# YOUYUAN INTERNATIONAL HOLDINGS LIMITED
# 優源國際控股有限公司

*(incorporated in the Cayman Islands with limited liability)*
Stock Code: 2268

## GLOBAL OFFERING

Sole Global Coordinator, Sponsor,
Bookrunner and Lead Manager

HSBC

# IMPORTANT

*If you are in any doubt about any of the contents of this prospectus, you should obtain independent professional advice.*

优源
YOUYUAN

# Youyuan International Holdings Limited

# 優源國際控股有限公司

*(incorporated in the Cayman Islands with limited liability)*

## GLOBAL OFFERING

| | | |
|---|---|---|
| **Number of Offer Shares under the Global Offering** | : | **250,000,000 Shares (subject to the Over-allotment Option)** |
| **Number of Hong Kong Offer Shares** | : | **25,000,000 Shares (subject to adjustment)** |
| **Number of International Offer Shares** | : | **225,000,000 Shares (subject to adjustment and the Over-allotment Option)** |
| **Maximum Offer Price** | : | **HK$3.38 per Offer Share payable in full on application in Hong Kong dollars, subject to refund, plus brokerage of 1%, SFC transaction levy of 0.004%, and Stock Exchange trading fee of 0.005%** |
| **Nominal value** | : | **HK$0.10 each** |
| **Stock Code** | : | **2268** |

**Sole Global Coordinator, Sponsor, Bookrunner and Lead Manager**

HSBC

The Stock Exchange of Hong Kong Limited and Hong Kong Securities Clearing Company Limited take no responsibility for the contents of this prospectus, make no representation as to its accuracy or completeness and expressly disclaim any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this prospectus.

A copy of this prospectus, having attached thereto the documents specified in the paragraph headed "Documents Delivered to the Registrar of Companies and Available for Inspection" in Appendix VII to this prospectus, has been registered by the Registrar of Companies in Hong Kong as required by section 342C of the Companies Ordinance (Chapter 32 of the Laws of Hong Kong). The Securities and Futures Commission and the Registrar of Companies in Hong Kong take no responsibility for the contents of this prospectus or any other document referred to above.

The Offer Price is expected to be determined by agreement between us and the Sole Global Coordinator (on behalf of the Underwriters) on the Price Determination Date. The Price Determination Date is expected to be on or around 20 May 2010 and, in any event, not later than 26 May 2010. The Offer Price will not be more than HK$3.38 and is currently expected not to be less than HK$2.58 unless otherwise announced. If, for any reason, the Offer Price is not agreed between us and the Sole Global Coordinator (on behalf of the Underwriters), the Global Offering (including the Hong Kong Public Offering) will not proceed.

The Sole Global Coordinator, on behalf of the Underwriters may, with the consent of our Company reduce the number of Offer Shares and/or the indicative Offer Price range below that stated in this prospectus (which is HK$2.58 to HK$3.38 per Offer Share) at any time on or prior to the morning of the last day for lodging applications under the Hong Kong Public Offering. In such a case, notices of the reduction in the number of Offer Shares and/or the indicative offer price range will be published in the Hong Kong Economic Times (in Chinese) and the South China Morning Post (in English) not later than the morning of the day which is the last day for lodging applications under the Hong Kong Public Offering. Such notice will also be available at the website of the Stock Exchange at www.hkexnews.hk and the Company's website at www.youyuan.com.hk. If applications for the Hong Kong Offer Shares have been submitted prior to the last day for lodging applications under the Hong Kong Public Offering, then even if the indicative Offer Price range is so reduced, such applications cannot be subsequently withdrawn. The obligations of the Hong Kong Underwriters under the Hong Kong Underwriting Agreement, are subject to termination by the Sole Global Coordinator (for itself, and on behalf of the Hong Kong Underwriters) if certain grounds arise prior to 8:00 a.m., on the Listing Date. Please refer to "Underwriting — Underwriting Arrangements and Expenses — Hong Kong Public Offering — Grounds for termination" in this prospectus for more details.

Prior to making an investment decision, prospective investors should consider carefully all of the information set out in this prospectus, including the risk factors set out in "Risk Factors" in this prospectus.

The Offer Shares have not been and will not be registered under the US Securities Act or any state securities law in the United States and may not be offered, sold, pledged or transferred within the United States, except that Offer Shares may be offered, sold or delivered to (i) Qualified Institutional Buyers in reliance on an exemption from registration under the US Securities Act provided by, and in accordance with the restrictions of, Rule 144A, or another available exemption from registration under the US Securities Act or (ii) outside the United States in accordance with Regulation S under the US Securities Act.

14 May 2010

**IMPORTANT NOTICE TO INVESTORS**

*This prospectus is issued by the Company solely in connection with the Hong Kong Offer Shares and does not constitute an offer to sell or a solicitation of an offer to buy any security other than the Hong Kong Offer Shares offered by this prospectus pursuant to the Hong Kong Public Offering. This prospectus may not be used for the purpose of, and does not constitute, an offer or invitation in any other jurisdiction or in any other circumstances. No action has been taken to permit a public offering of the Hong Kong Offer Shares in any jurisdiction other than Hong Kong and no action has been taken to permit the distribution of this prospectus in any jurisdiction other than Hong Kong. The distribution of this prospectus for purposes of a public offering and the offering and sale of the Hong Kong Offer Shares in other jurisdictions are subject to restrictions and may not be made except as permitted under the applicable securities laws of such jurisdictions pursuant to registration with or authorisation by the relevant securities regulatory authorities or an exemption therefrom.*

*You should rely only on the information contained in this prospectus and the Application Forms to make your investment decision. The Hong Kong Public Offering is made solely on the basis of the information contained and the representations made in this prospectus.*

*The Company has not authorised anyone to provide you with information that is different from what is contained in this prospectus.*

*Any information or representation not contained nor made in this prospectus and the Application Forms must not be relied on by you as having been authorised by the Company, the Sole Global Coordinator, the Sole Bookrunner, the Sole Sponsor, the Sole Lead Manager, any of the Underwriters, any of their respective directors, officers, employees, agents or representatives of any of them or any other parties involved in the Global Offering.*

# CONTENTS

## EXPECTED TIMETABLE[1]

| | |
|---|---|
| Application lists open[2] | 11:45 a.m. on Wednesday, 19 May 2010 |
| Latest time to lodging **WHITE** and **YELLOW** Application Forms | 12:00 noon on Wednesday, 19 May 2010 |
| Latest time to giving **electronic application instructions** to HKSCC[3] | 12:00 noon on Wednesday, 19 May 2010 |
| Latest time to complete electronic applications under the **White Form eIPO** service through the designated website **www.eipo.com.hk**[4] | 11:30 noon on Wednesday, 19 May 2010 |
| Latest time to complete payment of **White Form eIPO** applications by effecting internet banking transfer(s) or PPS payment transfer(s) | 12:00 noon on Wednesday, 19 May 2010 |
| Application lists close | 12:00 noon on Wednesday, 19 May 2010 |
| Expected Price Determination Date[5] | Thursday, 20 May 2010 |
| Announcement of the Offer Price, the level of indication of interest in the International Offering, level of applications in the Hong Kong Public Offering and basis of allotment of the Hong Kong Offer Shares under the Hong Kong Public Offering to be published on our Company's website at **www.youyuan.com.hk** and the website of the Stock Exchange at **www.hkexnews.hk** on | Wednesday, 26 May 2010 |
| Results of applications and Hong Kong identity card/passport/Hong Kong business registration numbers of successful applicants under the Hong Kong Public Offering to be available through a variety of channels as described in the section headed "How to Apply for Hong Kong Offer Shares — Results of Allocations" including our website at **www.youyuan.com.hk** and the website of the Stock Exchange at **www.hkexnews.hk** from | Wednesday, 26 May 2010 |
| Results of allocations for the Hong Kong Public Offering will be available at **www.iporesults.com.hk**, with a "search by ID" function | Wednesday, 26 May 2010 |
| Despatch of share certificates on or before[6] | Wednesday, 26 May 2010 |
| Despatch of White Form e-Refund payment instructions/refund cheques on[7] | Wednesday, 26 May 2010 |
| Dealings in Shares on the Stock Exchange expected to commence on | Thursday, 27 May 2010 |

*Notes:*

1 All times refer to Hong Kong local time.

2 If there is a "black" rainstorm warning or a tropical cyclone warning signal number 8 or above in force in Hong Kong at any time between 9:00 a.m. and 12:00 noon on Wednesday, 19 May 2010, the application lists will not open or close on that day. Please refer to "How to Apply for Hong Kong Offer Shares — When to Apply for the Hong Kong Offer Shares — Effect of bad weather conditions on the opening of the application lists" in this prospectus for more details. If the application lists do not open and close on Wednesday, 19 May 2010, the dates mentioned in this section headed "Expected Timetable" may be affected. We will make a press announcement in such event.

3 Applicants who apply for the Hong Kong Offer Shares by giving **electronic application instructions** to HKSCC should refer to "How to Apply for Hong Kong Offer Shares — How to Apply by Giving Electronic Application Instructions to HKSCC" in this prospectus.

4 You will not be permitted to submit your application through the designated website at **www.eipo.com.hk** after 11:30 a.m. on the last day for submitting applications. If you have already submitted your application and obtained an application reference number from the designated website prior to 11:30 a.m., you will be permitted to continue the application process (by completing payment of application monies) until 12:00 noon on the last day for submitting applications, when the application lists close.

5 The Price Determination Date, being the date on which the Offer Price is to be determined, is expected to be on or about Thursday, 20 May 2010 and, in any event, not later than Wednesday, 26 May 2010. If, for any reason, the Offer Price is not agreed between the Sole Global Coordinator (on behalf of the Underwriters), and us by Wednesday, 26 May 2010, the Global Offering (including the Hong Kong Public Offering) will not proceed and will lapse.

6 Share certificates for the Hong Kong Offer Shares are expected to be issued on Wednesday, 26 May 2010 but will only become valid certificates of title provided that (i) the Global Offering has become unconditional in all respects and (ii) the Underwriting Agreements have not been terminated in accordance with their terms. If the Global Offering does not become unconditional or the Underwriting Agreements are terminated in accordance with their terms, we will make an announcement as soon as possible.

7 e-Refund payment instructions/refund cheques will be issued in respect of wholly or partially unsuccessful applications pursuant to the Hong Kong Public Offering and also in respect of wholly or partially successful applications in the event that the final Offer Price is less than the price payable per Offer Share on application. Part of the applicant's Hong Kong identity card number or passport number, or, if the application is made by joint applicants, part of the Hong Kong identity card number or passport number of the first-named applicant, provided by the applicant(s) may be printed on the refund cheque, if any. Such data would also be transferred to a third party for refund purpose. Banks may require verification of an applicant's Hong Kong identity card number or passport number before cashing the refund cheque. Inaccurate completion of an applicant's Hong Kong identity card number or passport number may lead to delay in encashment of or may invalidate the refund cheque.

Applicants who have applied on **WHITE** Application Forms for 1,000,000 or more Hong Kong Offer Shares under the Hong Kong Public Offering and have indicated in their Application Forms that they wish to collect any refund cheques (if applicable) and share certificates (if applicable) in person, may do so from our Hong Kong Share Registrar, Computershare Hong Kong Investor Services Limited between 9:00 a.m. to 1:00 p.m. on Wednesday, 26 May 2010. Applicants being individuals who opt for personal collection must not authorise any other person to make collection on their behalf. Applicants being corporations who opt for personal collection must attend by their authorised representatives bearing letters of authorisation from their corporation stamped with the corporation's chop. Both individuals and representatives of corporations must produce, at the time of collection, identification and (where applicable) documents acceptable to Computershare Hong Kong Investor Services Limited at the time of collection. Applicants who have applied on **YELLOW** Application Forms for 1,000,000 or more Hong Kong Offer Shares under the Hong Kong Public Offering may collect their refund cheques (if applicable), if any, in person but may not elect to collect their share certificates which will be deposited into CCASS for the credit of their designated CCASS participants' stock accounts or CCASS investor participant stock accounts, as appropriate. The procedures for collection of refund cheques for **YELLOW** Application Form applicants are the same as those for **WHITE** Application Form applicants. Applicants who have applied through the **White Form eIPO** service by paying the application monies through a single bank account may have e-Refund payment instructions (if any) despatched to their application payment bank account, on Wednesday, 26 May 2010. Applicants who have applied through the **White Form eIPO** service by paying the application monies through multiple bank accounts may have refund cheque(s) sent to the address specified in their application instructions to the designated **White Form eIPO** Service Provider, on Wednesday, 26 May 2010, by ordinary post and at their own risk. Applicants who apply for Hong Kong Offer Shares by giving **electronic application instructions** to HKSCC should refer to "How to Apply for Hong Kong Offer Shares — How to Apply by Giving Electronic Application Instructions to HKSCC" in this prospectus for details. Uncollected share certificates (if applicable) and refund cheques (if applicable) will be despatched by ordinary post at the applicants' own risk to the addresses specified in the relevant Application Forms. Further information is set out in "How to Apply for Hong Kong Offer Shares — Despatch/Collection of Share Certificates/e-Refund Payment Instructions/Refund Cheques" in this prospectus.

Particulars of the structure of the Global Offering, including the conditions thereto, are set out in "Structure of the Global Offering" in this prospectus.

*This summary aims to give you an overview of the information contained in this prospectus. As this is a summary, it does not contain all the information that may be important to you. You should read the whole document before you decide to invest in the Hong Kong Offer Shares. There are risks associated with any investment. Some of the particular risks in investing in the Hong Kong Offer Shares are set out in "Risk Factors" in this prospectus. You should read this section carefully before you decide to invest in the Hong Kong Offer Shares.*

## OVERVIEW

We are a leading wrapping tissue paper manufacturer in the PRC. We were the largest among the major wrapping tissue paper manufacturers by production output in 2008 and achieved approximately 14.0% and 5.3% market share by production output for MF tissue paper and wrapping tissue paper, respectively, within the PRC, according to the China Paper Association. MF tissue paper makes up a small part of the paper and paperboard products industry, falling within the tissue paper sub-category of the packaging paper segment. According to a report issued by the China Paper Association regarding domestic PRC production output of the paper and paperboard products industry in 2008, MF tissue paper accounted for approximately 37.5% of the entire wrapping tissue paper segment, which in turn, accounted for approximately 21.4% of the total packaging paper segment, which in turn, accounted for approximately 7.0% of the total paper and paperboard products industry. Our total production output in 2008 accounted for approximately 0.1% of the total production output of paper and paperboard products in the PRC.

We were also recognised by the China Paper Association as one of the Top 30 Pulp and Paper Making Enterprises in the PRC in 2008* (2008年度全國制漿造紙30強企業). Our principal products include double-sided MF tissue paper and single-sided MF tissue paper with basis weights of less than $40g/m^2$ which are commonly used to wrap clothing, footwear, fruit and other consumer products. We also manufacture copy paper. We market our wrapping tissue paper under the brand and our copy paper under the "Scholar* (大學士學)", "Young Scholar* (小秀才秀)" and "Prodigy* (小神童神)" brands.

We are actively exploring opportunities to diversify our product lines to offer a broader range of products. We commenced production of paper towels and ivory boards in January and April 2010, respectively. Our research and development department is currently developing food wrapping paper products, which are proposed to be launched in September 2010.

Our head office is located at Xibin Industrial Zone, Jinjiang City, Fujian Province, the PRC. We have comprehensive and advanced production facilities with a large production capacity in Fujian Province, the PRC. We operate three factories: Youlanfa Factory and Huaxiang Factory, both of which are located in Jinjiang, and Xiyuan Factory, which is located in Longhai. All of our production sites are in close proximity to Xiamen Port and well-developed railway and highway transportation networks. As of 31 December 2009, we operated 16 paper production lines with an aggregate annual production capacity of approximately 124,440 tonnes.[1] We also have an in-house de-inking facility in our Huaxiang Factory with an annual design production capacity of 34,000 tonnes. We have our own water supply system in our Xiyuan Factory, and all of our factories have coal-fire boiler plants and wastewater treatment plants. According to the China Paper Association, most of the wrapping tissue paper manufacturers in the PRC purchase pulp from the market with only a few producing their own pulp. In recent years, some PRC manufacturers have begun to use de-inked pulp made from recovered paper in their production of wrapping tissue paper to reduce production costs and strengthen competitiveness. We are one such paper manufacturer in the PRC capable of making de-inked pulp suitable for the production of wrapping tissue paper. To capitalise on the growing demand for wrapping tissue paper, household paper and office paper in the PRC, we have purchased and installed one paper towel production line, one ivory board production line and two single-sided MF tissue paper production lines in 2010, all of which commenced production before the Latest Practicable Date, and we plan to add another nine paper production lines by the end of 2012. We expect these 13 new paper production lines will increase our maximum annual production capacity by 209,250 tonnes. For additional information on our new paper production lines, please refer to "Business — Production — Production facilities" in this prospectus.

---

*Note 1:* The annual production capacity is estimated by our Directors based on the basis weight per sheet of our products and the maximum operation speed achievable when producing such products. The annual production capacity is calculated on the presumption that each paper machine operates 340 days per year.

Our production capacity is different from the design production capacity estimated by the manufacturers of our paper machines because the latter is determined with reference to the average basis weight of products each paper machine can produce. Our products carry a lighter basis weight per sheet compared to the average basis weight contemplated by the manufacturers of our paper machines when they estimated the design production capacity. As a result, when running at the same speed, our paper machines produce fewer tonnes of paper. For additional information on our paper machines, please refer to "Business — Production — Production facilities" and "Business — Property, Plant and Equipment — Production equipment" in this prospectus.

We have a highly skilled and experienced production team. As of the Latest Practicable Date, our production team was comprised of more than 1,000 personnel led by approximately 20 experienced managerial and executive level personnel.

We have established an extensive sales and marketing network across the PRC, adopting a strategic regional distribution system pursuant to which we sell to regional distributors who either directly on-sell our products to, or further process our products in accordance with the specifications of, end-users. These end-users include clothing, footwear, and hardware manufacturers or retailers, fruit growers and wine retailers. We have designated six sales regions in the PRC, based on the geographical concentration of our customers, to facilitate the management of our sales and marketing activities. As of 31 December 2009, we had 98 customers who were regional distributors, located primarily in Fujian Province, the Yangtze River Delta region and the Pearl River Delta region. Our sales activities are therefore concentrated in the East China and South China regions.

The following table shows the breakdown of our revenue by products in the six sales regions for the periods indicated.

| Region[1] | 2007 Revenue | | | | 2008 Revenue | | | | 2009 Revenue | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper | % of total revenue | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper | % of total revenue | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper | % of total revenue |
| | (RMB in MN, except percentages) | | | | | | | | | | | |
| North China | 4.1 | — | 1.3 | 2 | 15.7 | 11.8 | 0.6 | 5 | 17.9 | 8.5 | 1.3 | 4 |
| Northeast China | — | — | — | — | 8.5 | 8.4 | — | 3 | 8.9 | 8.4 | — | 2 |
| East China | 119.0 | 25.1 | 69.7 | 80 | 157.8 | 86.6 | 86.8 | 58 | 239.4 | 81.0 | 77.9 | 55 |
| Central China | 1.2 | 0.6 | — | 1 | 0.2 | — | — | 1 | — | — | — | — |
| Southwest China | — | — | — | — | 1.1 | 1.3 | — | 1 | 0.2 | 1.0 | — | 1 |
| South China | 23.6 | 20.3 | 2.7 | 17 | 116.1 | 63.4 | 3.7 | 32 | 204.0 | 69.7 | 6.6 | 38 |
| **Total** | 147.9 | 46.0 | 73.7 | 100 | 299.4 | 171.5 | 91.1 | 100 | 470.4 | 168.6 | 85.8 | 100 |

(Year ended 31 December)

*Note 1:* North China mainly covers Beijing, Tianjin and Baoding. Northeast China mainly covers Dalian, Liaoyang and Shenyang. East China mainly covers Shanghai, Nanjing, Suzhou, Wenzhou, Xiamen and Quanzhou. Central China mainly covers Wuhan and Changsha. Southwest China mainly covers Guiyang and Kunming. South China mainly covers Guangzhou, Foshan, Shantou, Shenzhen and Huizhou.

