately RMB43.2 million in 2016. In addition, with the help of technology improvement to improve the product quality, the Group recorded an increase of the revenue in the OEM business, by approximately RMB26.2 million or 18.2%. Although the Group spent less effort on the marketing of the own branded products, resulting in a decrease in the sales of own branded products during the year by approximately RMB25.2 million, the Group's overall sales performance has improved by RMB44.1 million or 25.7% to approximately RMB215.8 million as compared with last year (2015: RMB171.7 million), with the commencement of the sales of Graphene-based Products and the increase in sales in OEM business.

During the year, the gross profit margin of the Group increased to 34.9% (2015: 25.0%), which was mainly attributable to the application of the graphene technology and the commencement of the sale of the Graphene-based Products with a higher gross profit margin than that of the traditional products, when compared with that in 2015.

Despite the substantial increase in gross profit of the principal business of the Group, the Group still recorded a substantial increase in net loss from approximately RMB25.7 million in 2015 to RMB317.6 million, which is mainly attributable to (i) share-based payment expenses of approximately RMB20.7 million (2015: RMB9.5 million) in relation to the share options granted by the Company on 10 December 2015, 24 June 2016 and 16 December 2016; (ii) amortisation of intangible assets of approximately RMB105.4 million (2015: RMB6.5 million) and impairment loss on intangible assets of approximately RMB325.6 million (2015: Nil) in relation to the acquisition of the Technology Know-how from Bluestone on 16 December 2015; (iii) the substantial increase in fair value loss on convertible notes and warrants at FVTPL of approximately RMB17.7 million; and (iv) offset by the fair value gain on provision for contingent consideration at FVTPL of approximately RMB141.9 million (2015: Nil).

FINANCIAL REVIEW

Revenue by Product Category

	2016 *RMB'000*	2015 *RMB'000*	Increase/ (decrease) *% change*
Revenue (Boree Products)	**2,698**	27,849	(90.3%)
Revenue (Graphene-based Products)	**43,171**	–	N/A
Revenue (OEM Business)	**169,962**	143,806	18.2%
Revenue (Total)	**215,831**	171,655	25.7%

Boree Products

The continuous slowdown of economic growth of the PRC and the change of local customers' shopping habit led to an adverse operating environment for the retail market in the PRC. The Boree brand, targeting the medium-to-high-end market of slippers, sandals and casual footwear, recorded a revenue for the year of approximately RMB2.7 million (2015: RMB27.8 million), representing a 90.3% decrease from the previous year. Decrease was due to less selling expenses spent on the marketing of Boree Products. The Group also shifted the resources to the new business segment line for the development and sales of Graphene-based Products during the year.

Graphene-based Products

Due to acquisition of Technology Know-how in December 2015, the Group has successfully applied the graphene technology and launched the Graphene-based Products in 2016. As the products have received the market recognition, the Graphene-based Products as a new business segment, contributed approximately RMB43.2 million sales revenue to the Group.

OEM Business

During the year, the sales of Group's OEM business increased by RMB26.2 million or 18.2% to approximately RMB170.0 million as compared with last year (2015: RMB143.8 million). Notwithstanding the labour cost and the raw material cost, as the major production cost of footwear, kept increasing during the year, the Group put effort to improve the technology to reduce production costs, maintaining its pricing competitiveness in the footwear market. Therefore, as more competitors were faded out in the market, the performance of the OEM business improved during the year.

FINANCIAL REVIEW *(continued)*

Selling and Distribution Expenses

During the year, selling and distribution expenses decreased by 28.2% to approximately RMB8.6 million as compared with that of last year (2015: RMB12.0 million), which accounted for 4.0% (2015: 7.0%) of the Group's revenue. The decrease was mainly attributable to less marketing activities held for the promotion of Boree Products.

General and Administrative Expenses

General and administrative expenses recorded an increase of approximately RMB15.8 million or 43.9% during the year as compared with that of last year (2015: RMB36.1 million), which was mainly attributable to share-based payment expenses of approximately RMB20.7 million (2015: RMB9.5 million) in relation to the share options granted by the Company on 10 December 2015, 24 June 2016 and 16 December 2016 and more research and development costs incurred during the year.

Liquidity and Financial Resources

During the year, net cash inflow from operating activities of the Group amounted to approximately RMB33.2 million (2015: net cash outflow of RMB4.3 million). As at 31 December 2016, cash and bank balances were approximately RMB4.8 million, representing a decrease of 99.4% as compared with the cash and bank balances as at the end of last year (2015: RMB789.8 million). The decrease was mainly due to the payment for the cash portion of the second and third instalment of the acquisition of the Technology Know-how of approximately RMB659.4 million and the payment for the deferred development cost for numerous products in relation to graphene technology during the year. As at 31 December 2016, around 57% and 35% of the Group's cash and bank balances were denominated in US Dollars and Renminbi. As at 31 December 2016, the interest-bearing bank borrowings of the Group were approximately RMB124.0 million (2015: approximately RMB129.6 million). All bank loans were denominated in Renminbi, with fixed interest rates and repayable within one year.