We are committed to enhancing production innovation and production efficiency through research and development. We have established technology exchange and cooperation programmes with four research and education facilities. In recognition of our research and development efforts and our market position, we have been invited by the China Standardisation Technical Committee for Paper Making Industry* (全國造紙工業標準化技術委員會) to participate in the drafting of industry standard specifications for wrapping tissue paper and semi-transparent paper, a type of double-sided MF tissue paper. In 2008, the Fujian Provincial Department of Science and Technology* (福建省科學技術廳) established the Paper-making Technology Development Base of Fujian Province* (福建省紙業技術開發基地) at our research and development centre and in 2009, Quanzhou Municipal Department of Science and Technology* (泉州市科學技術局) recognised our ultra-thin single-sided MF tissue paper product as a technologically advanced product. Youlanfa has applied to the Fujian Provincial Department of Science and Technology* (福建省科學技術廳) for a "High and New Technology Enterprises Certificate* (高新技術企業認定證書)", which upon receipt would allow Youlanfa to enjoy a reduced PRC enterprise income tax rate. We expect to obtain such certificate by August 2010.

We place strong emphasis on environmentally responsible practices in all aspects of our operations and have endeavored to increase our use of de-inked pulp, reclaimed pulp and recycled white paper and to reduce our reliance on wood pulp in our production process. We obtained ISO14001 certification for our environmental management standards in 2002 and have met or exceeded the relevant standards under the PRC environmental laws and regulations.

We have achieved significant growth during the Track Record Period. For the three years ended 31 December 2009, our revenue was RMB267.6 million, RMB562.0 million and RMB724.8 million, respectively, representing a CAGR of 64.6%. Our profits for the same periods were RMB42.3 million, RMB132.6 million and RMB170.7 million, respectively, representing a CAGR of 100.9%.

## OUR COMPETITIVE STRENGTHS

We attribute our success to the following key factors:

- we are a leading wrapping tissue paper manufacturer in the PRC and are well-positioned to capture future opportunities;
- close proximity to our customers, transportation hubs and water resources;
- secured sources of high quality and price competitive raw materials;
- distinguished research and development capabilities;
- environmentally responsible practices; and
- experienced management team and a highly skilled workforce.

## OUR BUSINESS STRATEGIES

We aim to maintain our position as a leading manufacturer of wrapping tissue paper products in the PRC. We will continue to seek opportunities to realise sustainable growth of our business and increase shareholder value. To achieve this, we plan to focus on the following strategies:

- continue to expand our production capacity to maintain our market leadership position in the PRC;
- expand and diversify product offerings;
- enhance supporting facilities to support our future production expansion; and
- enhance the brand awareness of our wrapping tissue paper products marketed under the "Youlanfa" trademark.

## SUMMARY OF HISTORICAL FINANCIAL INFORMATION

Our financial information included in this prospectus has been prepared in accordance with the IFRS. The following tables set forth summary combined financial data about the Company. We have derived the combined financial data for the years ended 31 December 2007, 2008 and 2009 from our combined financial statements set forth in the Accountants' Report in Appendix I to this prospectus. The summary combined financial data should be read together with, and is qualified in its entirety by reference to, these combined financial statements, including the related notes.

### Selected Combined Statements of Comprehensive Income Data

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Revenue | 267.6 | 562.0 | 724.8 |
| Cost of sales | (187.1) | (373.9) | (484.1) |
| Gross profit | 80.5 | 188.1 | 240.7 |
| Selling and distribution expenses | (2.1) | (3.0) | (4.1) |
| Administrative expenses | (12.6) | (25.4) | (37.0) |
| Other income and other gains and losses | 5.3 | 5.9 | 2.4 |
| Finance costs | (13.6) | (20.0) | (18.2) |
| Profit before tax | 57.5 | 145.6 | 183.8 |
| Taxation | (15.2) | (13.0) | (13.1) |
| Profit and total comprehensive income for the year | 42.3 | 132.6 | 170.7 |
| Profit and total comprehensive income for the year attributable to: | | | |
| Owners of the Company | 40.3 | 126.4 | 166.0 |
| Minority interests | 2.0 | 6.2 | 4.7 |
| | 42.3 | 132.6 | 170.7 |
| Earnings per share - Basic (RMB)[1] | 0.05 | 0.17 | 0.22 |

*Note 1:* The calculation of the basic earnings per share for the Track Record Period is based on the profit attributable to the Shareholders of the Company and 750,000,000 Shares of the Company, taking into account the share swap pursuant to the Reorganisation and adjusted for the effect of the Capitalisation Issue.

**Selected Combined Statements of Financial Position Data**

| | As of 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Non-current Assets | 626.8 | 700.5 | 945.0 |
| Currents Assets | 105.0 | 218.5 | 360.3 |
| Current Liabilities | 570.3 | 624.8 | 410.3 |
| Net Current Liabilities | (465.3) | (406.3) | (50.0) |
| Total Assets Less Current Liabilities | 161.5 | 294.2 | 895.0 |
| Non-current Liabilities | — | — | 340.2 |
| Share Capital/Paid-In Capital | 65.4 | 0.0 | 0.0 |
| Reserves | 83.0 | 274.8 | 554.8 |
| Equity Attributable to Owners of the Company | 148.4 | 274.8 | 554.8 |
| Minority Interests | 13.1 | 19.4 | — |

**Selected Combined Statements of Cash Flows Data**

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Operating cash flows before movements in working capital | 82.9 | 184.9 | 228.8 |
| Cash generated from operations before income taxes paid | 47.9 | 219.9 | 76.3 |
| Net cash from operating activities | 34.9 | 204.7 | 63.6 |
| Net cash used in investing activities | (215.0) | (122.5) | (244.1) |
| Net cash from (used in) financing activities | 178.4 | (81.7) | 261.5 |
| Net (decrease) increase in cash and cash equivalents | (1.7) | 0.5 | 81.0 |

**PROFIT FORECAST FOR THE SIX MONTHS ENDING 30 JUNE 2010**

On the bases and assumptions set out in “Profit Forecast” in Appendix III to this prospectus and, in the absence of unforeseen circumstances, certain profit forecast data of the Group for the six months ending 30 June 2010 is set out below:

Forecast consolidated profit attributable to the Shareholders of our Company[1] . . . . . . . . . . . . . . . . . . . . . . . . . . Not less than RMB82 million

Unaudited pro forma forecast earnings per Share[2] . . . . . . . . . . . . . . . . . . . . . Not less than RMB0.08 (HK$0.09)

*Notes:*

1 Our forecast consolidated profit attributable to the Shareholders of the Company for the six months ending 30 June 2010 is extracted from "Management's Discussion and Analysis of Financial Condition and Results of Operations — Profit Forecast for the Six Months Ending 30 June 2010" in this prospectus. The bases and assumptions on which the above profit forecast has been prepared are set out in "Profit Forecast" in Appendix III to this prospectus. Our Directors have prepared the forecast of our Group's consolidated profit attributable to Shareholders of our Company for the six months ending 30 June 2010 based on the unaudited management accounts of our Group for the two months ended 28 February 2010 and a forecast of the combined results of our Group for the remaining four months ending 30 June 2010. The forecast for the six months ending 30 June 2010 has been prepared on basis consistent in all material respects with the accounting policies adopted by our Group and its associates as set out in the Accountants' Report in Appendix I to this prospectus.

2 The calculation of the forecast earnings per Share is based on the forecast combined profit attributable to Shareholders for the six months ending 30 June 2010, assuming that we have been listed since 1 January 2010 and a total of 1,000,000,000 Shares were in issue during the period. This calculation assumes that the Over-allotment Option will not be exercised and options which may be granted pursuant to the Share Option Scheme will not be exercised.

## GLOBAL OFFERING STATISTICS

| | **Based on an Offer Price of HK$2.58** | **Based on an Offer Price of HK$3.38** |
|---|---|---|
| Market capitalisation of our Shares[1] | HK$2,580 million | HK$3,380 million |
| Unaudited pro forma adjusted net tangible assets per Share[2] | HK$1.23 | HK$1.42 |

*Notes:*

1 The calculation of market capitalisation is based on the assumption that 1,000,000,000 Shares will be in issue and outstanding immediately following the completion of the Global Offering and the Capitalisation Issue but excludes any Shares which may be issued pursuant to the exercise of the Over-allotment Option or pursuant to the exercise of the options which may be granted under the Share Option Scheme.

2 The unaudited pro forma adjusted net tangible assets per Share has been arrived at after the adjustments referred to in "Unaudited Pro Forma Financial Information — Unaudited Pro Forma Adjusted Net Tangible Assets" in Appendix II to this prospectus and on the basis that 1,000,000,000 Shares were in issue assuming that the Global Offering and the Capitalisation Issue had been completed, including 250,000,000 Shares proposed to be issued upon Listing at the respective Offer Price of HK$2.58 and HK$3.38 per Offer Share. This calculation takes no account of any Shares which may be issued pursuant to the exercise of the Over-allotment Option or pursuant to the exercise of the options which may be granted under the Share Option Scheme.

## DIVIDENDS

We may distribute dividends by way of cash or by other means that we consider appropriate. Dividends may be declared and paid out of profits of the Company, realised or unrealised, or from any reserve set aside from profits which the Board determines is no longer needed. Dividends may also be declared and paid out of the share premium account or any other fund or account which can be authorised under the Companies Law for this purpose. No unpaid dividend shall bear interest as against the Company. A decision to declare and pay any dividends would require the approval of our Board and will be at its discretion. In addition, any final dividend for a financial year will be subject to our Shareholders' approval. The payment and the amount of any dividends declared will be subject to our Articles of Association and the Companies Law. No dividends are payable if doing so would render our Company unable to pay our liabilities as they become due or if the realisable assets would be less than the aggregate of our liabilities and our issued share capital.

For details of our dividend policy, please refer to "Management's Discussion and Analysis of Financial Condition and Results of Operations — Dividend Policy" in this prospectus.

## FUTURE PLANS AND USE OF PROCEEDS

### Future Plans

We aim to maintain our position as a leading manufacturer of MF tissue paper products in the PRC. To achieve this, amongst other strategies, the Group plans to significantly expand its production capacity in the next few years.

As of the Latest Practicable Date, we have added four paper production lines in 2010 and plan to add another nine paper production lines by the end of 2012. These 13 new production lines include nine MF tissue paper production lines (of which two will be used for the manufacture of food wrapping paper), one copy paper production line, two paper towel production lines and one ivory board production line. We expect these 13 new paper production lines will increase our maximum annual production capacity by 209,250 tonnes, including 145,000 tonnes of MF tissue paper, 30,000 tonnes of copy paper, 20,000 tonnes of ivory boards and 14,250 tonnes of paper towels. Our new MF tissue paper production capacity is expected to be utilised to maintain our position as a leading manufacturer of wrapping tissue paper products in the PRC and to further expand our market share by strengthening our position in Eastern and Southern China as well as expand our footprint within Western China, where demand for packing materials has increased owing to the local economic development. Our new copy paper production capacity will be utilised to meet the market demand given that our existing copy paper production line has been fully utilised as of the Latest Practicable Date. Our new ivory board capacity is to meet the demand from existing customers who produce price tags. We expect demand for our paper towels to come from both our existing and new customers.

Our Directors' belief that our additional production capacity will be taken up by increased market demand is premised on industry growth forecasts issued by the China Paper Association. In 2008, the PRC produced approximately 450,000 tonnes of MF tissue paper and the growth of wrapping tissue paper consumption in the PRC is expected to continue at a rate of approximately 8% per annum, according to a report prepared by the China Paper Association. Assuming MF tissue paper production output in the PRC grows at the same rate, it would reach approximately 486,000 tonnes in 2009. Based on our production output of approximately 92,274 tonnes of MF tissue paper in 2009, we had achieved approximately 19.0% market share by production output, which is approximately 5% higher than that in 2008. Considering that a single-sided MF tissue paper production line is expected to commence operation in August 2012 and given its utilisation rate will be low during the trial period, our Directors expect our production output of MF tissue paper for the year ending 31 December 2012 to be approximately 207,000 tonnes. Assuming MF tissue paper production output in the PRC keeps growing at 8% per annum, it will reach approximately 612,000 tonnes in 2012. With this industry capacity as a backdrop and assuming our 2009 growth rate remains steady, we expect to achieve an approximately 33.8% market share for MF tissue paper by production output within the PRC in 2012.

We also intend to increase advertising and promotion activities of our products under the "Youlanfa" trademark. In particular, we plan to expand our sales team to enhance our marketing in Western and Central China, increase the number of our outdoor billboards and begin advertising campaigns on television.

For each of the three years ended 31 December 2010, 2011 and 2012, our planned investment on paper machines amounts to RMB201.5 million, RMB375.7 million and RMB341.2 million, respectively. The following table sets forth details of our 13 new paper production lines, including planned annual production capacity as estimated by our Directors.

| No. | Location | Products | Planned annual production capacity | Planned/Actual* commencement of operation |
|---|---|---|---|---|
| | | | (tonnes) | |
| 1 | Youlanfa Factory | paper towels | 6,000 | January 2010* |
| 2 | Youlanfa Factory | ivory boards | 20,000 | April 2010* |
| 3 | Youlanfa Factory | coloured single-sided MF tissue paper | 4,000 | October 2010 |
| 4 | Youlanfa Factory | coloured single-sided MF tissue paper | 4,000 | November 2010 |
| 5 | Huaxiang Factory | paper towels | 8,250 | June 2010 |
| 6 | Huaxiang Factory | double-sided MF tissue paper | 25,000 | October 2011 |
| 7 | Huaxiang Factory | double-sided MF tissue paper | 30,000 | December 2011 |
| 8 | Huaxiang Factory | single-sided MF tissue paper | 50,000 | August 2012 |
| 9 | Xiyuan Factory | single-sided MF tissue paper | 9,000 | January 2010* |
| 10 | Xiyuan Factory | single-sided MF tissue paper | 9,000 | January 2010* |
| 11 | Xiyuan Factory | food wrapping paper | 7,000 | September 2010 |
| 12 | Xiyuan Factory | food wrapping paper | 7,000 | September 2010 |
| 13 | Xiyuan Factory | copy paper | 30,000 | September 2010 |
| | | Total | 209,250 | |

Of the above 13 new paper production lines, our Youlanfa Factory has purchased and installed one production line for the production of paper towels which has a design capacity of 25 tonnes per day and a maximum design speed of 220 metres per minute. It has the capacity to produce paper towels with a maximum paper width of 2.8 metres. Our Youlanfa Factory also purchased and installed one production line for the production of ivory boards which has a design capacity of 70 tonnes per day and a maximum design speed of 380 metres per minute. It has the capacity to produce ivory boards with a maximum paper width of 2.75 metres. Our Xiyuan Factory has purchased and installed two production lines for the production of single-sided MF tissue paper, each of which has a design capacity of 30 tonnes per day and a maximum design speed of 450 metres per minute. These single-sided MF tissue paper machines can produce tissue paper with a maximum paper width of 2.9 metres. Each of these paper towels, ivory boards and single-sided MF tissue paper production lines commenced production before the Latest Practicable Date.

We also intend to upgrade our supporting facilities. We plan to construct a cogeneration plant at our Xiyuan Factory which will upon completion significantly reduce our Xiyuan Factory's reliance on local utilities for the supply of electricity. We also plan to add two de-inking facilities with an annual capacity of 160,000 tonnes of de-inked pulp by the end of 2012. We intend to utilise this added capacity to meet our increasing demand for de-inked pulp which, through further research and development, is expected to gradually replace reclaimed pulp and reduce the percentage of wood pulp we use in our production, thereby further lowering our production costs.

For each of the three years ended 31 December 2010, 2011 and 2012, our planned investment on other property, plant and equipment amounts to RMB352.2 million, RMB173.3 million and RMB124.5 million, respectively. The following table sets forth details of the major new plants and supporting facilities.

| No. | Location | New plants and supporting facilities | Expected capacity | Site area | Expected completion time |
|---|---|---|---|---|---|
| | | | (tonnes/year except otherwise specified) | (sq.m.) | |
| 1 | Youlanfa Factory | blue top linerboard production line | 8,400 | — | July 2010 |
| 2 | Huaxiang Factory | de-inking facility | 60,000[1] | — | July 2010 |
| 3 | Huaxiang Factory | water treatment and recycling system | — | — | July 2010 |
| 4 | Huaxiang Factory | warehouses | — | 33,894 | November 2010 |
| 5 | Huaxiang Factory | dormitories | — | — | July 2010 |
| 6 | Xiyuan Factory | production plants | — | — | September 2010 |
| 7 | Xiyuan Factory | cogeneration plant | 35t/h | — | September 2010 |
| 8 | Xiyuan Factory | water treatment and recycling system | — | — | September 2010 |
| 9 | Xiyuan Factory | warehouses | — | 23,000 | October 2010 |

| No. | Location | New plants and supporting facilities | Expected capacity | Site area | Expected completion time |
|---|---|---|---|---|---|
| | | | (tonnes/year except otherwise specified) | (sq.m.) | |
| 10 | Huaxiang Factory | production plants | — | — | October 2011 |
| 11 | Huaxiang Factory | coal yard | — | 5,000 | October 2011 |
| 12 | Huaxiang Factory | boiler plant | 20t/h | — | October 2011 |
| 13 | Huaxiang Factory | warehouses | — | 30,000 | December 2011 |
| 14 | Xiyuan Factory | de-inking facility | 60,000 | — | February 2011 |
| 15 | Xiyuan Factory | dormitory | — | — | July 2011 |
| 16 | Huaxiang Factory | production plant | — | — | August 2012 |
| 17 | Huaxiang Factory | boiler plant | 20t/h | — | August 2012 |
| 18 | Huaxiang Factory | warehouses | — | 4,000 | June 2012 |
| 19 | Xiyuan Factory | warehouses | — | 5,000 | May 2012 |

*Note 1:* To be upgraded to 100,000 tonnes in July 2011.

Our planned investment on paper machines, plants and supporting facilities is expected to be financed primarily by the proceeds from the Global Offering, operating cashflow and bank loans.

Apart from paper production lines that are not comparable with our existing production facilities as they will produce new products such as paper towels and ivory boards, most of the planned new production lines and supporting facilities are expected to have higher capacities than our existing production facilities. We plan to procure the double-sided MF tissue paper and the single-sided MF tissue paper production lines for our Huaxiang Factory from overseas manufacturers, and the specifications for such machines are expected to include higher speeds and wider paper widths as compared to paper machines produced domestically.

**Use of Proceeds**

We estimate that the net proceeds of the Global Offering (after deducting underwriting commissions and estimated expenses payable by us in connection with the Global Offering and assuming the Over-allotment Option is not exercised), assuming an Offer Price of HK$2.98 per share, being the mid-point of the indicative Offer Price range, will be approximately HK$677.9 million. We intend to apply such net proceeds in the following manner:

- approximately HK$305.1 million or approximately 45% of the aggregate net proceeds is expected to be used for the purchase of machinery and equipment relating to new production facilities, of which approximately HK$164.7 million or 54% is expected to be spent on the new production lines at Huaxiang Factory, approximately HK$131.2 million or 43% is expected to be spent on the new production lines at Xiyuan Factory, and approximately HK$9.2 million or 3% is expected to be spent on the new production lines at Youlanfa Factory;

- approximately HK$271.2 million or approximately 40% of the aggregate net proceeds is expected to be used for the construction of new plant and supporting facilities to support production of new products and increases to production capacity, of which approximately HK$130.2 million or 48% is expected to be spent on the new plant and supporting facilities of Huaxiang Factory, approximately HK$135.6 million or 50% is expected to be spent on the new plant and supporting facilities of Xiyuan Factory, and approximately HK$5.4 million or 2% is expected to be spent on the new plant and supporting facilities of Youlanfa Factory;

- approximately HK$67.7 million or approximately 10% of the aggregate net proceeds is expected to be used for working capital and other general corporate purposes; and

- approximately HK$33.9 million or approximately 5% of the aggregate net proceeds is expected to be used for marketing expenses for growing our existing business in the PRC.

If the Offer Price is set at the high-end of the indicative Offer Price range, being HK$3.38 per Share, the net proceeds of the Global Offering (assuming the Over-allotment Option is not exercised), will increase by approximately HK$95.7 million. We intend to apply the additional net proceeds for the above purposes on a pro-rata basis.

If the Offer Price is set at the low-end of the indicative Offer Price range, being HK$2.58 per Share, the net proceeds of the Global Offering (assuming the Over-allotment Option is not exercised), will decrease by approximately HK$95.7 million. In such case, we intend to reduce the allocation of such net proceeds for the above purposes on a pro-rata basis.

If the Over-allotment Option is exercised in full, the net proceeds from the Global Offering will be approximately HK$784.9 million, assuming the Offer Price is set at the mid-point of the indicative Offer Price range. If the Offer Price is set at the high-end of the indicative Offer Price range, the net proceeds from the Global Offering (including the proceeds from the exercise of the Over-allotment Option) will be approximately HK$895.0 million. If the Offer Price is set at the low-end of the indicative Offer Price range, the net proceeds from the Global Offering (including the proceeds from the exercise of the Over-allotment Option) will be approximately HK$674.8 million. We intend to apply any additional net proceeds to the above purposes on a pro-rata basis.

To the extent that the net proceeds are not immediately required for or applied to the above purposes, we may hold such funds in short-term deposits with licensed banks and authorised financial institutions in Hong Kong for so long as it is in our best interests.

As advised by our PRC legal advisers, subject to the relevant PRC governmental approvals, registrations and/or filings, the net proceeds from the Global Offering can be applied in the PRC according to the above intended uses of the net proceeds under the relevant existing laws and regulations in the PRC by: (i) increasing the registered capital of the Company's PRC subsidiary; (ii) establishing a new PRC subsidiary; (iii) acquiring equity interests in the other companies in the PRC; and/or (iv) providing shareholder loans to the Company's subsidiary in the PRC in an amount not exceeding the difference between the investment amount and the registered capital of such subsidiary. As advised by our PRC legal advisers, there are no material legal obstacles to obtaining the relevant PRC governmental approvals to apply the net proceeds from the Global Offering in the PRC, if all requirements of the relevant PRC government authorities are satisfied.

We will make an appropriate announcement and comply with the requirements of the Listing Rules if there is any change to the above proposed use of proceeds.

## RISK FACTORS

There are certain risks relating to an investment in our Shares. These can be categorised into (i) risks relating to our business and our Group, (ii) risks relating to the industry, (iii) risks relating to the PRC, and (iv) risks relating to the Shares and Global Offering. These risk factors are further described in "Risk Factors" and are summarised below.

### Risks relating to our Business and our Group

- We may be unable to implement our expansion plans in full, within budget or on schedule or sustain the considerable business growth that we have experienced during the Track Record Period.

- Any oversupply in the PRC wrapping tissue paper market could negatively affect our business.

- The prices for and availability of raw materials, and the prices of our products, will significantly impact our business.

- We rely on constant and reliable supplies of water to support our production activities.

- We maintain a high level of indebtedness and we may be adversely affected by increases in interest rates.

- We are exposed to risks associated with our net current liabilities position.

- We have not obtained property title for some of our properties, which could adversely affect our rights to use such properties.

- We generally do not enter into long-term contracts with our customers and are thus subject to uncertainty and potential volatility with respect to our revenue from period to period.

- We rely on the continuing service of our executive Directors and senior management, and we may be unable to successfully recruit, train and retain management and highly skilled personnel.

- Failure to comply with the applicable quality, health and safety standards or labour laws of the PRC could lead to fines, lawsuits, or other penalties.

- We may be subject to losses that are not covered in whole or in part by our insurance policies.

- We may not be able to adequately protect our intellectual property rights and industrial know-how, and we may become involved in costly or unsuccessful intellectual property disputes.

- Any mechanical failure or disruption within our production facilities could negatively affect our business.

- We rely on the orderly operation of transportation infrastructure.

- We are exposed to payment delays and/or defaults by our customers.

**Risks relating to the Industry**

- We may face increased competition in relation to our products.

- Compliance with environmental regulations may significantly increase our operating costs.

**Risks relating to the PRC**

- All our revenue is derived from sales in the PRC. Changes in political or economic policies or a slowdown in the PRC economy may have an adverse impact on the demand for our paper products.

- Our business and operations may be adversely affected by events that are beyond our control.

- A change in the PRC tax policy could cause an increase in our tax liabilities.

- Any change in PRC industrial policy could adversely impact our profitability and ability to implement our expansion plans.

- Gains on the sales of the Offer Shares and distributions on the Offer Shares may be subject to PRC withholding taxes.

- Our PRC subsidiaries are subject to restrictions on paying dividends to us and the tax exemptions on dividends received by the Company and the Shareholders may be affected by the newly enacted Income Tax Law.

- Changes in foreign exchange regulations may adversely affect our ability to pay dividends.

- Fluctuation in the value of the Renminbi may adversely affect our business.

- PRC regulations concerning direct investment and loans by offshore holding companies to PRC entities may delay or limit us from funding our PRC subsidiaries.

- Changes and uncertainties in the PRC legal system may have an adverse impact on our operations.

- It may be difficult to effect service of process upon the Company or on our Directors who live in the PRC or to enforce judgments obtained from non-PRC courts against us.

- The enforcement of the Labour Contract Law and other labour-related regulations in the PRC may adversely affect our business and our results of operations.

- Failure to comply with PRC regulations in respect of the registration of share options belonging to our employees who are PRC citizens may subject such employees or us to fines and legal or administrative sanctions.

**Risks relating to the Shares and Global Offering**

- We will continue to be controlled by Mr Ke, whose interests may differ from those of our other Shareholders.

- Due to the time lag between pricing and trading of the Shares, there is a risk that the price of our Shares may fall before trading begins.

- We may not pay any dividends on our Shares.

- There has been no previous public market for our Shares, and an active trading market may not develop.

- Investors will experience immediate dilution and may experience further dilution in the value of their Shares.

- The trading volume and share price of our Shares may fluctuate.

- Future sales, or perceived sales, of substantial amounts of our Shares in the public market could materially and adversely affect the prevailing market price of our Shares.

- Investors may face difficulties in protecting their interests because we are incorporated under Cayman Islands law, and Cayman Islands law may provide different remedies to minority shareholders when compared with the laws of Hong Kong and other jurisdictions.

- Investors should not place undue reliance on certain statistics, facts and other information contained in this prospectus with respect to the PRC, the PRC economy and the PRC paper industry derived from third party research reports.

## THE INVESTMENTS

Cathay Special Paper, a company wholly-owned by Cathay Capital Holdings II, L.P., invested in the Company on 19 August 2009 pursuant to the Cathay Subscription Agreement.

Pursuant to the Cathay Subscription Agreement (as supplemented by a supplemental deed entered into between the parties dated 3 December 2009), the Smart Port Preferred Shares issued to Cathay Special Paper are convertible into shares of the future listed vehicle of our Group (i.e. the Company) after completion of the Reorganisation. Further, the shareholding by Cathay Special Paper in our Group is subject to adjustment depending on the financial performance of our Group for the year ended 31 December 2009 and for the year ending 31 December 2010. As our Group has met the stipulated financial performance for the year ended 31 December 2009, no adjustment will be made for the year ended 31 December 2009. Notwithstanding the fact that the forecast for the profit of our Group for the period ending 30 June 2010 is not less than RMB82 million, we expect, solely for the purposes of estimating the likelihood of fulfillment of the 2010 Performance Benchmark, that our full year profit for the year ended 31 December 2010 will meet the 2010 Performance Benchmark. In the event that the 2010 Performance Benchmark is not met thus triggering any share adjustment or payment of the Performance Benchmark Cash Compensation, we will duly make an announcement in accordance with the requirements of the Listing Rules.

Pursuant to an undertaking dated 28 August 2009 entered into between Mr Ke, Smart Port and Cathay Special Paper, Mr Ke and Smart Port have undertaken to Cathay Special Paper that, among other things, if the valuation of our Group immediately prior to the Global Offering is less than RMB1.485 billion, Mr Ke and Smart Port shall cause our Group to declare a special dividend to our then Shareholders prior to the Global Offering. On 1 April 2010, the said parties entered into a deed of release, pursuant to which, Cathay Special Paper released and discharged Mr Ke and Smart Port from causing our Group to declare the said special dividend.

For further details, please refer to "History and Corporate Structure — Investment by Cathay Special Paper — Cathay Subscription Agreement" in this prospectus.

## WORKING CAPITAL

As of 31 December 2007, 2008 and 2009, we had net current liabilities primarily attributable to borrowings comprising mainly short-term loans from commercial banks. For the two years ended 31 December 2008, we mainly relied on short-term bank borrowings to finance our operations and production capacity expansion. As of 31 December 2009, we had long-term bank borrowings of RMB340.2 million. The payment obligations of our trade and other payables and our outstanding short-term debt, as and when they become due, may be satisfied if we maintain adequate cash inflows from operating activities and obtain adequate external financing.

Taking into account our cash inflows from operating and financing activities, including total bank loans and facilities of RMB603.0 million, of which we had drawn down RMB568.0 million and had RMB35.0 million available as of 31 March 2010, and the estimated net proceeds from the Global Offering, our Directors believe that we have sufficient working capital for our present requirements for at least the next 12 months from the date of this prospectus.

*In this prospectus, unless the context otherwise requires, the following expressions shall have the following meanings. Certain other terms are explained in the section headed "Glossary of Technical Terms".*

| | |
|---|---|
| "2009 Adjusted Equity Ratio" | the ratio in determining the transfer of shares from Mr Ke to Cathay Special Paper in order to maintain the equity ratio held by Cathay Special Paper in the Company in the case where the Group failed to achieve the 2009 Performance Benchmark. As we have met the 2009 Performance Benchmark, no share adjustment was triggered for the year ended 31 December 2009, thus 2009 Adjusted Equity Ratio lapsed |
| "2009 Adjustment" | please refer to the formula defining the 2009 Adjustment in "History and corporate structure — Investment by Cathay Special Paper — Cathay Subscription Agreement — Share adjustment mechanism" in this prospectus |
| "2009 Performance Benchmark" | the audited net profit of the Group, including minority interest (if any), for the year ended 31 December 2009 of at least RMB165 million, which we have met the requirement and no share adjustment or payment of Performance Benchmarks Cash Compensation was triggered |
| "2010 Adjusted Equity Ratio" | the ratio in determining the transfer of shares from Mr Ke to Cathay Special Paper in order to maintain the equity ratio held by Cathay Special Paper in the Company in the case where the Group failed to achieve the 2010 Performance Benchmark |
| "2010 Adjustment" | please refer to the formula defining the 2010 Adjustment in "History and corporate structure — Investment by Cathay Special Paper — Cathay Subscription Agreement — Share adjustment mechanism" in this prospectus |
| "2010 Performance Benchmark" | the audited net profit of the Group, including minority interest (if any), for the year ended 31 December 2010 of at least RMB 220 million |
| "Application Form(s)" | **WHITE** application form(s), **YELLOW** application form(s) and **GREEN** application form(s), or where the context so requires, any of them, relating to the Hong Kong Public Offering |
| "Articles of Association" | Articles of Association of our Company, adopted by our Shareholders and as amended from time to time, a summary of which is set forth in Appendix V to this prospectus |
| "associates" | has the meaning ascribed thereto under the Listing Rules |

| | |
|---|---|
| "Best Believe" | Best Believe Holdings Limited, a limited liability company incorporated on 25 September 2009 under the laws of the BVI and a Shareholder, which is owned as to 50% by Mr Johnny Chen and 50% by Mr Li Ho Tan, each an Independent Third Party |
| "Board of Directors" or "Board" | board of Directors of our Company |
| "Business Day" | any day (other than a Saturday or a Sunday) on which banks in Hong Kong are generally open for banking business to the public |
| "BVI" | British Virgin Islands |
| "Capitalisation Issue" | the issue of 749,990,000 Shares to be made upon capitalisation of certain sum standing to the credit of the share premium account of our Company referred to "Written resolutions of our Shareholder passed on 30 April 2010" in Appendix VI to this prospectus |
| "Cathay Special Paper" | Cathay Special Paper Limited, a limited liability company incorporated on 31 July 2009 under the laws of the BVI and a Shareholder, which is wholly owned by Cathay Capital Holdings II, L.P., a limited partnership incorporated in the Cayman Islands to undertake investment in PRC related companies; Cathay Master GP, Ltd. is the general partner of Cathay Capital Holdings II, L.P. and Mr Paul Steven Wolansky, our non-executive Director, has an effective control of 45% in Cathay Master GP, Ltd.; Mr Paul Steven Wolansky is the chairman, president and chief executive officer of New China Capital Management, L.P., the investment manager of Cathay Capital Holdings II, L.P., in which Mr Paul Steven Wolansky has an effective control of 50% |
| "Cathay Subscription Agreement" | the subscription and shareholders' agreement dated 19 August 2009 entered into between, among others, Cathay Special Paper, Smart Port, Xi Yuan BVI, Sunwell, Mr Ke and Mr Ke Jixiong, pursuant to which Cathay Special Paper subscribed for the Smart Port Preferred Shares and as supplemented by the Supplemental Deed |
| "CCASS" | the Central Clearing and Settlement System established and operated by HKSCC |
| "CCASS Clearing Participant" | a person admitted to participate in CCASS as a direct clearing participant or a general clearing participant |

| | |
|---|---|
| "CCASS Custodian Participant" | a person admitted to participate in CCASS as a custodian participant |
| "CCASS Investor Participant" | a person admitted to participate in CCASS as an investor participant, who may be an individual or joint individuals or a corporation |
| "CCASS Participant" | a CCASS Clearing Participant, a CCASS Custodian Participant or a CCASS Investor Participant |
| "China" or "PRC" | People's Republic of China, excluding, except the context otherwise requires and for purposes of this prospectus, the Hong Kong Special Administrative Region of the PRC, the Macau Special Administrative Region of the PRC and Taiwan |
| "China Paper Association" | China Paper Association* (中國造紙協會), a national trade association for paper manufacturers in China which provides its members with regulatory and market information relating to the paper making industry in China, an Independent Third Party |
| "Companies Law" | Companies Law, Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands |
| "Companies Ordinance" | Companies Ordinance (Chapter 32 of the Laws of Hong Kong), as amended and supplemented or otherwise modified from time to time |
| "Company", "our Company", "us", "our" and "we" | Youyuan International Holdings Limited (優源國際控股有限公司), an exempted company incorporated on 12 October 2009 under the laws of the Cayman Islands |
| "connected persons" | has the meaning ascribed to it under the Listing Rules |
| "Controlling Shareholder(s)" | has the meaning ascribed to it under the Listing Rules and unless the content requires otherwise, refers to Smart Port and Mr Ke |
| "Deed of Indemnity" | a deed of indemnity entered by Smart Port and Mr Ke in favour of our Company dated 11 May 2010 pursuant to which Smart Port and Mr Ke have given certain indemnities to our Group |
| "Deed of Non-competition" | a deed of non-competition entered into between Mr Ke and Smart Port as the Controlling Shareholders in favour of the Company dated 5 May 2010 in respect of certain non-competition undertakings given by Mr Ke and Smart Port in favour of the Group |

| | |
|---|---|
| "Denron" | Denron International Limited (利宏國際有限公司), a limited liability company incorporated under the laws of the BVI on 18 March 2009 and a Shareholder, which is wholly-owned by Ms Cai Lishuang |
| "Director(s)" | Director(s) or the board of directors of our Company, respectively |
| "Everproud" | Everproud International Limited (永傲國際有限公司), a limited liability company incorporated under the laws of the BVI on 25 September 2009 and a Shareholder, which is wholly-owned by Mr Ke Jixiong |
| "GDP" | gross domestic product (all references to GDP growth rates are real as opposed to nominal rates of GDP growth) |
| "Giantwish" | Giantwish International Limited (昇望國際有限公司), a limited liability company incorporated under the laws of the BVI on 18 February 2009 and a Shareholder, which is wholly-owned by Ms Ke Jinzhen (柯金珍), the elder daughter of Mr Ke and Ms Cai Lishuang, and the sister of Mr Ke Jixiong and Ms Ke Jinzhi (柯金治) |
| "Global Offering" | the Hong Kong Public Offering and the International Offering |
| "Grand Earning" | Grand Earning International Limited (盈創國際有限公司), a limited liability company incorporated under the laws of the BVI on 25 September 2009 and a Shareholder, which is wholly-owned by Ms Ke Jinzhi (柯金治), the youngest daughter of Mr Ke and Ms Cai Lishuang, and the sister of Mr Ke Jixiong and Ms Ke Jinzhen (柯金珍) |
| "Green Application Form(s)" | the Application Form(s) to be completed by the **White Form eIPO** Service Provider, Computershare Hong Kong Investor Services Limited |
| "Group" | our Company and its subsidiaries or, where the context so requires, in respect of the period before our Company became the holding company of our present subsidiaries, the present subsidiaries of our Company and the businesses carried on by such subsidiaries or (as the case may be) their predecessors, as the case may be |
| "HK$" or "HK dollars" or "HKD" or "Hong Kong dollars" and "cents" | Hong Kong dollars and cents respectively, the lawful currency of Hong Kong |
| "HK GAAP" | generally accepted accounting principles in Hong Kong |

| | |
|---|---|
| "HKSCC" | Hong Kong Securities Clearing Company Limited, a wholly-owned subsidiary of Hong Kong Exchanges and Clearing Limited |
| "HKSCC Nominees" | HKSCC Nominees Limited, a wholly-owned subsidiary of HKSCC |
| "Hong Kong" or "HK" | Hong Kong Special Administrative Region of the People's Republic of China |
| "Hong Kong Public Offering" | the offer for subscription of the Hong Kong Offer Shares to the public in Hong Kong at the Offer Price (plus brokerage of 1%, SFC transaction levy of 0.004% and the Stock Exchange trading fee of 0.005%), subject to and in accordance with the terms and conditions set out in this prospectus and the related Application Forms, as further described in "Structure of the Global Offering — The Hong Kong Public Offering" in this prospectus |
| "Hong Kong Offer Shares" | the 25,000,000 new Shares being initially offered by us for subscription at the Offer Price pursuant to the Hong Kong Public Offering (subject to reallocation as described in "Structure of the Global Offering" in this prospectus) |
| "Hong Kong Share Registrar" | Computershare Hong Kong Investor Services Limited |
| "Hong Kong Underwriters" | the underwriters of the Hong Kong Public Offering whose names are set out in "Underwriting — Hong Kong Underwriters" in this prospectus |
| "Hong Kong Underwriting Agreement" | the underwriting agreement dated 13 May 2010 entered into by, among others, the Company, Mr Ke, Mr Ke Jixiong, the Sole Global Coordinator and the Hong Kong Underwriters relating to the Hong Kong Public Offering, as further described in "Underwriting — Hong Kong Public Offering — Hong Kong Underwriting Agreement" in this prospectus |
| "HSBC" or "Sole Bookrunner" or "Sole Global Coordinator" or "Sole Lead Manager" or "Sole Sponsor" | The Hongkong and Shanghai Banking Corporation Limited |
| "Huaxiang" | Quanzhou Huaxiang Paper Industry Co., Ltd.* (泉州華祥紙業有限公司), a limited liability company established on 9 March 2006 under the laws of China, which is a wholly-owned subsidiary of the Company |

| | |
|---|---|
| "Huaxiang Factory" | Huaxiang's production site located in Jinjiang, Fujian province, the PRC |
| "IFRS" | International Financial Reporting Standards, which include standards, amendments and interpretations issued by the International Accounting Standards Board (IASB) |
| "Independent Third Party(ies)" | persons who, as far as our Directors are aware after having made all reasonable enquiries, are not connected persons of our Company within the meanings of the Listing Rules |
| "International Offering" | the offer of the International Offer Shares outside the United States pursuant to Regulation S and a public offering without listing to investors, including retail investors, in Japan), and in the United States to QIBs as defined in Rule 144A, or any other available exemption from registration under the U.S. Securities Act, as further described in "Structure of the Global Offering" in this prospectus |
| "International Offer Shares" | the 225,000,000 new Shares being initially offered by us for subscription at the Offer Price pursuant to the International Offering together, where relevant, with any additional Shares issued pursuant to the exercise of the Over-allotment Option, the number of which is further subject to reallocation as described in "Structure of the Global Offering" in this prospectus |
| "International Underwriters" | the underwriters of the International Offering, who are expected to enter into the International Underwriting Agreement |
| "International Underwriting Agreement" | the underwriting agreement relating to the International Offering which is expected to be entered into by, among others, the Company, the Sole Global Coordinator and the International Underwriters on or before the Price Determination Date |
| "Latest Practicable Date" | 6 May 2010, being the latest practicable date for the purpose of ascertaining certain information contained in this prospectus prior to its publication |
| "Listing" | listing of the Shares on the Main Board of the Stock Exchange |
| "Listing Date" | the date, expected to be on or about 27 May 2010, on which the Shares are initially listed and from which dealings therein are permitted to take place on the Stock Exchange |
| "Listing Rules" | Rules Governing the Listing of Securities on the Hong Kong Stock Exchange, as amended from time to time |