Capital Structure

As at 1 January 2016, there were 1,067,579,608 shares in issue and the Company carried a share capital of approximately RMB70,555,000. During the year, the Company issued a total of 16,480,000 shares to share option holders who exercised their share options. As at 31 December 2016, the Company had 1,084,059,608 shares in issue and a paid-up capital of approximately RMB71,629,000.

FINANCIAL REVIEW *(continued)*

Significant Investments, Material Acquisitions and Disposals

Saved for the acquisition of the Technology Know-how, O2O distribution vending system and deferred development cost as disclosed in note 10 to the financial results, the Group did not have any other significant investments, material acquisitions and disposals during the year.

Pledge of Assets

As at 31 December 2016, the bills payables were secured by a pledge of the Group's time deposits amounting to approximately RMB4.3 million (2015: RMB2.7 million). The bank borrowings of the Group were also secured by a pledge of the Group's buildings and land use right with a net carrying value of approximately RMB15.7 million (2015: RMB18.9 million) and approximately RMB33.5 million (2015: RMB34.3 million) respectively.

Contingent Liabilities

As at 31 December 2016 and 2015, there were no material contingent liabilities.

Foreign Exchange Risk

During the year, the sales of the Group were mainly denominated in US dollars and Renminbi. The cost of sales and operating expenses were mainly denominated in Renminbi. Management of the Group monitors the foreign exchange risk and will consider hedging significant foreign currency risk exposure if necessary.

Gearing Ratio

As at 31 December 2016, the gearing ratio of the Group was 44.6% (2015: 54.2%). Gearing ratio was calculated as total debt divided by the total equity plus total debt. Total debt refers to the total liability minus the sum of tax payable, dividend payable and deferred tax liability.

FINANCIAL REVIEW *(continued)*

Human Resources

As at 31 December 2016, the Group had a total of approximately 840 employees (2015: 900 employees), with total staff costs for the year ended 31 December 2016, including directors' remuneration, amounted to approximately RMB70,309,000 (2015: RMB55,732,000). The Group's emolument policies are based on the merit, qualifications and competence of individual employee and are reviewed by the remuneration committee periodically. The emoluments of the Directors are recommended by the remuneration committee and are decided by the Board, having regard to the Group's operating results, individual performance and comparable market statistics. The Company also adopted a share option scheme on 8 January 2011 to motivate and reward its Directors and eligible employees.

Use of Net Proceeds from the Share Offering

As at 31 December 2016, the Company had unutilised net proceeds from the Initial Public Offering ("IPO") in the amount of approximately RMB67.4 million, representing approximately 17.4% of the total net proceeds from the IPO (the "Unutilised Net Proceeds"). As disclosed in the announcement dated 8 September 2016, approximately RMB73.4 million of the Unutilised Net Proceeds were originally intended to be used to acquire other branded product business and establish flagship shops and showrooms. The Company believed that such intended use no longer met the Group's imminent business development needs. In view of the fulfillment of the Third Instalment Conditions of in relation to the acquisition of the Technology Know-how, the Board had resolved to change the proposed use of such RMB73,443,000 and apply them for the partial settlement of the third instalment of the consideration for the acquisition of the Technology Know-how. In light of current market conditions of footwear industry in the PRC, the Company believes that the use of the Unutilised Net Proceeds under the original intended purpose may no longer meet the Group's imminent business development needs. In order to maximise the benefits of the Company and its shareholders, the Company may change the usage of the Unutilised Net Proceeds from the original intended purposes to working capital and other general corporate purposes of the Group. If this happen, further announcements will be made by the Company as and when appropriate in compliance with the Listing Rules on the Stock Exchange.

The Shares were listed on the main board of the Stock Exchange on 28 January 2011 with net proceeds received by the Company from the share offering of HK$453,570,000 (approximately RMB387,666,000) (after deducting underwriting commission and related expenses).