| | |
|---|---|
| "Main Board" | the stock exchange (excluding the option market) operated by the Stock Exchange which is independent from and operated in parallel with the Growth Enterprise Market of the Stock Exchange |
| "Memorandum of Association" | Memorandum of Association of the Company as amended from time to time |
| "Ministry of Commerce" or "MOFCOM" | Ministry of Commerce of the PRC* (中華人民共和國商務部) |
| "MN" | millions |
| "Mr Ke" | Mr Ke Wentuo (柯文托), founder of our Group, our chairman, executive Director, a Controlling Shareholder, the spouse of Ms Cai Lishuang (蔡麗雙), and the father of Mr Ke Jixiong, Ms Ke Jinzhen (柯金珍) and Ms Ke Jinzhi (柯金治) |
| "Mr Ke Jixiong" | Mr Ke Jixiong (柯吉熊), our executive Director and chief executive officer, the son of Mr Ke and Ms Cai Lishuang, and the elder brother of Ms Ke Jinzhen (柯金珍) and Ms Ke Jinzhi (柯金治) |
| "Ms Cai Lishuang" | Ms Cai Lishuang (蔡麗雙), the spouse of Mr Ke, and the mother of Mr Ke Jixiong, Ms Ke Jinzhen (柯金珍) and Ms Ke Jinzhi (柯金治) |
| "NDRC" | National Development and Reform Commission of the PRC* (中華人民共和國國家發展和改革委員會) |
| "NPC" or "National People's Congress" | National People's Congress of the PRC* (中華人民共和國全國人民代表大會), the national legislative body of the PRC |
| "Offer Price" | the final offer price per Offer Share (exclusive of a brokerage of 1%, SFC transaction levy of 0.004% and Stock Exchange trading fee of 0.005%) of not more than HK$3.38 and expected to be not less than HK$2.58, such price to be agreed upon by us and the Sole Global Coordinator (for itself and on behalf of the Underwriters) on or before the Price Determination Date |
| "Offer Shares" | the Hong Kong Offer Shares and the International Offer Shares with any additional Shares to be issued and sold pursuant to the exercise of the Over-allotment Option |

| | |
|---|---|
| "Over-allotment Option" | the option to be granted by our Company to the International Underwriters exercisable by the Sole Global Coordinator on behalf of the International Underwriters at any time from the date of the International Underwriting Agreement until 30 days from the last day for lodging applications under the Hong Kong Public Offering, to require us to allot and issue up to an aggregate of 37,500,000 additional new Shares at the Offer Price (representing 15% of Shares initially being offered under the Global Offering) solely to cover over-allocations in the International Offering, details of which are described in the section headed "Structure of the Global Offering" in this prospectus |
| "PBOC" | People's Bank of China* (中國人民銀行), the central bank of the PRC |
| "PBOC Rate" | the exchange rate for foreign exchange transactions set daily by the PBOC based on the previous day's interbank foreign exchange rate in China and with reference to prevailing exchange rates on the world financial markets |
| "PHP" | Philippines Peso, the lawful currency of the Philippines |
| "PRC GAAP" | Accounting Standards for Business Enterprises and its interpretations issued by the Ministry of Finance of the People's Republic of China* (中華人民共和國財政部) |
| "PRC government" or "Chinese government" | the central government of the PRC, including all governmental subdivisions (including provincial, municipal and other regional or local government entities) and organisations of such government or, as the context requires, all of them |
| "Price Determination Agreement" | the agreement to be entered into among the Company and the Sole Global Coordinator (on behalf of the Underwriters) on the Price Determination Date to record and fix the Offer Price |
| "Price Determination Date" | the date on which the Offer Price will be fixed for the purposes of the Global Offering expected to be on or about Thursday, 20 May 2010 but no later than Wednesday, 26 May 2010 |
| "prospectus" | this prospectus being issued in connection with the Hong Kong Public Offering |
| "QIBs" or "Qualified Institutional Buyers" | qualified institutional buyers as defined in Rule 144A |
| "Regulation S" | Regulation S under the US Securities Act |

| | |
|---|---|
| "Reorganisation" | the reorganisation of our Group of companies now comprising our Group as described in "History and Corporate Structure — Reorganisation" and in Appendix VI "Statutory and General Information — Reorganisation" to this prospectus |
| "RMB" or "Renminbi" | Renminbi, the lawful currency of the PRC |
| "Rule 144A" | Rule 144A under the US Securities Act |
| "SAFE" | State Administration of Foreign Exchange of the PRC* (中華人民共和國國家外匯管理局), the PRC governmental agency responsible for matters relating to foreign exchange administration |
| "SEPA" | State Environmental Protection Administration of the PRC* (中華人民共和國環境保護總局), which is now known as Ministry of Environmental Protection of the PRC* (中華人民共和國環境保護部) |
| "SFC" | Securities and Futures Commission of Hong Kong |
| "SFO" | Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong), as amended, supplemented or otherwise modified from time to time |
| "Share(s)" | the ordinary shares in the share capital of our Company with a nominal value of HK$0.10 each |
| "Shareholder(s)" | the holder(s) of the Share(s) |
| "Share Option Scheme" | the share option scheme conditionally adopted by our Company on 30 April 2010, the principal terms of which are set forth in Appendix VI "Statutory and General Information — Share Option Scheme" to this prospectus |
| "Smart Port" | Smart Port Holdings Limited, a limited liability company incorporated on 20 July 2009 under the laws of the BVI, which was wholly owned by Mr Ke as at the Latest Practicable Date |
| "Smart Port Loan Agreement" | the loan agreement dated 3 December 2009 entered into between, among others, Cathay Special Paper as lender and Smart Port as borrower in respect of a loan of RMB71.95 million |

| | |
|---|---|
| "Smart Port Preferred Shares" | the 1,178 Series A Preferred Shares issued by Smart Port to Cathay Special Paper pursuant to the Cathay Subscription Agreement representing 11.78% of the total issued share capital of Smart Port between 1 September 2009 and 8 April 2010 |
| "sq.m." | square meter(s) |
| "State Council" | State Council of the PRC* (中華人民共和國國務院) |
| "Stock Borrowing Agreement" | a securities lending agreement to be entered into between HSBC and Smart Port pursuant to which Smart Port agrees to lend certain Shares to HSBC on the terms set out therein |
| "Stock Exchange" | The Stock Exchange of Hong Kong Limited |
| "subsidiary(ies)" | has the meaning ascribed thereto in section 2 of the Companies Ordinance |
| "Sunwell" | Sunwell Trading (HK) Company Limited (香港順優貿易有限公司), a limited liability company incorporated on 13 September 2005 under the laws of Hong Kong, a wholly-owned subsidiary of the Company |
| "Supplemental Deed" | a supplemental deed dated 3 December 2009 entered into between parties to the Cathay Subscription Agreement, pursuant to which the Cathay Subscription Agreement was amended |
| "Takeovers Code" | Codes on Takeovers and Mergers and Share Repurchases issued by the SFC, as amended, supplemented or otherwise modified from time to time |
| "Track Record Period" | the three years ended 31 December 2009 |
| "UFIDA" | UFIDA Software Co. Ltd., one of the leading providers of management software solutions and services in Asia, an Independent Third Party |
| "Underwriters" | the Hong Kong Underwriters and the International Underwriters |
| "Underwriting Agreements" | the Hong Kong Underwriting Agreement and the International Underwriting Agreement |
| "Uniland" | Uniland Box Products Manufacturing, a sole proprietorship established in the Philippines which is wholly-owned by Mr Ke and which is dormant |
| "U.S." or "United States" | United States of America, its territories, its possessions and all areas subject to its jurisdiction |

| | |
|---|---|
| "US$" or "U.S. dollars" | United States dollars, the lawful currency of the United States |
| "US Securities Act" | U.S. Securities Act of 1933, as amended from time to time |
| "**White Form eIPO**" | the application for Hong Kong Offer Shares to be issued in the applicant's own name by submitting applications online through the designated website of **White Form eIPO** **www.eipo.com.hk** |
| "**White Form eIPO** Service Provider" | Computershare Hong Kong Investor Services Limited |
| "WTO" | World Trade Organisation |
| "Xiyuan" | Fujian Xiyuan Paper Co., Ltd.* (福建希源紙業有限公司), a limited liability company established on 18 January 2006 under the laws of China, which is a wholly-owned subsidiary of our Company |
| "Xiyuan Factory" | Xiyuan's production site located in Longhai, Fujian province, the PRC |
| "Xi Yuan BVI" | Xi Yuan Paper Limited (希源紙業有限公司) (previously known as Speed Great Limited), a limited liability company incorporated on 10 July 2009 under the laws of the BVI, which is a wholly-owned subsidiary of our Company |
| "YLF Industry" | Fujian Youlanfa Group Industry Co., Ltd.* (福建優蘭發集團實業有限公司) (previously known as Fujian Jinjiang Xibin Nanxin Recycled Paper Factory* (福建省晉江縣西濱南興再生造紙廠), Fujian Jinjiang Xibin Nanxin Fuli Paper Factory* (福建省晉江西濱南興福利造紙廠) and Jinjiang Younan Paper Manufacturing Co., Ltd.* (晉江優南造紙有限公司)), a limited liability company established on 4 December 1991 under the laws of the PRC, which was owned as to 20% by Mr Cai Qingjiang (蔡清江), brother-in-law of Mr Ke and brother of Ms Cai Lishuang, and as to 80% by Mr Ke Jixiong |
| "YLF Leathercover" | Fujian Youlanfa Leathercover Paper Co., Ltd.* (福建優蘭發塗革紙製品有限公司), a limited liability company established on 25 February 1997 under the laws of the PRC, which is owned as to 75% by YLF Industry and 25% by Uniland |

| | |
|---|---|
| "YLF Trading" | Fujian Jinjiang Youlanfa Trading Co., Ltd.* (福建晉江優蘭發貿易有限公司) (previously known as Fujian Jinjiang Xibin Nanxing Paper Product Industrial Company* (福建省晉江西濱南興製紙品實業公司) and Fujian Jinjiang Xibin Nanxing Paper Product Co., Ltd.* (福建省晉江西濱南興製紙品有限公司)), a limited liability company established on 18 May 2001 under the laws of the PRC, which was owned as to approximately 16.67% by Ms Cai Lishuang and approximately 83.33% by YLF Industry |
| "Youlanfa" | Youlanfa Paper Co., Ltd. Fujian* (福建省晉江優蘭發紙業有限公司), a limited liability company established on 11 November 1994 under the laws of the PRC, which is a wholly-owned subsidiary of our Company |
| "Youlanfa Factory" | Youlanfa's production site located in Jinjiang, Fujian province, the PRC |

*Unless otherwise specified, translations of HK$ into US$, RMB into HK$ and HK$ into RMB in this prospectus are based on the rates set out below (for the purpose of illustration only):*

*US$1.00 : HK$7.7668*
*US$1.00 : RMB6.8269*
*HK$1.00 : RMB0.87898*

*No representation is made that any amounts in RMB, HK$ and US$ can be or could have been converted at the relevant dates at the above rates or any other rates at all.*

*Certain amounts and percentage figures included in this prospectus have been subject to rounding adjustments. Accordingly, figures shown as totals in certain tables may not be an arithmetic aggregation of the figures preceding them.*

** denotes the English translation of the name of a Chinese company or entity or vice versa and is provided for identification purposes only.*

*This glossary contains explanations of certain technical terms used in this prospectus in connection with our Group and our business. These terminologies and their given meanings may not correspond to those standard meanings and usage adopted in the industry.*

| | |
|---|---|
| "bagasse pulp" | fibrous material obtained from the crushed stalks of sugar cane, following the extraction of the juices. The pulp produced is coarse, bulky, and of low strength, and is used principally in the manufacture of boards |
| "basis weight" or "grammage" | weight per unit area of a paper product. This can be expressed as the weight in grams per square meter ($g/m^2$) or pounds per 1,000 square feet (lb/sq), among others |
| "copy paper" | a kind of paper commonly used for photocopying and printing, being one of the three types of products which we manufacture and sell |
| "de-inked pulp" | purified and reusable pulp produced by removing ink and colour from recovered paper |
| "double-sided MF tissue paper" | a type of MF tissue paper usually with a basis weight around $17g/m^2$, being one of the three types of products which we manufacture and sell. We categorise both semi-transparent paper and food wrapping paper as double-sided MF tissue paper. It is commonly used to wrap consumer products and food. It provides higher bursting strength and transparency and is usually sold at higher prices compared with single-sided MF tissue paper |
| "hydrapulper" | a tank-type pulper mainly used to beat and disintegrate recovered paper and pulp board into fluid pulp |
| "ISO" | International Organisation for Standardisation |
| "ISO 10012" | ISO standards for a measurement management system that can be used by an organisation performing measurements as part of an overall management system, and to ensure metrological requirements are met |
| "ISO 14001" | ISO standards for environmental management which are primarily concerned with what an organisation does to minimise harmful effects on the environment caused by its activities and which set requirements for what an organisation must do to manage processes influencing the impact of its activities on the environment |

| | |
|---|---|
| "ISO 9001" | ISO standards for quality management which are primarily concerned with what an organisation does to ensure that its products conform to customer and applicable regulatory requirements and which set requirements for what an organisation must do to manage processes influencing product quality |
| "ivory board" | a type of white paperboard commonly used to manufacture price tags for clothing and other goods or in some instances, boxboard |
| "Kwh" | kilowatts per hour |
| "MF tissue paper" | a type of machine finished (MF) wrapping tissue paper that includes single-sided MF tissue paper and double-sided MF tissue paper |
| "paper towel" | a type of one-time use household paper intended for hygienic purposes, usually used in hotels, restaurants, airports, other public places, or at home for household cleaning purposes |
| "reclaimed pulp" | purified and reusable pulp reclaimed from milkboxes and other packaging boxes for use in paper-making |
| "recovered paper" | used paper and board, composed mainly of used office paper collected separately for re-use as fibre raw material in our production |
| "recycled white paper" | shredded white paper recycled during book and other white paper production, which we use as supplements to wood pulp |
| "single-sided MF tissue paper" | a type of MF tissue paper usually with a basis weight around $14g/m^2$, being one of the three types of products which we manufacture and sell. It has a smooth glazed side and a rough back side and is commonly used to wrap consumer products. It provides lower bursting strength and transparency and is usually sold at lower prices compared with double-sided MF tissue paper |
| "specialty paper" | paper that is typically suitable for special purposes because of its unique characteristics and properties, and is not considered to be one of the standard types of paper used by the paper industry |
| "t/h" | tonne per hour |
| "tissue paper" | paper with grammage of less than 40 $g/m^2$ |
| "tonne" | a metric tonne, equivalent to 1,000 kilograms |

| | |
|---|---|
| "white water" | process water within a paper machine system, especially referring to water that is derived from paper as the sheet is being formed |
| "wood pulp" | fibrous material prepared from wood, cotton, grasses, etc., by chemical or mechanical processes for use in making paper or cellulose products |
| "wrapping tissue paper" | a thin tissue paper generally with basis weight of less than $40g/m^2$ used for wrapping and cushioning items |

We have included in this prospectus forward-looking statements in respect of our plans, intentions, beliefs, expectations or predictions for the future, in particular under the section headed “Business” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations”, which are, by their nature, subject to risks and uncertainties.

The forward-looking statements include, without limitation, statements relating to:

- our business and operating strategies and our various measures to implement such strategies;
- our dividend policy;
- our future capital expenditure plans;
- future development of our business, particularly plans relating to the construction of new production facilities and the launch of new products;
- future developments in the papermaking industry in China;
- the regulatory environment as well as the general industry outlook for the papermaking industry in China; and
- the general economic trends of China.

In some cases, we use words such as “believe”, “intend”, “anticipate”, “estimate”, “project”, “plan”, “potential”, “will”, “may”, “should”, “expect” and similar expressions to identify forward-looking statements. These forward-looking statements reflect our current views with respect to future events and are not a guarantee of future performance. Actual results may differ materially from information contained in the forward-looking statements as a result of a number of factors, including, without limitation, the risk factors set forth under the section headed “Risk Factors” in this prospectus and the following:

- fluctuating paper prices and rising raw material costs or price fluctuations in raw materials;
- increase in competition or any inability to compete effectively and price pressures in the marketplace;
- general economic, market and business conditions in China and other countries;
- our high gearing ratio and our significant floating rate debt which exposes us to fluctuations in interest rates;

- inability to implement our expansion plans in full, within budget or on schedule;
- payment delays and/or default by our customers;
- discontinuance of government grants, changes in government policies and regulations, including changes in tax policy and environmental regulations; and
- the other risk factors discussed in this prospectus as well as other factors beyond our control.

We do not intend to update or otherwise revise the forward-looking statements in this prospectus, whether as a result of new information, future events or otherwise except as required by law. As a result of these and other risks, uncertainties and assumptions, the forward-looking events and circumstances discussed in this prospectus might not occur in the way we expect, or at all. Accordingly, you should not place undue reliance on any forward-looking information. All forward-looking statements contained in this prospectus are qualified by reference to the cautionary statements set forth in this section.

*You should consider carefully all the information set out in this prospectus and, in particular, you should consider and evaluate the following risks associated with an investment in our Group before making any investment decision in relation to the Offer Shares. You should pay particular attention to the fact that our Company is incorporated in the Cayman Islands and that all of our Group's operations are conducted in the PRC and are governed by a legal and regulatory environment which in some respects may differ from what might prevail in other countries. The occurrence of any of the following risks could have a material adverse effect on the business and financial condition of our Group. The trading prices of our Offer Shares could decline due to any of these risks, and you may lose all or part of your investment.*

## RISKS RELATING TO OUR BUSINESS AND OUR GROUP

**We may be unable to implement our expansion plans in full, within budget or on schedule or sustain the considerable business growth that we have experienced during the Track Record Period.**

We have experienced considerable business growth during the Track Record Period. Our revenues increased from RMB267.6 million for the year ended 31 December 2007 to RMB724.8 million for the year ended 31 December 2009, representing a CAGR of 64.6%. We intend to build on the growth we have experienced in recent years by further expanding our production capacity, range of products, and ability to produce de-inked pulp. We expect to spend approximately RMB1.57 billion on capital expenditures between 2010 and 2012 in order to increase our total annual production capacity by an additional 209,250 tonnes. In addition to the four paper production lines added by us between 1 January 2010 and the Latest Practicable Date, our plans include adding nine production lines by the end of 2012 for the production of MF tissue paper and copy paper and adding new de-inking facilities. Additional capital expenditures, other than that related to the anticipated expansion of our production lines, may also be required in the future in order to maintain our operations and for environmental compliance. We anticipate that our capital expenditures will be financed primarily by the proceeds from the Global Offering as well as cash from operating and financing activities. We cannot assure you that our cash generated from operations, together with the proceeds from the Global Offering, will be sufficient to fund our operating needs and expansion projects. We may also be unable to acquire external funding on favourable terms, or at all, in light of the disruptions experienced by the global credit markets since the second half of 2007. If our capital resources are insufficient to fund our expansion projects, we may be unable to implement our development plans in full, or at all.

Moreover, our expansion plans are subject to other operational and market risks that could significantly alter our ability to meet our expansion goals, delay implementation of such expansion plans, lead to an increase in costs or cause our growth rate to slow down. These risks include the inability to procure, or delays in receiving, the equipment and technology necessary for expansion, delays or complications in the design and roll-out of new technologies, delays in obtaining or the inability to obtain government approvals, or increased competition. If we fail to effectively manage these risks, our business operations and expansion plans could be materially and adversely affected, and we may be unable to sustain our historical rates of growth and maintain our position, which could have a material adverse effect on our business, financial condition and results of operations.

**Any oversupply in the PRC wrapping tissue paper market could negatively affect our business.**

In light of strong demand and anticipated strong growth in the domestic PRC wrapping tissue paper market, new companies may enter the wrapping tissue paper market and existing manufacturers may elect to expand production capacity. This additional production capacity could outstrip domestic demand levels and result in an oversupply of wrapping tissue paper in the PRC. If the domestic wrapping tissue paper market suffers from an oversupply, our product prices and profit margins could suffer. In such event, our investment of approximately RMB1.57 billion to expand our production capacity by an additional 209,250 tonnes could take longer to break-even, or may never break-even, and our business, financial condition and results or operations may be materially and adversely affected.

**The prices for and availability of raw materials, and the prices of our products, will significantly impact our business.**

Our business operations are affected by the prices of our raw materials and our products. Our successful operations depend on our ability to obtain from our suppliers sufficient quantities of raw materials, energy supplies and other commodities at acceptable prices and quality levels in a timely manner. Our operations consume substantial amounts of pulp and other raw materials, water, coal and electricity. Any substantial increase in our raw material or energy costs will directly impact our cost of sales. In particular, as a result of the Chilean earthquake in February 2010 and an overall pickup in global economic activity, the market price for wood pulp rose substantially during the first quarter of 2010. In addition, as the prices we charge for our products generally follow market prices, we may not be able to adjust our prices to fully recover significant cost increases, which could adversely affect our operating margins.