FINANCIAL REVIEW *(continued)*

The utilisation of the net proceeds as at 31 December 2016 is set out as follows:

Nature	**Amount raised** *RMB'000*	**Amount utilised** *RMB'000*
To increase production capacity	135,683	88,311
Marketing and advertising expenses	96,917	96,917
To acquire other branded product business (changed to "To settle the payment of the acquisition of the Technology Know-how" as detailed in the announcement dated 8 September 2016)	58,150	58,150
To strengthen design capability	19,383	14,297
To establish flagship shops and showrooms (changed to "To settle the payment of the acquisition of the Technology Know-how" as detailed in the announcement dated 8 September 2016)	19,383	19,383
To strengthen the distribution resource planning system	19,383	4,409
General working capital	38,767	38,767
Total:	387,666	320,234

Use of Net Proceeds from the Issue of 2015 Warrants

The net proceeds from the issue of 2015 Warrants of approximately HK$6,000,000 was intended to be retained in Hong Kong as general working capital of the Company and its offshore subsidiaries incorporated in Hong Kong and overseas (the "Offshore Group Members") to settle the expenses such as administrative expenses, the professional fees and the salary expenses incurred by the Offshore Group Members. The net proceeds of approximately HK$6,000,000 from the issue of 2015 Warrants had been fully utilised for general working capital of the Offshore Group Members to settle the expenses such as administrative expenses, the professional fees and the salary expenses incurred by the Offshore Group Members during the year ended 31 December 2015. All warrants from the issue of 2015 Warrants have been expired as at 31 December 2016. No 2015 Warrants have been exercised during both years ended 31 December 2015 and 2016.

FUTURE PROSPECTS

As the Group targets to expand its business from traditional industries to high technology industries to create long-term benefits for the Group, after the acquisition of the Technology Know-how from Bluestone in December 2015, the Group focused on the graphene technology application and the development of graphene application products in 2016. Graphene-based Products were successfully launched in June 2016 and have received the market recognition. In addition, with the help of technology improvement to improve the product quality, the Group recorded an increase of the revenue in the OEM business. Due to these two major reasons, the sales performance of the Group has improved in 2016 despite the slow-down of China's economic growth. Besides, due to the higher gross profit margin of Graphene-based Products, the gross profit margin of the Group increased to 34.9% in 2016 from 25.0% in 2015.

In order to develop different types of graphene application products, the Group engaged several independent third parties in the research and development of manufacturing and application technology of graphene material on sterilizing chips for air purifiers and air conditioners, energy storage materials for batteries and pressure sensitive lighting devices for shoes in 2016. The Directors seek the opportunities in applying the graphene material in products other than EVA foam material and slippers and plan to launch in the coming years.

In the coming year, the Group would deploy more resources in upgrading its technology and cooperate with different professional parties to develop and launch more and more innovative graphene application products in order to gradually transform the Company from a traditional manufacturing company to a high technology company. Besides, the Group would focus on promoting the graphene technology application and the development of graphene application products in order to develop new markets and new business. The Group targets to seek for opportunities to cooperate with different branded sports shoes manufacturers and household products manufacturers to develop graphene application products for sports shoes and household products. Besides, the Group targets to cooperate with textile enterprises to develop textile products with new functions.

Regarding the existing slipper business, as the slippers retail industry experiences stiff competition from online retailers, the Group continuously develops different types of distribution channels and decided to focus on developing O2O business model for the sales and distribution of slippers. The Group has engaged a PRC domestic company to design and develop the do-it-yourself ("DIY") automated vending system which is the key machine for the O2O business model. The Directors consider that the introduction of the DIY automated vending system is an innovative business model which combines the new retail method and customised and personalised features. The Directors are of the view that the introduction of the DIY automated vending system for selling our own branded automated customised graphene-based slippers ("Graphene-based Slippers") will contribute to the Group in the following three areas:

1. Market interaction model: The DIY automated vending system will provide customers with tailor-made interactive and unique shopping experience;

2. Business model: The business model of the DIY automated vending system is likely to replace the traditional shop sales model with the benefit of lower operating cost, higher gross profit margin and immediate cash inflow and establishes another essential and effective distribution channel for the products of the Group; and

3. Product technology: The graphene-based sterilizing foam material of Graphene-based Slippers will provide a better experience to customers and will establish the core technical competitiveness of the Group.

The Group considers that DIY automated vending system is an effective and efficient way of selling the Graphene-based Slippers and can maximize the profit of the Group. With the above benefits, the Group focused on the development of DIY automated vending system for the sales and distribution of Graphene-based Slippers in the first half of 2017 and decided to mainly use graphene-based sterilizing foam material for the production of Graphene-based Slippers and would reduce the sales of graphene-based sterilizing foam material directly to customers in the coming years.

In the first half of 2017, the trial run of the first generation of the DIY automated vending system was completed and based on the trial run data and feedback from customers, improvement and upgrade on the automated vending system hardware and software was made and the second generation of the DIY automated vending system was launched in July 2017. Besides, the Group engaged a market research company to perform a market research on the China's O2O slippers vending machines market. The Group based on the market analysis data and consumer survey of this report to position our products and according to the target customers' preferences to choose the locations of DIY automated vending system. As the Group targets to greatly increase the number of DIY automated vending system and will launch marketing campaign with more resources on the Graphene-based Slippers, the Directors expect that sales of the Group will improve in the second half of 2017.