Moreover, we may experience shortages of raw materials or energy supplies or be forced to seek alternative sources of supply. We rely on a consistent supply of high quality wood pulp, reclaimed pulp, de-inked pulp and recycled white paper for the production of our paper products and coal for the production of power and steam from our own coal-fired boiler plants. We purchase raw materials other than de-inked pulp from third parties. We purchase our supply of reclaimed pulp, our second largest raw material component, from one supplier. If we are not able to obtain an adequate supply of reclaimed pulp from this supplier, we might be required to purchase more expensive wood pulp. Similarly, if we are forced to seek alternative sources of supply for wood pulp, recycled white paper or other raw materials, we may not be able to obtain them on favorable terms, or at all.

The supply of raw materials and energy depends on a number of factors which are beyond our control, including general economic conditions, environmental and conservation regulations, and import and export regulations. Because of limited domestic forest resources and a pulp production rate that is lagging behind the increasing consumer demand for paper products, there is a shortage of high quality pulp in the PRC and a heavy reliance by the PRC on the international market for wood pulp supply. The PRC also relies on the import of recovered paper for pulp production to meet the growing domestic demand of high quality recovered paper. This supply scarcity and rising demand have driven up the prices of pulp and recovered paper in recent years. For the three years ended 31 December 2009, our total cost of pulp and recycled white paper amounted to RMB128.9 million, RMB257.6 million and RMB322.9 million, respectively, and accounted for 68.9%, 68.9%, and 66.7% of our total cost of sales, respectively. We expect the prices of pulp and recycled white paper to continue to rise. As at the Latest

Practicable Date, we were unable to hedge against any future rise in pulp prices. There is no assurance that we will be able to secure sufficient supplies of raw materials to satisfy our operating requirements in the future. Any disruption in the supply of raw materials or energy could adversely affect our business and results of operations.

Because our revenues are sensitive to fluctuations in MF tissue paper and copy paper prices, a decline in the prices of those products could adversely affect our competitiveness and profitability if we cannot reduce our production costs accordingly, which could have a material adverse effect on our business, financial condition and results of operations.

**We rely on constant and reliable supplies of water to support our production activities.**

Our production processes require significant and constant supplies of water. Our demand for stable supplies of water will increase as we expand our production capacity. Fujian Province, where our operations are based, may suffer from water shortages as a result of interruptions to water supply from local municipalities. Moreover, in the event our boiler plants at our Youlanfa, Huaxiang and Xiyuan Factories cannot satisfy our demand for steam, we are unlikely to be able to obtain steam from alternative sources. Any disruption to or shortage of water and steam supplies or increase in water costs may adversely affect our operations, prevent us from meeting customer orders and/or increase our costs of production and possibly require us to secure alternative sources of supply that may be more expensive or not obtainable at all, which in turn could have a material adverse effect on our business, financial condition and results of operations.

**We maintain a high level of indebtedness and we may be adversely affected by increases in interest rates.**

We currently maintain high levels of indebtedness. As of 31 December 2009, we had secured and unsecured bank borrowings amounted to RMB523.0 million, comprised of short, medium and long-term loan agreements and revolving credit facilities, all of which are denominated in RMB and none of which falls due by 31 March 2010 and RMB182.8 million of which falls due by 31 December 2010. As of 31 March 2010, being the indebtedness date, our bank borrowings amounted to RMB568.0 million, and RMB528.0 million of which falls due within 2010 to 2012. As of 31 March 2010, we had RMB35.0 million available under undrawn bank credit facilities, with expiry dates ranging from 9 July 2010 to 29 October 2010. We have granted security interests over our assets in connection with much of our indebtedness, including our plants and equipments at, and land use rights over, our Youlanfa, Huaxiang and Xiyuan production sites.

Our indebtedness could potentially (a) limit our ability to obtain additional financing; (b) limit our flexibility in reacting to changes in the markets in which we compete; (c) place us at a competitive disadvantage relative to our competitors with less indebtedness and greater cash resources; (d) lead to a partial or complete loss of control over some of our equipment or land use rights, if the security interests given as collateral are enforced; (e) render us more vulnerable to adverse economic and market conditions; and (f) require us to dedicate a certain portion of our cash flow to service our debt. We cannot assure you that we will be able to continue to refinance our bank loans when they become due or that we will have sufficient funds available to repay our bank loans upon maturity. Failure to service our debts or comply with the terms, conditions and covenants of our credit facility agreements could result in the imposition of penalties, including among other things, accelerated repayment of loans and interest, termination of credit facilities, legal action against us by our creditors, and enforcement of security interests over certain of our assets, any of which could materially and adversely affect us.

Moreover, if we are unable to service our debt, we could also be forced to take certain actions which had not previously formed part of our strategy, including delaying or reducing capital or other expenditures in an attempt to restructure or refinance our debt; selling our assets or operations; or raising capital through the sale of additional equity. We might be unable to take any of these actions on favourable terms or in a timely manner, which could have a material adverse effect on our financial condition and results of operations.

In addition, due to our high level of indebtedness, we are exposed to interest rate risks resulting from fluctuations in interest rates. As of 31 December 2009, approximately 66.9% in principal amount of our bank borrowings were subject to floating interest rates. For each of the three years ended 31 December 2009, our interest expenses amounted to approximately RMB13.6 million, RMB20.0 million and RMB18.2 million, respectively. The weighted average interest rates of our total outstanding borrowings as of 31 December 2007, 2008 and 2009 were approximately 7.0%, 6.8% and 4.8%, respectively. We do not currently hedge against increases in interest rates. The PBOC has consistently increased the benchmark loan interest rate since 2004 and only reduced it for the first time in 2008 in light of the slowing economy. We cannot give assurance that the PBOC will not raise the benchmark loan interest rate in the near future. Any increase in interest rates would increase our interest expenses relating to our outstanding floating rate borrowings and increase the cost of new borrowings, including rolled over short term loans, which would adversely affect our financial condition and results of operations.

**We are exposed to risks associated with our net current liabilities position.**

As of 31 December 2007, 2008 and 2009, we had net current liabilities of RMB465.3 million, RMB406.3 million and RMB50.0 million, respectively. As of 31 March 2010, being the indebtedness date, we had net current liabilities of RMB60.9 million. For a more detailed discussion of our net current liabilities position, please refer to “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Net current liabilities” in this prospectus.

For the two years ended 31 December 2008, we mainly relied on short-term bank borrowings to finance our operations and production capacity expansion. As of 31 December 2009, we had long-term bank borrowings of RMB340.2 million. We intend to rely on long-term borrowings to finance our future operations and expansion. Our net current liabilities position exposes us to liquidity risk. Our ability to satisfy the payment obligations of our trade and other payables and our outstanding short-term debt, as and when they become due will depend on our ability to maintain adequate cash inflows from operating activities and to obtain adequate external financing. We cannot assure you that we will not continue to record net current liabilities in the foreseeable future or that we will always be able to obtain the necessary funding to refinance our short-term borrowings upon maturity and finance our capital commitments. The global markets and credit markets have been volatile since the second half of 2007.

In some cases, the markets have restricted the availability of liquidity and credit capacity. We may be unable to raise the necessary funding to finance our working capital and short-term borrowings, which in turn could have a material adverse effect on our business, financial condition and results of operations.

**We have not obtained property title for some of our properties, which could adversely affect our rights to use such properties.**

We have made substantial investments in acquiring land use rights in Jinjiang and Longhai for our existing operations and future expansion. As of the Latest Practicable Date, we had obtained land use rights certificates for 30 parcels of land with a total site area of approximately 620,427.1 sq.m. and building ownership certificates for 84 buildings with a total gross floor area of approximately 167,752.5 sq.m.

As of the Latest Practicable Date, we had not yet obtained building ownership certificates for buildings with a total gross floor area of approximately 2,832.6 sq.m. in Jinjiang, of which, approximately 1,213.3 sq.m. (comprised of a car parking garage of approximately 230.0 sq.m., a waste paper warehouse of approximately 546.0 sq.m., a scrap iron warehouse of approximately 238.0 sq.m., a guard room of approximately 19.3 sq.m., a power distribution room of approximately 60.0 sq.m. and an office room for auxiliary operation purposes of approximately 120.0 sq.m.) was built on parcels for which we did not have use rights ("property A"), and approximately 1,619.3 sq.m. (comprised of a dining area of approximately 279.5 sq.m., a temporary raw materials warehouse of approximately 219.5 sq.m., a resting area of approximately 138.8 sq.m., a security guard room and utilities storage of approximately 82.0 sq.m., dormitories of approximately 514.7 sq.m., an auxiliary manufacturing area of approximately 116.5 sq.m., and an office area of approximately 268.3 sq.m.) partially encroached over property lines of others ("property B"). In addition, we had not obtained construction permits for three buildings ("property C") currently under construction (comprised of a dormitory, a factory building and a warehouse) at our Huaxiang Factory in Jinjiang.

We received a confirmation letter dated 23 December 2009 issued by the Jinjiang Construction Planning and Building Administration Bureau* (晉江市規劃建設與房產管理局) confirming that the construction of the said property C is in compliance with building and construction plans and we shall not encounter legal hindrance in obtaining title certificates after completion of the project and fulfilment of relevant required procedures. Further, due to the progress of the construction project, we expect to obtain the title certificates for property C by the end of 2010. Property C is not directly related nor crucial to the existing operations of the Group.

However, with respect to properties A and B, we will not be able to obtain the relevant land use rights and building ownership certificates and they may be subject to demolition orders by the relevant administrative authority. Properties A and B have been used by us mainly for warehousing, residential and ancillary purposes which are not directly related nor critical to our production process. In this connection, we received two confirmation letters issued by Jinjiang Xibin Town People's Government* (晉江市西濱鎮人民政府) and the Jinjiang Construction Planning and Building Administration Bureau* (晉江市規劃建設與房產管理局) dated 12 January 2010 and 13 January 2010, respectively, and two confirmation letters dated 11 April 2010 issued by each of Jinjiang Xibin Town People's Government* (晉江市西濱鎮人民政府) and the Jinjiang Construction Planning and Building Administration Bureau* (晉江市規劃建設與房產管理局), confirming that we will be allowed to continue to occupy and use properties A and B and we will not be ordered to demolish these properties and no penalty will be imposed on us for our usage of them.

Based on the above confirmations issued by the relevant administrative authorities, we believe that the likelihood of our Group being ordered to close down properties A and B is remote. However, we cannot assure you that the relevant authorities will not order demolition of those properties with title defects, in which case our planned expansion and future growth may be adversely affected, which could have a material adverse effect on our business, financial condition and results of operations.

**We generally do not enter into long-term contracts with our customers and are thus subject to uncertainty and potential volatility with respect to our revenue from period to period.**

Our customers are predominantly regional distributors who sell our products to end users. Our sales agreements with our customers are normally for a term of one year and in the form of "framework letters" which allow our customers to cancel, reduce or defer purchase orders at will. Accordingly, the volume of our customers' purchase orders may vary from period to period, which makes it difficult for us to forecast future order quantities with certainty. No assurance can be given that our customers will continue to purchase from us in the future at the same levels as they have done during the Track Record Period, or at all. Furthermore, the actual volume of our customers' purchase orders may be inconsistent with our anticipated volumes at the time that we plan our expenditures which could negatively impact our procurement and inventory management of raw materials. Any significant or unexpected decrease in customer purchases could have a material adverse effect on our business, financial condition and results of operations.

**We rely on the continuing service of our executive Directors and senior management, and we may be unable to successfully recruit, train and retain management and highly skilled personnel.**

Our ability to successfully implement our proposed plans and maintain growth is dependant on the continued service of our executive Directors and senior management. We depend on their expertise in corporate management and papermaking for the success of our day to day operations. If we were to lose the services of any of our executive Directors or senior management members, especially Mr Ke, an executive Director and our chairman, or Mr Ke Jixiong, an executive Director and our general manager, we may be unable to recruit and retain personnel with equivalent qualifications in a timely manner, which would negatively impact the management and growth of our business. In addition, if any member of our senior management were to join a competitor or form a competing company, we may lose some of our know-how and customers. The departure of one or more of our executive Directors or senior management may have a significant impact on our ability to manage our business effectively and realize our future growth plans and may adversely affect our operations.

Our future success also relies on our ability to attract and retain management and highly skilled personnel who possess the necessary experience and expertise with respect to the papermaking business. In order to implement our expansion plans in full, we will require additional labour. Competition for qualified management and technical personnel in the PRC is intense. Our ability to attract qualified personnel is dependent on the resources available in individual geographic areas and the effect on the labour supply caused by general economic conditions. We may not be able to maintain an adequate skilled labour force necessary for us to operate efficiently, and labour costs may increase as a result of a shortage in the supply of skilled personnel. If we cannot recruit and retain an adequate number of suitable personnel necessary for our operations, our ability to operate and expand our production facilities may be limited, which could reduce our profitability and adversely affect our business, financial condition and results of operations.

**Failure to comply with the applicable quality, health and safety standards or labour laws of the PRC could lead to fines, lawsuits, or other penalties.**

Our products are subject to strict PRC product quality specifications, and our operations are also subject to rigorous PRC safety standards and routine safety inspections. If the PRC government determines that our products or operations do not meet national or local standards for quality and safety, or are in breach of labour laws, we could be subject to significant fines or be required to invest additional capital to carry out necessary improvements to meet such standards, which could cause us to be less profitable or have less resources available to invest in future expansion. In addition, should our products or failure to adhere to standard practices lead to harm, or cause property damage, injury or death to employees as a result of a failure to meet the relevant quality or safety standards in the PRC or labour laws of the PRC, we could be subject to fines, penalties and lawsuits, and suffer significant harm to our reputation, which could have a material adverse effect on our business, financial condition and results of operations.

**We may be subject to losses that are not covered in whole or in part by our insurance policies.**

We may become subject to liabilities against which we have not insured adequately or at all or liabilities against which we cannot insure. Should any significant property damage or personal injury occur to our production facilities or employees due to accidents, natural disasters or similar events, our business may be adversely impacted, potentially leading to a loss of assets, lawsuits, employee compensation obligations or other forms of economic loss. Consistent with customary practice in the PRC, we do not have certain types of insurance, such as business interruption insurance, third party liability insurance for personal injury, environmental damage, or product liability insurance. Our insurance policies also may not continue to be available at economically acceptable premiums. Moreover, we cannot obtain certain types of insurance at a reasonable cost or at all. For example, insurance covering losses from acts of war, terrorism or natural catastrophes is either unavailable or cost prohibitive. Any losses that we incur for which we are uninsured may adversely affect our business, financial condition and results of operations.

**We may not be able to adequately protect our intellectual property rights and industrial know-how, and we may become involved in costly or unsuccessful intellectual property disputes.**

If we fail to protect our intellectual property rights and industrial know-how adequately, our competitors might gain access to our technology. Monitoring unauthorized use of our intellectual property is difficult, and we cannot be certain that the steps we have taken will prevent unauthorized use of our technology and confidential information, and applicable laws may not fully protect our proprietary rights. Any claims or litigation that we may initiate in the future to protect our intellectual property rights could be time consuming and expensive and divert the attention of our technical and management resources whether or not the disputes are decided in our favor. Moreover, any significant infringement of our confidential information and the proprietary technologies and processes used in our business could weaken our competitive position, increase our operating costs and have an adverse effect on our operations.

As we expand our business and increase our market coverage, third parties may assert that our technology or products violate their intellectual property rights. Successful intellectual property claims against us could result in significant financial liability or prevent us from operating our business or parts of our business. In addition, resolution of claims may require us to redesign our technology, to obtain licenses to use intellectual property belonging to third parties, which we may not be able to obtain on reasonable terms, or at all, or to cease using the technology covered by those third party rights. Any of these events could adversely affect our business, financial condition and results of operations.

**Any mechanical failure or disruption within our production facilities could negatively affect our business.**

Our production lines operate on a continuous and uninterrupted basis, except for temporary stoppages for machine cleaning, periodic inspection and maintenance work, which lasts for approximately 24 to 36 hours once a month and annual maintenance which lasts for approximately one week. All of our production lines are comprised of an interdependent chain of machines. Operation failure of one machine would lead to a failure of or disruption to the operation of the entire production line. As such, there is a risk that damage to a single machine could cause a disruption to an entire production line, which could significantly delay our production schedule. In addition, our facilities could cease operations due to prolonged power failures, chemical spills, explosion of a boiler and other operational problems. Any such disruption to our production operations may adversely affect our business, financial condition and results of operations.

**We rely on the orderly operation of transportation infrastructure.**

The success of our operation depends on the timely delivery to us of raw materials, which depends, in turn, on an effective transportation infrastructure. Our raw material purchases are transported mainly by road and sea freight by third-party transportation providers. Shipments of raw materials may be delayed due to weather conditions, work stoppages at Xiamen Port, lack of rail capacity, sub-standard transportation infrastructure, shipping problems or disruptions in operations. There can be no assurance that events beyond our control will not cause disruption of our raw material supply, which could cause a material adverse effect on our business, financial condition and results of operations.

**We are exposed to payment delays and/or defaults by our customers.**

With the exception of new customers or those without a proven credit history, we generally offer our customers credit periods of up to 60 days following the date of delivery of our products. There is no assurance that our customers will meet their payment obligations on time or in full or that our average trade receivables turnover days will not increase. Any inability on the part of our customers to settle or settle promptly the amounts due to us may adversely affect our financial performance and operating cash flows, which could have a material adverse effect on our business, financial condition and results of operations.

## RISKS RELATING TO THE INDUSTRY

**We may face increased competition in relation to our products.**

The markets for our paper products are highly competitive in the PRC. We compete on the basis of our product quality, consistency, performance and price. If we are unable to anticipate and respond to changing customer preferences or control our costs in connection with our planned expansion, raw materials and energy, we may not be able to compete effectively.

In addition, in local markets where we are not currently a market leader or where we do not currently have an established presence, we cannot assure you that we will be able to compete effectively or gain market share. The inability to compete effectively in new local markets may adversely affect our expansion plans and future growth.

As the PRC wrapping tissue paper industry is open to foreign investment, foreign companies may establish wrapping tissue paper manufacturing enterprises in the PRC, in which case we may face increasing competition from such enterprises, which may have greater access to financial resources, more sophisticated technologies and longer operating histories. If we are unable to maintain our operating efficiency and economies of scale, we may not be able to compete effectively. In addition, as the volume of imported wrapping tissue continues to increase, up 8.6% in 2008 as compared to 2007 according to the China Paper Association, our products may face more competition from imported products. Our failure to compete successfully against our competitors could have a material adverse effect on our business, financial condition and results of operations.

**Compliance with environmental regulations may significantly increase our operating costs.**

Paper production generates solid and liquid waste by-products, including wastewater, sludge, gaseous emissions, and other hazardous wastes. Compliance with environmental regulations is of vital importance to our business. Local and national environmental regulations govern our responsibilities and liabilities with respect to the discharge of these by-products.

In recent years, PRC regulators have placed greater emphasis on environmental issues, and have issued numerous national and local environmental laws and regulations, such as the Environmental Protection Law of the People's Republic of China* (中華人民共和國環境保護法), Law of the People's Republic of China on the Prevention and Control of Water Pollution* (中華人民共和國水污染防治法), Law of the People's Republic of China on the Prevention and Control of Environmental Pollution by Solid Waste* (中華人民共和國固體廢物污染環境防治法), and Laws of the People's Republic of China on Environmental Impacts Appraisal* (中華人民共和國環境影響評價法), Law of the People's Republic of China on Promoting Cleaner Production* (中華人民共和國清潔生產促進法), and Environmental Protection Regulation of Fujian Province* (福建省環境保護條例). Environmental laws and regulations could become more stringent in the future. These environmental laws and regulations impose rigorous standards on us regarding water discharge, airborne emissions, the use, handling, discharge and disposal of solid waste and hazardous materials, noise pollution, and remediation of environmental contamination. Failure by us to meet the environmental standards stipulated by PRC law could cause us to suffer business suspension, fines, lawsuits and may cause significant damage to our reputation.

In addition, our operating expenses may increase if the standards, or interpretation or enforcement of standards, for discharge become stricter. In such cases, we may be required to construct additional waste disposal treatment facilities or take stricter internal control measures or restrict our production capacity in order to reduce the amount of discharge generated, which would leave us with less capital to pursue our growth and development.

We are liable for damages caused by pollutants generated during our production. We cannot assure you that we will at all times be in full compliance with all of the environmental laws and regulations that apply to our operations. Any failure, or any claim that we have failed, to comply with environmental laws and standards could cause delays in our production and capacity expansion, which may adversely affect our business, financial condition and results of operations.

## RISKS RELATING TO THE PRC

All of our assets are located in the PRC and all of our revenue is derived from our operations in the PRC. As a result, our assets and operations are subject to significant political, economic, legal and other uncertainties associated with doing business in the PRC, which are discussed below in greater detail.

**All our revenue is derived from sales in the PRC. Changes in political or economic policies or a slowdown in the PRC economy may have an adverse impact on the demand for our paper products.**

For each of the three years ended 31 December 2009, we generated all our revenue from sales of products in the PRC. We anticipate that revenues from sales of our products in the PRC will continue to represent all, if not, substantially all, of our total revenue in the medium term as all our distributor customers are located in the PRC. Consequently, our results of operations and prospects are and will continue to be subject to political, legal and economic developments in the PRC to a significant degree.

The PRC economy differs from the economies of most developed countries in that the extent of government involvement plays a pivotal role in affecting many aspects of the economy, such as allocation of resources, capital reinvestment, levels of development, growth rate, and control of foreign exchange. The PRC government has implemented various measures to guide the development of the paper industry, such as restructuring the fragmented paper industry and encouraging foreign investment, both of which have led to changes in market conditions including paper prices and market structure of the paper industry. However, policies and measures that were introduced and those that may be introduced by the PRC government in the future to benefit the PRC paper industry in general may have a negative effect on us. For example, the forced shut down of smaller pulp mills for environmental reasons has reduced domestic pulp supply and driven up pulp prices. Any adverse change in government policies that increases our cost of production could adversely affect our business and financial condition.

The demand in the PRC for our paper products has increased as the PRC has undergone rapid economic growth resulting in rising living standards and use of value-added paper products such as wrapping tissue paper, the consumption of which grew by approximately 7.2% in 2008 as compared to 2007. Accordingly, any negative development of general economic conditions in the PRC and demand for products for which our paper products are used may have a material adverse impact on the demand and prices for our products. In addition, the PRC's integration into the global economy has made it more susceptible to volatility and disruption in global capital and credit markets. In recent periods, concerns over inflation or deflation, energy costs, geopolitical issues and the availability and cost of credit have contributed to unprecedented levels of market volatility and diminished expectations for the global economy and the capital and consumer markets in the future. These factors, combined with volatile oil prices, declining business activity and consumer confidence and increased unemployment, have precipitated an economic slowdown and a possible prolonged global recession. As a result, we could face decreasing prices and sales volumes should such a global economic downturn persist and inhibit demand for our paper products, which could have a material adverse effect on our business, financial position and results of operations.

**Our business and operations may be adversely affected by events that are beyond our control.**

Our business is subject to events that are beyond our control, such as natural disasters, epidemics, acts of God, fires, floods, earthquakes, industrial accidents, labour strikes, equipment failures, wars, transportation bottlenecks or damage to public infrastructure. Any of these events has the potential to materially disrupt our normal operations and those of our customers and suppliers, which could result in a loss of revenue and profit. The eastern part of the PRC, where our business and operations are principally located, is under the threat of flood, earthquake, tropical cyclones, fire and drought. Certain areas of the PRC, including Fujian province, are susceptible to epidemics, such as Severe Acute Respiratory Syndrome ("SARS") or swine or avian influenza. A recurrence of SARS, an outbreak of swine or avian influenza, or any epidemic in Fujian province or other areas of the PRC, could result in material disruptions to our operations or a slowdown of the PRC's economy. Any of the events listed above could disrupt our operations, increase our production costs, and cause significant losses, which in turn may adversely affect our business, financial condition and results of operations.

**A change in the PRC tax policy could cause an increase in our tax liabilities.**

Our revenue is derived from our operations in the PRC. Under the PRC law, income generated by companies in the PRC is subject to the PRC enterprise income taxes. Under the previous PRC laws and regulations, a PRC domestic company was subject to an enterprise income tax at the rate of 33% on its taxable income. The PRC Government has provided various incentives to foreign-invested enterprises to encourage foreign investments. Such incentives include exemption and reduction of income tax and other measures. Pursuant to the previous enterprise income tax laws applicable to foreign-invested enterprises, a foreign-invested enterprise engaged in manufacturing, such as Youlanfa, Huaxiang and Xiyuan, is exempted from paying enterprise income tax for two years starting from the first profit-making year followed by a 50% reduction in the enterprise income tax in the following three years. Our PRC subsidiaries Xiyuan and Huaxiang are exempted from enterprise income tax for two years starting from 2008, and are entitled to a 50% reduction in enterprise income tax thereafter for three years, or until 2012. Our PRC subsidiary Youlanfa ceased benefiting from the tax exemption and reduction in 2003.

Pursuant to the Enterprise Income Tax Law of the PRC*（中華人民共和國企業所得稅法）enacted on 16 March 2007 and the Implementation Regulations of Enterprise Income Tax Law of the PRC*（中華人民共和國企業所得稅法實施條例）enacted on 6 December 2007 (collectively the "Income Tax Law"), both of which took effect on 1 January 2008, a uniform tax rate of 25% is adopted for all enterprises, including foreign-invested enterprises, and revokes many of the previous tax exemptions, reductions and preferential treatments which were applicable to foreign-invested enterprises. However, foreign-invested enterprises that were incorporated before 16 March 2007 and were entitled to exemptions or reductions of the enterprise income tax for a fixed term according to the then applicable tax laws and administrative regulations, such as those enjoyed by Huaxiang and Xiyuan, may continue to enjoy such favourable treatment until the earlier of the expiration of such fixed terms and 2012.

Moreover, under the Income Tax Law, if an enterprise incorporated outside the PRC has its "de facto management organisation" located within the PRC, the enterprise may be recognised as a PRC resident enterprise and thus may be subject to an enterprise income tax at the rate of 25% on its worldwide income. The term "de facto management organisations" refers to entities exercising overall management and control over issues such as operations, personnel, finance and assets. Substantially all of our management team members are residing in the PRC. If most of them continue to reside in the PRC, we can not assure you that our offshore companies will not be deemed as PRC resident enterprises under the Income Tax Law and therefore be subject to the PRC enterprise income tax at a rate of 25% on our worldwide income, which excludes the dividends received directly from another PRC resident enterprise, and our distributable profits may be adversely affected. An increase in our effective income tax rate or a finding that subjects us to PRC enterprise income tax may adversely affect our business, financial condition and results of operations.

In addition, under the Income Tax Law, PRC withholding income tax at the rate of 10% is applicable to dividends payable by a PRC tax resident enterprise to investors that are "non-tax resident enterprises" (and that do not have an establishment or place of business in the PRC, or that have such establishment or place of business but the relevant income is not effectively connected with the establishment or place of business) to the extent that such dividends have their sources within the PRC. If our offshore companies are deemed PRC resident enterprises, it is unclear whether the dividends we pay with respect to the Shares may be treated as income derived from sources within the PRC and be subject to PRC taxes. If we are required under the Income Tax Law to withhold PRC income taxes on our dividends payable to our foreign Shareholders, the value of your investment in the Shares may be materially and adversely affected.

In addition, the Notice on Strengthening Administration of Enterprise Income Tax for Share Transfers by Non-PRC Resident Enterprise* (關於加強非居民企業股權轉讓所得企業所得税管理的通知) (Circular Guoshuihan [2009] No. 698) issued by the State Administration of Taxation* (國家税務總局) on 10 December 2009 provides that where a foreign investor indirectly transfers the equity of a PRC resident enterprise by disposing the equity of an overseas holding company ("Indirect Transfer") located in a tax jurisdiction that: (i) has an effective tax rate of less than 12.5%, or (ii) does not tax its residents on their foreign incomes, the foreign investor shall report the Indirect Transfer to the competent PRC tax authority. The PRC tax authority will examine the true nature of the Indirect Transfer. Should it deem the foreign investor to have made the transfer in order to avoid the PRC tax, the PRC tax authority may disregard the existence of the overseas holding company and re-characterize the Indirect Transfer. As a result, gains derived from such Indirect Transfer may be subject to the PRC withholding tax at the rate of 10%. Circular Guoshuihan [2009] No. 698 also provides that, where a non-PRC resident enterprise transfers its equity interests in a PRC resident enterprise to its related parties at a price lower than the fair market value, the competent tax authority has the authority to adjust the amount of taxable income pertaining to the transaction.

We cannot assure you any direct or indirect transfer of our equity interests in our PRC subsidiaries via our overseas holding companies in the future will not be subject to examinations by our PRC subsidiaries' tax authorities and will be imposed a withholding tax of 10%, even if we or our overseas subsidiaries are considered as non-PRC resident enterprises.

**Any change in PRC industrial policy could adversely impact our profitability and ability to implement our expansion plans.**

With regard to the paper industry, the PRC government has implemented a policy which encourages the growth of larger enterprises by providing support, such as supply of materials and assistance with new product development, while restricting the establishment of smaller paper companies, in an effort to reduce pollution and save timber and energy. Any change in PRC industrial policy could cause us to lose the governmental support we currently enjoy, which could lead to difficulty in adequately funding key projects or accessing the raw materials we need. Should this happen, our profitability and ability to expand our operation may be adversely affected.

The NDRC promulgated the "Paper Making Industry Development Policy* (造紙產業發展政策)" (the "Policy") on 15 October 2007 which provides that enterprises whose production of a single type of paper product that accounts for more than 35% of the domestic market share shall be disallowed from filing for the approval of new construction projects related to that particular type of paper product. Furthermore, the Policy states that a paper company with a production capacity exceeding 20% of the total domestic market consumption volume shall be disallowed from filing for the approval of new pulp and paper making projects. Finally, the Policy allows the NDRC to enact various standards relating to water and energy consumption, pollution discharge, the phasing out of certain obsolete pulp and paper producing equipment, and the construction of new pulp and paper production lines, all of which apply to businesses with a single product that have a domestic market share exceeding 35% or a paper and paperboard production capacity exceeding 20% of the domestic market.

As of the Latest Practicable Date, we did not produce any single type of paper product (according to the classification in the Policy) that has a domestic market share exceeding 35% for any single type of paper product and we did not have an aggregate production capacity exceeding 20% of the total domestic market consumption volume. Therefore, we are not currently affected by the aforesaid provisions of the Policy. However, as our business and production capacity grows, we may become subject to the provisions described above and other restrictions contained in the Policy in the future. Should our market share and aggregate production capacity in the future require us to comply with the Policy and NDRC's standards, our business, financial condition and results of operations may be adversely affected.

**Gains on the sales of the Offer Shares and distributions on the Offer Shares may be subject to PRC withholding taxes.**

Under the Income Tax Law, we may in the future be treated as a PRC resident enterprise by the PRC tax authorities. As such, we may be required to withhold PRC income tax on gains realised from sales of our Shares and distributions on our Shares, as such income may be regarded as income from "sources within the PRC." In such case, our foreign corporate shareholders may become subject to a 10% withholding income tax under the Income Tax Law, unless any such foreign corporate shareholder is qualified for a preferential withholding rate under a tax treaty. Other shareholders may also become subject to similar withholding as well. If the PRC tax authorities treat us as a PRC resident enterprise, shareholders who are not PRC tax residents and seek to enjoy preferential tax rates under relevant tax treaties will need to apply to the PRC tax authorities for recognition of eligibility for such treaty benefits in accordance with the Administration Measures on Non-resident Enjoying Treatment in Tax Treaties (Trail)* (非居民享受稅收協定待遇管理辦法(試行)) (Circular Guoshuifa [2009] No. 124), issued by the State Administration of Taxation* (國家稅務總局) on 24 August 2009. It is likely that eligibility for such treaty benefits will be based on a substantive analysis of the applicable shareholder's tax residency and economic substance and, in the case of dividends, also will be based on the beneficial ownership tests pursuant to the Notice on How to Understand and Identify "Beneficial Owners" in Tax Treaties*

(關於如何理解和認定稅收協定中"受益人"的通知) (Circular Guoshuihan [2009] No. 601). If any PRC tax is imposed on gains realised from sales of our Shares or on distributions on our Shares, the value of an investment in the Offer Shares by a shareholder who is not a PRC resident may be materially and adversely affected.

**Our PRC subsidiaries are subject to restrictions on paying dividends to us and the tax exemptions on dividends received by the Company and the Shareholders may be affected by the newly enacted Income Tax Law.**

We are a holding company incorporated in the Cayman Islands, and we rely on dividends paid by our PRC operating subsidiaries for our cash requirements, including the funds necessary to pay dividends and other cash distributions to our Shareholders, to service any debt we may incur, and to pay our operating expenses. Under PRC laws, dividends may be paid only out of distributable profits. Distributable profits with regard to the subsidiaries of a company incorporated in the PRC means their after tax profits as determined under PRC GAAP, less any recovery of accumulated losses and allocations to statutory funds that it is required to make. Any distributable profits that are not distributed in a given year are retained and available for distribution in subsequent years. The calculation of distributable profits under PRC GAAP differs from generally accepted accounting policies in other jurisdictions. As a result, the subsidiaries of a company incorporated in the PRC may not be able to pay dividends in any given year to a company if they do not have distributable profits as determined under PRC GAAP, even if they have profits for that year as determined under generally accepted accounting principles in other jurisdictions. In addition, if our PRC subsidiaries incurs debt on their own or enter into certain other agreements in the future, the instruments governing the debt or such other agreements may restrict their ability to pay dividends or make other distributions to us. Accordingly, since we derive all of our profits from our subsidiaries, we may not have sufficient distributable profits to pay dividends to our Shareholders, even if there is such an amount shown in our accounts prepared under other generally accepted accounting policies.

In addition, we hold interests in Youlanfa, Huaxiang and Xiyuan through a Hong Kong company. Under the Income Tax Law, dividends from PRC enterprises to their foreign shareholders will be subject to a withholding tax at a rate of 10%, unless the jurisdiction of incorporation of such foreign shareholders has a tax treaty with the PRC that provides for a different withholding arrangement. On 21 August 2006, Hong Kong and the PRC entered into the Arrangement between the PRC and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income* (內地和香港特別行政區關於對所得避免雙重徵稅和防止偷漏稅的安排) (the "Tax Arrangement"), which provides that the withholding tax rate for the dividends between Hong Kong resident enterprises and PRC resident enterprises is: (a) 5% of dividends in case that the enterprise of one side holds at least a 25% equity interest of the enterprise of the other side or (b) 10% of dividends in other cases. According to the Administrative Measures for Non-resident Enterprises to Enjoy Treatments under Tax Treaties* (非居民享受稅收協定待遇管理辦法)(試行) (the "Administrative Measures") which came into force on 1 October 2009, where a non-resident enterprise (as defined under the PRC tax laws) receiving dividends from PRC resident enterprises wants to enjoy the favorable tax benefits under the tax treaties, it shall submit an application for approval to the competent tax authority. If the application for enjoying the favourable withholding tax under the Tax Arrangement is not approved, it may not enjoy the favorable withholding tax under the Tax Arrangement. Moreover, according to the

Notice of the State Administration of Taxation on Issues Relating to the Implementation of the Dividend Provision in Tax Treaties* (關於執行稅收協定股息條款有關問題的通知) ("Notice 81"), if the primary purpose of a transaction or an arrangement in relation to the reorganisation of PRC subsidiaries is deemed by the competent authorities to have been made for the purpose of enjoying favorable tax treatment, such favorable tax treatment may be adjusted by the competent authorities. As we may receive dividends from Youlanfa, Huaxiang and Xiyuan through our Hong Kong subsidiary, we cannot assure you that the Hong Kong subsidiaries can enjoy the favourable withholding tax rate of 5% as the reorganisation of the PRC subsidiaries may be deemed to have been made in order to enjoy favourable tax treatment. This may reduce the amount of our future distribution of profits to our Shareholders.

**Changes in foreign exchange regulations may adversely affect our ability to pay dividends.**

We receive all of our revenue in RMB, which is not freely-convertible into other currencies. As a result, any restriction on currency exchange may limit the ability of our subsidiaries to use our revenue generated in RMB to pay dividends to us. Under existing foreign exchange regulations in the PRC, following completion of the Global Offering, our PRC subsidiaries may make payment of dividends without prior approval from SAFE by producing documents including but not limited to commercial documents evidencing dividend allocation, provided that they are processed through PRC banks licensed to engage in foreign currency transactions. The PRC government has stated publicly that it intends to make the RMB freely convertible in the future. However, uncertainty exists as to whether the PRC government may restrict access to foreign currency for current account transactions if foreign currency becomes scarce in the PRC, in which case our ability to pay dividends or satisfy other foreign exchange requirements may be adversely affected.

**Fluctuation in the value of the Renminbi may adversely affect our business.**

We purchase wood pulp from suppliers in the United States, Canada, Germany and Chile using the U.S. dollar. The exchange rates of these currencies relative to RMB, our functional currency, may fluctuate and may materially and adversely affect our business, financial condition and results of operations in the future.

The value of the RMB against the U.S. dollar and other currencies fluctuates and is affected by, among other things, changes in the PRC's political and economic conditions. The conversion of RMB into foreign currencies, including U.S. dollars, has been based on the PBOC Rates. On 21 July 2005, the PRC government changed its policy of pegging the value of the RMB to the U.S. dollar. Under the new policy, the RMB is permitted to fluctuate within a narrow and managed band, against a basket of certain foreign currencies. On 23 September 2005, the PRC government widened the daily trading band for RMB against non-U.S. dollar currencies from 1.5% to 3.0% to improve the flexibility of the new exchange system. Between 21 July 2005 and 31 December 2008, the RMB appreciated approximately 18.6% against the U.S. dollar. Any negative development in the exchange rate of RMB to U.S. dollars may increase our raw material procurement costs, which may adversely affect our business, financial condition and results of operations.

**PRC regulations concerning direct investment and loans by offshore holding companies to PRC entities may delay or limit us from funding our PRC subsidiaries.**

Any capital contribution or loans that we, as an offshore entity, make to our PRC subsidiaries including from the proceeds of this Global Offering, are subject to PRC laws. For example, any of our loans to our PRC subsidiaries cannot exceed the margin between the total amount of investment that our PRC subsidiaries are approved to make under relevant PRC laws and the registered capital of those PRC subsidiaries, and any such loans must be registered with the competent SAFE branches. In addition, our additional capital contributions to our PRC subsidiaries must be approved by the PRC Ministry of Commerce or its local counterpart. We cannot give assurance that we will be able to obtain these approvals on a timely basis, or at all. If we fail to obtain such approvals, our ability to make equity contributions or provide loans to our PRC subsidiaries or to fund their operations may be affected, which could harm our PRC subsidiaries' liquidity and their ability to fund working capital and expansion projects, all of which may adversely affect our business, financial condition and results of operations.

**Changes and uncertainties in the PRC legal system may have an adverse impact on our operations.**

The PRC is still in the process of developing a comprehensive statutory framework. Since 1979, the PRC government has established a commercial law system, and significant progress has been made in promulgating laws and regulations relating to economic affairs and matters such as corporate organisation and governance, foreign investment, commerce, taxation and trade. However, many of these laws and regulations are relatively new, and the implementation and interpretation of these laws and regulations remain uncertain in many areas. Consequently, developments and changes in PRC laws and regulations, including their interpretation and enforcement, may adversely affect our business, financial condition and results of operations.

**It may be difficult to effect service of process upon the Company or on our Directors who live in the PRC or to enforce judgments obtained from non-PRC courts against us.**

We are incorporated in the Cayman Islands and the majority of our Directors reside in the PRC. All of our assets and some of the assets of our Directors are located within the PRC. Therefore, it may not be possible for investors to effect service of process upon us or our Directors inside the PRC. The PRC has not entered into treaties or arrangements providing for the recognition and enforcement of judgments made by courts of most other jurisdictions. More specifically, the PRC does not have treaties or agreements providing for the reciprocal recognition and enforcement of judgments awarded by courts of the United States, the United Kingdom, or most other western countries or Japan. Hence, the recognition and enforcement in the PRC of judgments of a court in any of these jurisdictions in relation to any matter not subject to a binding arbitration provision may be difficult or even impossible. The possible need to re-litigate in the PRC a judgment obtained in a foreign court on the merits may require investors to incur significant additional costs and delays. As a result, it may be difficult or impossible for investors to effect service of process against our assets or Directors in the PRC in order to seek recognition and enforcement for foreign judgments in the PRC.