In the coming years, the Group would continue deploy more resources on the research and development of graphene application products in order to enhance the leading position in this area. The Board is of the view that the combination of graphene technology with conventional industry would enhance the competitiveness and long term development of the Group and help the Group to generate more revenue and profit in the future.

CORPORATE GOVERNANCE

The Board and the management of the Company are committed to the maintenance of good corporate governance practices and procedures. The Company believes that good corporate governance provides a framework that is essential for effective management, a healthy corporate culture, successful business growth and enhancing shareholders' value.

Throughout the year ended 31 December 2016, the Company has complied with the code provisions as set out in the Corporate Governance Code (the "CG Code") contained in Appendix 14 to the Listing Rules, save for the deviations as detailed below. The Company periodically reviews its corporate governance practices to ensure its continuous compliance.

Code Provision A.2.1 stipulates that the roles of the Chairman and Chief Executive Officer should be separated and should not be performed by the same individual. The Company deviates from this provision because Mr. Zheng Jingdong has been performing both the roles of Chairman and Chief Executive Officer. The Directors consider that vesting two roles in the same person provides the Group with strong and consistent leadership in the development and execution of the Group's business strategies and is beneficial to the Group. The balance of power and authorities is ensured by the operation of the senior management and the Board, which comprise experienced and high caliber individuals. The Board currently comprises 2 executive Directors, 1 non-executive Director and 3 independent non-executive Directors and therefore has a strong independence element in its composition.

Code Provision A.6.7. stipulates that non-executive Directors and independent non-executive Directors should attend annual general meeting and develop a balanced understanding of the views of the shareholders of the Company. The Company deviates from this provision because the then non-executive Director, Mr. Chan Chak Chak Daniel, was unable to attend the annual general meeting held on 8 June 2016 due to his other business commitments.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 to the Listing Rules (the "Model Code") as the required standard for securities transactions by the Directors. The Company made specific enquiries of all the Directors and each of them confirmed that they have complied with the required standards set out in the Model Code during the financial year ended 31 December 2016.

AUDIT COMMITTEE

The audit committee was established by the Board with written terms of reference in compliance with the CG Code as set out in Appendix 14 to the Listing Rules. The primary duties of the audit committee are to review and supervise our Group's financial reporting process and risk management and internal control systems and review and monitor appointment of the auditors and their independence. As at 31 December 2016, the audit committee comprised three independent non-executive Directors, namely Mr. Chen Shaohua, Professor Zhao Jinbao and Ms. An Na, and Mr. Chen Shaohua was the chairperson of the audit committee. The annual results of the Group for the year ended 31 December 2016 have been reviewed by the audit committee.

REVIEW OF THIS ANNUAL RESULTS ANNOUNCEMENT

This preliminary announcement have been agreed by the Group's auditor, Pan-China, Certified Public Accountants, to the amounts set out in the Group's consolidated financial statements for the year and the amounts were found to be in agreement. The work performed by Pan-China in this respect did not constitute an audit, review or other assurance engagement in accordance with Hong Kong Standards on Auditing, Hong Kong Standards on Review Engagements or Hong Kong Standards on Assurance Engagements issued by the Hong Kong Institute of Certified Public Accountants and consequently no assurance has been expressed by the auditor on this preliminary announcement. The auditor disclaimed an opinion and an extract of its report is reproduced on pages 25 to 27 of this announcement.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

During the year ended 31 December 2016, neither the Company nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities.

DIVIDEND

The Board does not recommend the payment of a final dividend for the year ended 31 December 2016.

ANNUAL GENERAL MEETING

A notice convening the annual general meeting will be published on the websites of the Stock Exchange and the Company and despatched to the shareholders of the Company in the manner as required by the Listing Rules in due course.

PUBLICATION OF ANNUAL RESULTS ANNOUNCEMENT AND ANNUAL REPORT

The annual results announcement is available for viewing on the website of the Stock Exchange and the website of the Company at http://www.baofengmodern.com. The annual report of the Company will be despatched to shareholders of the Company in due course.

On behalf of the Board
Baofeng Modern International Holdings Company Limited
Zheng Jingdong
Chairman

Hong Kong, 28 July 2017

As at the date of this announcement, the executive Directors are Mr. Zheng Jingdong and Mr. Leung Tsz Chung; the non-executive Director is Ms. Lin Weihuan; and the independent non-executive Directors are Professor Zhao Jinbao, Mr. Chen Shaohua and Ms. An Na.