In addition, any judgment obtained in the United States or Hong Kong against us, including a judgment based on the civil liability provisions of the U.S. federal securities laws or under the laws of Hong Kong, may not be collectable in the United States or Hong Kong, as the case may be, and may not be enforced by a Cayman Island court as Cayman Islands does not have bilateral conventions on recognition of foreign court judgments with either the United States or Hong Kong. It also may be difficult for investors to assert U.S. securities law claims or claims under the laws of Hong Kong in original actions instituted in the Cayman Islands.

**The enforcement of the Labour Contract Law and other labour-related regulations in the PRC may adversely affect our business and our results of operations.**

On 29 June 2007, the National People's Congress of the PRC enacted the PRC Labour Contract Law* (中華人民共和國勞動合同法) ("Labour Contract Law"), which was implemented on 1 January 2008. Compared to the Labour Law of the PRC* (中華人民共和國勞動法), the Labour Contract Law establishes more restrictions and increases an employer's costs when reducing its workforce. The Labour Contract Law includes specific provisions related to fixed-term employment contracts, temporary employment, probation, consultation with labour unions and employee general assemblies, employment without a contract, dismissal of employees, compensation upon termination and overtime work, and collective bargaining. According to the Labour Contract Law, an employer is obligated to enter into a labour contract without fixed term with an employee if the employer continues to employ the employee after two consecutive fixed term labour contracts. The employer also has to pay compensation to employees if the employer terminates an unlimited term labour contract for any reason other than those set out under the Labour Contract Law. Further, under the Regulations on Paid Annual Leave for Employees* (職工帶薪年休假條例), which were implemented on 1 January 2008, employees who have served more than one year with an employer are entitled to paid vacation ranging from five to 15 days, depending on their length of service. Employees who waive such vacation entitlement at the request of employers shall be compensated at three times of their normal salaries for each waived vacation day. As a result of these protective labour measures, our Group's historical labour costs may not be indicative of our labour costs going forward. Compliance with the relevant laws and regulations may substantially affect our operating costs and thus may have a material adverse effect on our results of operations.

**Failure to comply with PRC regulations in respect of the registration of share options belonging to our employees who are PRC citizens may subject such employees or us to fines and legal or administrative sanctions.**

Pursuant to the Implementation Rules of the Administration Measure for Individual Foreign Exchange* (個人外匯管理辦法實施細則), (the "Individual Foreign Exchange Rules"), issued on 5 January 2007 by SAFE and the Operating Rules on the Foreign Exchange Administration of the Involvement of Domestic Individuals in the Employee Stock Ownership Plans and Share Option Schemes of Overseas Listed Companies* (境內個人參與境外上市公司員工持股計劃和認股期權計劃等外匯管理操作規程) issued on 28 March 2007 by SAFE (the "Operating Rules"), PRC citizens residing in the PRC who are granted shares or share options by an offshore listed company through an employee share option or share incentive plan are required, through the PRC subsidiary of such offshore listed company or other qualified domestic PRC agents, to obtain the approval from SAFE or its local branches and complete certain other procedures related to the share option or other share incentive plan.

In order to comply with the requirements of the Individual Foreign Exchange Rules and the Operating Rules, we will require our PRC employees to obtain approval from SAFE or its local branches when joining the Share Option Scheme. Foreign exchange income from the sale of shares or dividends distributed by an offshore listed company must be remitted into the PRC. In addition, an offshore listed company or its PRC subsidiary or a qualified PRC agent is required to appoint an asset manager or administrator and a custodian bank, as well as open foreign currency accounts to handle transactions relating to the share option or other share incentive plan. We and our PRC citizen employees who have been granted share options, or PRC option holders, will be subject to these rules upon the listing of our

Shares on the Stock Exchange. If we or our PRC option holders fail to comply with these rules in the future, we or our PRC option holders may be required to rectify such non-compliance, and a maximum fine of RMB300,000 may be imposed, according to Foreign Exchange Administration Rules* (外匯管理條例).

## RISKS RELATING TO THE SHARES AND GLOBAL OFFERING

### We will continue to be controlled by Mr Ke, whose interests may differ from those of our other Shareholders.

Immediately following the Global Offering, assuming the Over-allotment Option is not exercised, Mr Ke will own approximately 55% of our issued share capital and will remain our single largest shareholder. As our controlling shareholder, Mr Ke will be in a position to control the Company upon Listing and, subject to our Articles of Association and applicable laws and regulations, Mr Ke will be able to influence major policy decisions, including our overall strategic and investment decisions, as a result of his shareholdings, by:

- controlling the election of Directors which, in turn, allows for indirect control of the selection of senior management;
- determining the amount and timing of dividend payments;
- deciding on increases or decreases in share capital;
- determining the size and timing of any new securities issuances;
- approving annual budgets;
- approving mergers, acquisitions and disposals of our assets or businesses; and
- amending our Articles of Association.

The interests of Mr Ke could conflict with the interests of our other Shareholders. Mr Ke may take actions (including, for example, deciding on an excessively high rate of dividend distributions) which may not be in the best interests of our other shareholders or our business.

### Due to the time lag between pricing and trading of the Shares, there is a risk that the price of our Shares may fall before trading begins.

The Offer Price will be determined on the Price Determination Date, which is expected to be on or about 20 May 2010. However, trading of the Shares on the Stock Exchange will not commence until the Shares are delivered, which is expected to be on 26 May 2010. During this period, investors may not be able to sell or otherwise deal in the Shares. Accordingly, holders of the Shares are subject to the risk that the Shares' trading price could fall before trading begins as a result of adverse market conditions or other adverse developments that could occur between the time of the sale and the time trading begins.

**We may not pay any dividends on our Shares.**

Subject to the Companies Law, our Company may declare dividends in any currency to be paid to the Shareholders, but no dividend shall be declared in excess of the amount recommended by our Board of Directors. Our Articles of Association provide dividends may be declared and paid out of the profits of our Company, realised, or unrealised, or from any reserve set aside from profits which our Directors determine is no longer needed, or not in the same amount. Save as disclosed in "History and Corporate Structure", no dividend has been paid or declared by any entity within our Group since our incorporation. There is no assurance that we will declare dividends at all in the future. Future dividends, if any, will be at our Board of Directors' discretion and will depend on our future results of operations, capital requirements, financial condition, legal and contractual restrictions and other factors deemed relevant by the Board of Directors.

**There has been no previous public market for our Shares, and an active trading market may not develop.**

Prior to the completion of the Global Offering, there has been no public market for our Shares. The Offer Price will be determined by the Sole Sponsor and Sole Bookrunner (on behalf of the Underwriters) and us. The Offer Price may differ from the market price of our Shares after the Global Offering. We cannot give assurances that the Listing of our Shares on the Stock Exchange will result in the development of an active or liquid trading market for the Shares following the Global Offering or in the future or, if it does develop, that it will be sustained after the Listing or that the market price of our Shares will not decline below the Offer Price.

**Investors will experience immediate dilution and may experience further dilution in the value of their Shares.**

Because the Offer Price of our Shares is higher than the net tangible book value per Share of our Shares immediately prior to the Global Offering, purchasers of our Shares in the Global Offering will experience an immediate dilution in pro forma combined net tangible assets value to HK$1.42 per Share, based on the maximum Offer Price of HK$3.38, assuming that the Over-allotment Option is not exercised.

In addition, our Board of Directors approved our Share Option Scheme on 30 April 2010, particulars of which are summarised under the paragraph headed Share Option Scheme in Appendix VI to this prospectus. The maximum number of Shares in respect of which options may be granted under the Share Option Scheme is 100,000,000 Shares, which represents approximately 10% of the total number of our enlarged share capital upon completion of the Global Offering, assuming the Over-allotment Option is not exercised. Any exercise of the options granted under the Share Option Scheme will result in a dilution in the earnings per Share and net asset value per Share.

**The trading volume and share price of our Shares may fluctuate.**

The price and trading volume of our Shares may be highly volatile. Factors such as variations in our revenue, earnings and cash flow, changes in our pricing policy as a result of the presence of competitors, announcements of new technologies, strategic alliances or acquisitions, industrial or environmental accidents we may suffer, changes in our senior management personnel, changes in ratings by financial analysts and credit rating agencies, litigation, or fluctuations in the market prices for our products or raw materials could cause large and sudden changes in the volume and price at which our Shares will trade. In addition, the Stock Exchange and other securities markets have, from time to time, experienced significant price and volume fluctuations that are not related to the operating performance of any particular company. These fluctuations may also materially and adversely affect the market price of the Shares.

**Future sales, or perceived sales, of substantial amounts of our Shares in the public market could materially and adversely affect the prevailing market price of our Shares.**

Future sales by us or our Controlling Shareholder of substantial amounts of our Shares in the public markets after the Global Offering could adversely affect market prices prevailing from time to time. Please refer to "Underwriting — Underwriting Arrangements and Expenses — Other undertakings" in this prospectus for a more detailed discussion of the lock-up restrictions that will apply to us and our Controlling Shareholder immediately following the Global Offering.

After these restrictions lapse, the market price of our Shares may decline as a result of future sales of substantial amounts of our Shares or other securities convertible into our Shares in the public market, the issuance of new Shares or other securities convertible into our Shares, or the perception that such sales or issuances may occur. This could also materially and adversely affect our ability to raise capital in the future at a time and at a price we deem appropriate.

**Investors may face difficulties in protecting their interests because we are incorporated under Cayman Islands law, and Cayman Islands law may provide different remedies to minority shareholders when compared with the laws of Hong Kong and other jurisdictions.**

Our corporate affairs are governed by our Memorandum and Articles of Association and by the Companies Law and the common law of the Cayman Islands. The laws of the Cayman Islands relating to the protection of the interests of minority shareholders differ in some respects from those established under statutes or judicial precedents in Hong Kong, the United States and other jurisdictions. Such differences may mean that the remedies available to our minority Shareholders may be different from those under the laws of Hong Kong, the United States or other jurisdictions. Please refer to "Summary of the Constitution of our Company and Companies Law" in Appendix V to this prospectus.

**Investors should not place undue reliance on certain statistics, facts and other information contained in this prospectus with respect to the PRC, the PRC economy and the PRC paper industry derived from third party research reports.**

Certain statistics, facts and other information in this prospectus relating to the PRC, the PRC economy and the PRC paper industry are derived from various official government and/or other research agency sources that we believe to be appropriate sources for such information. The Sole Sponsor and the Directors have taken reasonable care in extracting and reproducing such information and statistics derived from official government publications and/or studies from other research agencies and have no reason to believe that such information is false or misleading. These facts and statistics from government and/or other research agencies have not been independently verified by the Company, the Sole Sponsor, the Sole Lead Manager, the Underwriters or any of their respective directors, affiliates or advisers and therefore, the Company makes no representation as to the accuracy of such facts and statistics from government and/or other research agencies, which may not be consistent with other information compiled within or outside the relevant jurisdiction and may not be complete or up-to-date. Due to possibly flawed or ineffective collection methods or discrepancies between published information and market practice and other problems, the facts and statistics from government and/or other research agencies contained herein may be inaccurate or may not be comparable from period to period or to statistics from government and/or other research agencies produced for other economies and should not be unduly relied upon. Further, there can be no assurance that they are stated or compiled on the same basis or with the same degree of accuracy as may be the case elsewhere. As such, prospective investors should consider carefully how much weight or importance they should attach to or place on such facts or statistics and should not place undue reliance on any of such information and statistics.

In preparation for the Listing, we have sought the following waivers from strict compliance with the relevant provisions of the Listing Rules and the Companies Ordinance:

## MANAGEMENT PRESENCE

Rule 8.12 of the Listing Rules requires that a new applicant applying for a primary listing on the Stock Exchange must have a sufficient management presence in Hong Kong. This normally means that at least two of its executive directors must be ordinarily resident in Hong Kong. Since the core business operations and manufacturing facilities of our Group are primarily located in the PRC, the executive Directors and senior management members of our Group are and will therefore continue to be based in the PRC. At present, other than Mr Wong Yat Sum, the chief financial officer and the company secretary of our Company, is ordinarily resident in Hong Kong and none of our executive Directors and senior management members of our Group is ordinarily resident in Hong Kong. We have applied to the Stock Exchange for a waiver from the strict compliance with the requirement under Rule 8.12.

We have received from the Stock Exchange a waiver from strict compliance with Rule 8.12 of the Listing Rules subject to the following conditions:

(a) the authorised representatives, Mr Wong Yat Sum and Mr Ke, will act as the principal channel of communication between the Stock Exchange and our Company and will be readily contactable by telephone, fax or email;

(b) both of the authorised representatives have means to contact all of our Directors promptly at all times as and when the Stock Exchange wishes to contact our Directors for any matters;

(c) all of our Directors who are not ordinarily resident in Hong Kong possess valid travel documents to visit Hong Kong and will be able to meet with the Stock Exchange within a reasonable period;

(d) our Company has appointed Somerley Limited pursuant to Rule 3A.19 of the Listing Rules to act as our compliance adviser, who will act as an additional channel of communication with the Stock Exchange from the Listing Date to the date when our Company distributes our annual reports to our Shareholders for the first full financial year immediately after Listing; and

(e) each of our Directors and the authorised representatives of our Company have provided their respective mobile phone numbers, office phone numbers, e-mail addresses and fax numbers to the Stock Exchange.

## DIRECTORS' RESPONSIBILITY FOR THE CONTENTS OF THIS PROSPECTUS

This prospectus includes particulars given in compliance with the Companies Ordinance, the Securities and Futures (Stock Market Listing) Rules and the Listing Rules for the purpose of giving information to the public with regard to our Group. Our Directors collectively and individually accept full responsibility for the accuracy of the information contained in this prospectus and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief, there are no other facts the omission of which would make any statement in this prospectus misleading.

## INFORMATION ABOUT THE GLOBAL OFFERING

The Global Offering comprises initially of 25,000,000 new Shares for the Hong Kong Public Offering and 225,000,000 new Shares for the International Offering (both subject to adjustments). The Offer Shares are offered solely on the basis of the information contained and representations made in this prospectus and the Application Forms and on the terms and subject to the conditions set out herein and therein. No person is authorised to give any information in connection with the Global Offering or to make any representation not contained in this prospectus, and any information or representation not contained herein must not be relied upon as having been authorised by us, the Sole Global Coordinator, the Sole Sponsor, the Sole Lead Manager, the Underwriters, any of our/their respective directors, agents, employees, advisers or any other party involved in the Global Offering.

Details of the structure of the Global Offering, including its conditions, are set out in "Structure of the Global Offering", and the procedures for applying for Hong Kong Offer Shares are set out in "How to Apply for Hong Kong Offer Shares" in this prospectus and in the relevant Application Forms.

## UNDERWRITING

This prospectus is published solely in connection with the Hong Kong Public Offering. For applicants under the Hong Kong Public Offering, this prospectus and the Application Forms contain the terms and conditions of the Hong Kong Public Offering.

The Listing is sponsored by the Sole Sponsor. Pursuant to the Hong Kong Underwriting Agreement, the Hong Kong Public Offering is fully underwritten by the Hong Kong Underwriters under the terms of the Hong Kong Underwriting Agreement and the Price Determination Agreement on the Price Determination Date, subject to the agreement on the Offer Price between the Sole Global Coordinator (on behalf of the Underwriters) and us on the Price Determination Date. The Global Offering is managed by the Sole Global Coordinator. The International Underwriting Agreement relating to the International Offering is expected to be entered into on or before 20 May 2010, subject to determination of the pricing of the Offer Shares. If for any reason, the Offer Price is not agreed among our Company, and the Sole Global Coordinator (on behalf of the Underwriters) by 26 May 2010, the Global Offering (including the Hong Kong Public Offering) will not proceed and will lapse. Details about the Underwriters and the underwriting arrangements are contained in the section headed "Underwriting" in this prospectus.

## DETERMINATION OF OFFER PRICE

The Offer Price is expected to be fixed by agreement between the Sole Global Coordinator (on behalf of the Underwriters) and our Company on the Price Determination Date. The Price Determination Date is expected to be on or before 20 May 2010 and, in any event, not later than 26 May 2010 (unless further extended at the sole discretion of the Sole Global Coordinator (on behalf of the Underwriters)). If, for whatever reason, the Offer Price is not agreed between the Sole Global Coordinator and our Company on the Price Determination Date, the Global Offering will not become unconditional and will lapse immediately. Further information about the Underwriters and the underwriting arrangements is set out in "Underwriting" in this prospectus.

## RESTRICTIONS ON OFFER AND SALE OF THE OFFER SHARES

Each person acquiring the Offer Shares will be required to, or be deemed by his/her acquisition of the Offer Shares to, confirm that he/she is aware of the restrictions on offers of the Offer Shares described in the prospectus. No action has been taken to permit an offering of the Offer Shares or the distribution of this prospectus in any jurisdiction other than in Hong Kong. Accordingly, this prospectus or the related Application Forms may not be used for the purpose of, and does not (and is not intended to) constitute an offer or invitation in any jurisdiction or in any circumstances in which such an offer or invitation is not authorised or to any person to whom it is unlawful to make such an offer or invitation. The distribution of this prospectus or the related Application Forms and the offering and sales of the Offer Shares in other jurisdictions may be restricted by law and therefore persons into whose possession this prospectus or any of the related Application Forms falls should inform themselves about, and observe any such restrictions. Any failure to comply with these restrictions may constitute a violation of applicable securities laws.

## APPLICATION FOR LISTING ON THE STOCK EXCHANGE

We have applied to the Listing Committee of the Stock Exchange for the listing of, and permission to deal in, the Shares in issue and to be issued as mentioned in this prospectus (including the Offer Shares and any additional Shares which may be issued pursuant to the Capitalisation Issue, Shares which may fall to be issued upon the exercise of the Over-allotment Option and any options that may be granted under the Share Option Scheme). Except as disclosed in this prospectus, no part of the share or loan capital of our Company is listed on or dealt in on any other stock exchange and no such listing of or permission to deal in its securities on any other stock exchange is being or proposed to be sought in the near future.

## HONG KONG SHARE REGISTER AND HONG KONG STAMP DUTY

All Offer Shares will be registered on our Company's register of members to be maintained in Hong Kong by the Hong Kong Share Registrar.

No stamp duty is payable by applicants in the Global Offering.

Dealings in the Shares registered in the register of members of our Company in Hong Kong will be subject to Hong Kong stamp duty. For further details about Hong Kong stamp duty, please seek professional tax advice.

Unless determined otherwise by our Company, dividends payable in Hong Kong dollars in respect of the Shares will be paid to the Shareholders listed on the register of members of our Company in Hong Kong, by ordinary post, at the Shareholders' risk, to the registered address of each Shareholder, or if joint Shareholders, to the first-named therein in accordance with the Articles of Association.

## PROFESSIONAL TAX ADVICE RECOMMENDED

Applicants for the Offer Shares are recommended to consult their professional advisers if they are in any doubt as to the taxation implications of holding and dealing in the Shares. It is emphasized that none of our Company, the Sole Sponsor, the Sole Global Coordinator, the Sole Lead Manager, the Underwriters, any of our/their respective directors, supervisors, agents or advisers or any other party involved in the Global Offering accepts responsibility for any tax effects or liabilities of holders of the Shares resulting from the subscription, purchase, holding or disposal of the Shares.

## OVER-ALLOTMENT AND STABILISATION

Stabilisation is a practice used by underwriters in some markets to facilitate the distribution of securities. To stabilise, the underwriters may bid for, or purchase, the newly issued securities in the secondary market, during a specified period of time, to retard, and if possible, prevent any decline in the market price of the securities below the offer price. In Hong Kong and certain other jurisdictions, the price at which stabilisation is effected is not permitted to exceed the offer price.

In connection with the Global Offering, the Sole Global Coordinator, as stabilising manager, or any person acting for it may over-allocate or effect any other transactions with a view to stabilising or maintaining the market price of the Offer Shares at a level higher than that which might otherwise prevail in the open market for a limited period after the Listing Date. Such market purchases of Offer Shares will be effected in compliance with all applicable laws and regulatory requirements. However, there is no obligation on the stabilising manager or any person acting for it to conduct any such stabilising activity, which if commenced, will be done at the absolute discretion of the stabilising manager and may be discontinued at any time. Any such stabilising activity is required to be brought to an end on the 30th day after the last day for the lodging of applications under the Hong Kong Public Offering. The number of the Shares that may be over-allocated will not be greater than the number of Shares which may be issued and sold upon exercise of the Over-allotment Option, being 37,500,000 Shares, which is approximately 15% of the Shares initially available under the Global Offering.

As a result of effecting transactions to stabilise or maintain the market price of the Shares, the Sole Global Coordinator, or any person acting for it, may maintain a long position in the Shares. The size of the long position, and the period for which the stabilising manager, or any person acting for them, will maintain the long position is at the discretion of the stabilising manager and is uncertain. Investors should be warned that, in the event that the stabilising manager liquidates this long position by making sales in the open market, this may lead to a decline in the market price of the Shares.

Stabilising action by the stabilising manager, or any person acting for it, is not permitted to support the price of the shares for longer than the stabilising period, which begins on the day on which trading of our Shares commences on the Stock Exchange and ends on the 30th day after the last day for the lodging of applications under the Hong Kong Public Offering. The stabilising period is expected to end on 18 June 2010. As a result, demand for the Shares, and their market price, may fall after the end of the stabilising period. A public announcement will be made within seven days after the end of the stabilising period in accordance with the Securities and Futures (Price Stabilising) Rules.

Any stabilising action taken by the stabilising manager, or any person acting for them, may not necessarily result in the market price of the Offer Shares staying at or above the Offer Price either during or after the stabilising period. Stabilising bids for or market purchases of the Offer Shares by the stabilising manager, or any person acting for them, may be made at or below the Offer Price and can therefore be made at or below the price paid for the Offer Shares by applicants for, or investors in, the Offer Shares.

## PROCEDURE FOR APPLICATION FOR HONG KONG OFFER SHARES

The procedures for applying for Offer Shares are set out in "How to Apply for Hong Kong Offer Shares" in this prospectus and on the relevant Applications Forms.

## STRUCTURE OF THE GLOBAL OFFERING

Details of the structure of the Global Offering including its conditions, and the Over-allotment Option, are set out in "Structure of the Global Offering" in this prospectus.

## LANGUAGE

If there is any inconsistency between this prospectus and the Chinese translation of this prospectus, this prospectus shall prevail. Translated English names of Chinese laws and regulations, governmental authorities, institutions, natural persons or other entities included in this prospectus and for which no official English translation exists are unofficial translations for your reference only.

## ROUNDING

Any discrepancies in any table in this prospectus between totals and sums of amounts listed therein are due to rounding.

## SHARES WILL BE ELIGIBLE FOR ADMISSION INTO CCASS

Subject to the granting of the listing of, and permission to deal in, the Shares on the Stock Exchange and the Company's compliance with the stock admission requirements of HKSCC, the Shares will be accepted as eligible securities by HKSCC for deposit, clearance and settlement in CCASS with effect from the Listing Date or on any other date as determined by HKSCC. Settlement of transaction between participants of the Stock Exchange is required to take place in CCASS on the second Business Day after any trading day. All activities under CCASS are subject to the General Rules of CCASS and CCASS Operational Procedures in effect from time to time.

All necessary arrangements have been made for the Shares to be admitted into CCASS. Investors should seek the advice of their stockbroker or other professional advisor for details of those settlement arrangements and how such arrangements will affect their rights and interests.

## DIRECTORS

| Name | Address | Nationality |
|---|---|---|
| *Executive Directors* | | |
| Mr Ke Wentuo (柯文托) | 277 Haibin Street, Xibin Town, Jinjiang, Fujian, the PRC | Chinese |
| Mr Ke Jixiong (柯吉熊) | 277 Haibin Street, Xibin Town, Jinjiang, Fujian, the PRC | Chinese |
| Mr Cao Xu (曹旭) | No. 59, 6th Floor, Unit 5, Building 242, Heping Road, Tiedong District, Anshan, Liaoning, the PRC | Chinese |
| Mr Zhang Guoduan (張國端) | Room 503, Building 4, 62 Jiangsheng Road, Jinjiang, Fujian, the PRC | Chinese |
| *Non-executive Director* | | |
| Mr Paul Steven Wolansky | 35 Edgewood Drive, Greenwich, CT 06831, United States | American |
| *Independent non-executive Directors* | | |
| Prof. Zhang Daopei (張道沛) | Room 202 No. 362 Wusi Road, Fuzhou, Fujian, the PRC | Chinese |
| Prof. Chen Lihui (陳禮輝) | Room 603, Block 1, High School Residential Area, 12 Xijiangbing Avenue, Gulou District, Fuzhou, Fujian, the PRC | Chinese |
| Mr Chow Kwok Wai (周國偉) | Flat C, 27/F., Tower 3, Hillsborough Court 18 Old Peak Road Mid-level Hong Kong | Chinese |

## PARTIES INVOLVED IN THE GLOBAL OFFERING

| | |
|---|---|
| **Sole Global Coordinator, Bookrunner, Lead Manager and Sponsor** | The Hongkong and Shanghai Banking Corporation Limited<br>HSBC Main Building<br>1 Queen's Road Central<br>Hong Kong |
| **Auditors and Reporting Accountants** | Deloitte Touche Tohmatsu<br>*Certified Public Accountants*<br>35/F, One Pacific Place<br>88 Queensway<br>Hong Kong |
| **Our Legal Advisors** | *As to Hong Kong and US laws:*<br><br>Orrick, Herrington & Sutcliffe<br>43rd Floor, Gloucester Tower<br>The Landmark<br>15 Queen's Road Central<br>Hong Kong<br><br>*As to PRC law:*<br><br>King & Wood<br>28th Floor, Huai Hai Plaza<br>1045 Huai Hai Road<br>Shanghai 200031<br>PRC<br><br>*As to Cayman Islands law:*<br><br>Conyers Dill & Pearman<br>Cricket Square<br>Hutchins Drive<br>P.O. Box 2681<br>Grand Cayman KY1-1111<br>Cayman Islands |

| | |
|---|---|
| **Legal Advisors to the Sole Sponsor and the Underwriters** | *As to Hong Kong and US laws:*<br><br>Norton Rose Hong Kong<br>38/F Jardine House<br>1 Connaught Place<br>Central<br>Hong Kong<br><br>*As to PRC law:*<br><br>Commerce & Finance Law Offices<br>6F NCI Tower<br>A12 Jianguomenwai Avenue<br>Chaoyang District<br>Beijing 100022<br>PRC |
| **Property Valuer** | Jones Lang LaSalle Sallmanns Limited<br>17/F Dorset House, Taikoo Place<br>979 King's Road<br>Quarry Bay<br>Hong Kong |
| **Receiving Banker** | The Hongkong and Shanghai Banking Corporation Limited<br>HSBC Main Building<br>1 Queen's Road Central<br>Hong Kong |

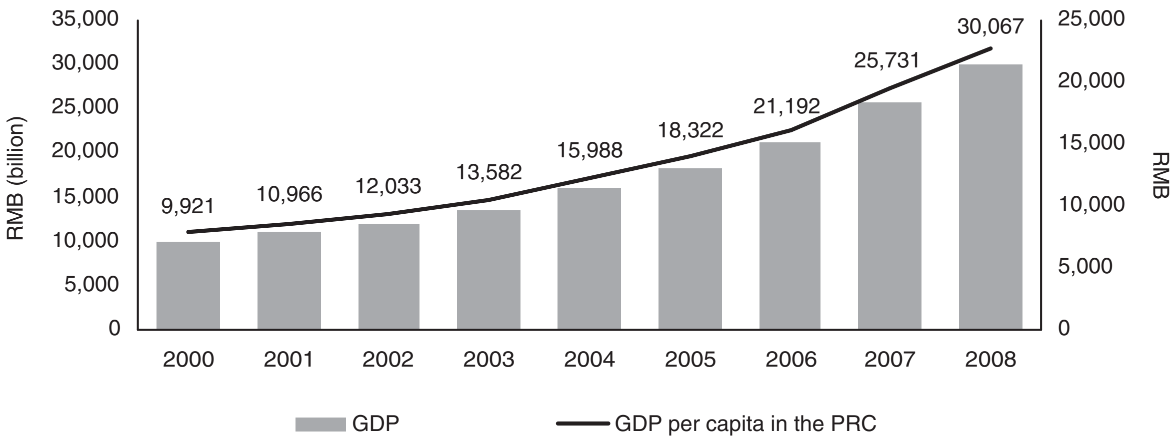
| | |
|---|---|
| **Registered office** | Cricket Square, Hutchins Drive<br>PO Box 2681<br>Grand Cayman, KY1-1111<br>Cayman Islands |
| **Headquarters in the PRC** | Xibin Industrial Zone<br>Jinjiang City<br>Fujian Province<br>The People's Republic of China |
| **Principal place of business in Hong Kong** | Unit 04, 13/F.,<br>Bank of America Tower<br>No. 12 Harcourt Road<br>Hong Kong |
| **Company's website** | www.youyuan.com.hk<br>*(information contained in this website does not form part of the prospectus)* |
| **Company secretary** | Mr Wong Yat Sum, *ACCA, HKICPA* |
| **Authorised representatives** | Mr Ke Wentuo<br>277 Haibin Street, Xibin Town,<br>Jinjiang, Fujian, the PRC |
| | Mr Wong Yat Sum<br>Block C Rear<br>2/F., 60 Castle Peak Road<br>Kowloon<br>Hong Kong |
| **Audit committee** | Mr Chow Kwok Wai (Chairman)<br>Mr Zhang Daopei<br>Mr Chen Lihui |
| **Remuneration committee** | Mr Ke Wentuo (Chairman)<br>Mr Zhang Daopei<br>Mr Chen Lihui |
| **Compliance adviser** | Somerley Limited<br>10th Floor, The Hong Kong Club Building<br>3A Chater Road<br>Central<br>Hong Kong |

| | |
|---|---|
| **Principal bankers** | Bank of China<br>Quanzhou Branch<br>Bank of China Building<br>Fengze Street<br>Quanzhou, Fujian<br>the PRC |
| | China Merchants Bank<br>Quanzhou Branch<br>Floor 14, Huixing Building<br>Fengze Street<br>Quanzhou, Fujian<br>the PRC |
| | China CITIC Bank<br>Quanzhou Branch<br>Floors 1-2, PBOC Building<br>Fengze Street<br>Quanzhou, Fujian<br>the PRC |
| **Cayman Islands principal share registrar and transfer office** | Butterfield Fulcrum Group (Cayman) Limited<br>Butterfield House<br>68 Fort Street<br>P.O. Box 609<br>Grand Cayman KY1-1107<br>Cayman Islands |
| **Hong Kong Share Registrar** | Computershare Hong Kong Investor Services Limited<br>Shops 1712-1716, 17th Floor<br>Hopewell Centre,<br>183 Queen's Road East<br>Wanchai<br>Hong Kong |

*The information provided in this section is derived from various government and/or private publications. Certain information and statistics in this section were extracted from a commissioned report issued by the China Paper Association in May 2010. We purchased the commissioned report for RMB100,000. The China Paper Association is a non-governmental entity founded in 1992. Its main functions include collecting and analysing information pertaining to the PRC paper and paperboard industry and publishing industry reports and statistics. Its members, who are industry organisations both in the PRC and abroad, are obligated to actively provide production and technology information to keep the China Paper Association abreast of industry developments. The China Paper Association also routinely provides information, including its annual publication of PRC paper industry report, and conducts research on the paper and pulp industry for the PRC government and private business entities. It also participates in industry development planning and advises on industry regulation, by supplying industry statistics to the PRC government, such as the NDRC, for formulation and revision of industry standards. The Company is of the view that the China Paper Association is an authoritative source of data pertaining to the PRC paper industry. We also extracted information from the website of the China Paper Association, which is publicly available. Our Directors believe that the sources of this information are appropriate sources for such information and have taken reasonable care in extracting and reproducing such information. Our Directors have no reason to believe that such information is false or misleading or that any fact has been omitted that would render such information false or misleading. The information derived from such sources has not been prepared or independently verified by our Company, the Sole Sponsor, the Sole Lead Manager or the Underwriters or any of their respective affiliates and advisers. No representation is given as to its accuracy.*

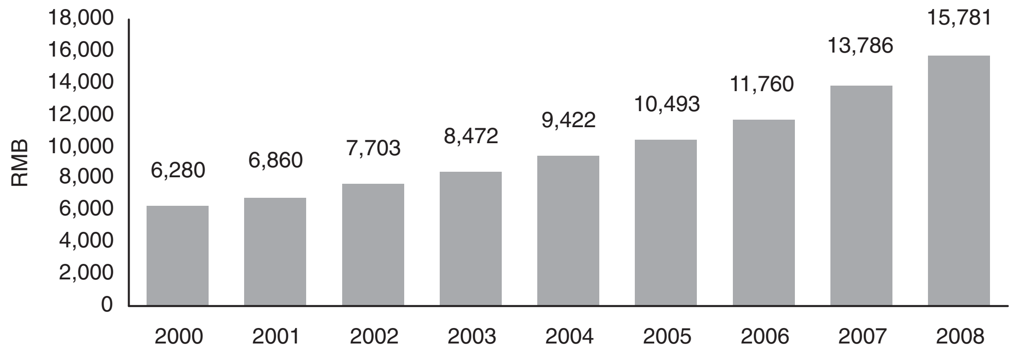
## THE PRC ECONOMY

The PRC economy has enjoyed continuous and rapid growth since 2000. According to the National Bureau of Statistics of China, the PRC nominal gross domestic product ("GDP") reached approximately RMB30 trillion in 2008, registering a CAGR of approximately 14.9% from 2000 to 2008. The table below shows the growth of nominal GDP and GDP per capita in the PRC from 2000 to 2008.



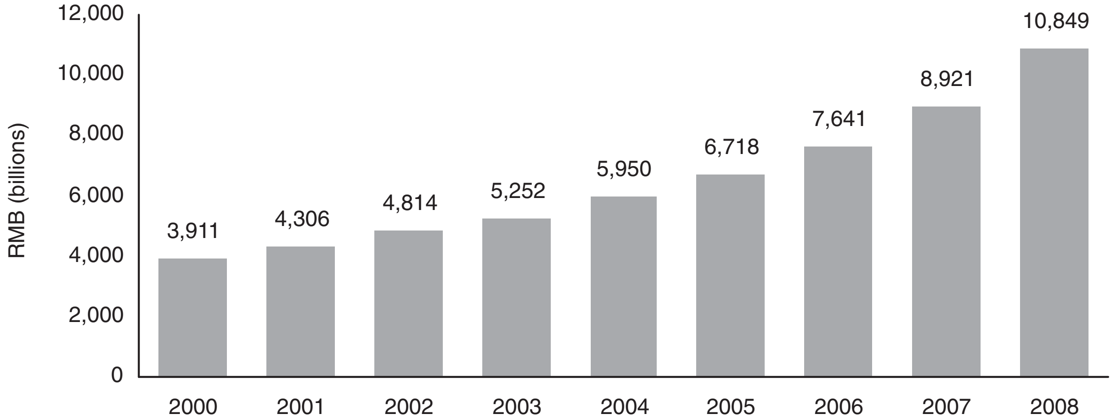

*Source: National Bureau of Statistics of China, October 2009*

With the rapid economic growth, the climbing GDP per capita, and the improved standard of living and purchasing power of average PRC consumers, the average national income has shown a significant increase. The annual disposable income per capita for urban households expanded from RMB6,280 in 2000 to RMB15,781 in 2008, representing a CAGR of approximately 12.2%. The table below shows the growth of annual disposable income per capita for urban households from 2000 to 2008.




*Source: National Bureau of Statistics of China, October 2009*

The rising per capita income and a strong consumer base have put the PRC on course to become the world's largest consumer market. According to the National Bureau of Statistics of China, the total retail sales of consumer goods grew at a CAGR of approximately 13.6% from 2000 to 2008. The table below shows the growth of total retail sales of consumer goods in the PRC from 2000 to 2008.




*Source: National Bureau of Statistics of China, October 2009*

During the same period, the PRC has also become the world's leading manufacturer and exporter. The development of the PRC paper industry correlates with the growth in domestic retail and export sales, especially the wrapping tissue paper market.

## OVERVIEW OF THE GLOBAL PAPER AND PAPERBOARD INDUSTRY

Global paper demand reached approximately 390.9 million tonnes in 2008 with production concentrated in Asia, Europe and North America. According to the China Paper Association, an organisation that provides research information pertaining to the PRC pulp and paper industry to the PRC government and its papermaking enterprise members, the United States, the PRC and Japan were the three leading paper producers and consumers in 2008. The production and consumption of paper by the three countries in 2008 are set out below:

| Rank | Country | Production | 2007-2008 | Consumption | 2007-2008 |
|---|---|---|---|---|---|
| | | (tonnes) | (% change) | (tonnes) | (% change) |
| 1 | United States | 80.0 million | -4.0 | 81.7 million | -6.8 |
| 2 | PRC | 79.8 million | 8.6 | 79.4 million | 8.9 |
| 3 | Japan | 30.6 million | -2.1 | 30.7 million | -2.6 |

*Source: China Paper Association, May 2010*

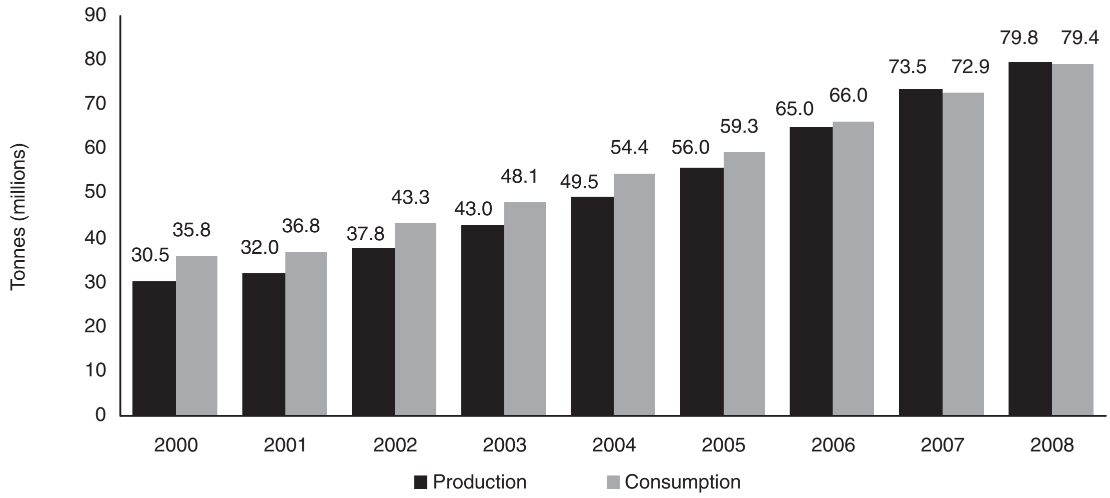
Per capita consumption of paper in the United States, the PRC and Japan was 266 kilogrammes, 60 kilogrammes and 242 kilogrammes, respectively. The PRC was the only country demonstrating continuous growth in 2008 in terms of both production and consumption.

## OVERVIEW OF THE PRC PAPER AND PAPERBOARD INDUSTRY

### Growth of the PRC Paper and Paperboard Industry

The PRC paper and paperboard industry grew at a rapid pace from 2000 to 2008. According to the China Paper Association, the output of paper and paperboard grew at a CAGR of approximately 12.8% while consumption increased at a CAGR of approximately 10.5%. Total output was 79.8 million tonnes in 2008, up approximately 8.6% from 73.50 million tonnes in 2007. Total domestic consumption was approximately 79.4 million tonnes in 2008, up approximately 8.9% from 72.9 million tonnes in 2007.

Calculated based on a population of 1.3 billion, paper consumption was about 60 kilogrammes per capita in 2008, up 5 kilogrammes from a year before. The China Paper Association estimates that the demand for paper products in the PRC will continue to grow in the next few years. The table below shows the growth of paper production and consumption in the PRC from 2000 to 2008.

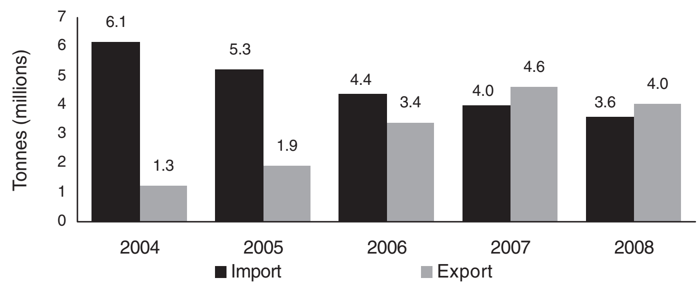



*Source: China Paper Association, April 2009*

According to the China Paper Association, total industry output value for paper and paperboard products has reached RMB457.1 billion in 2008, up approximately 21.5% compared to 2007 and total sales revenue for a total of 3,494 paper and paperboard enterprises has reached RMB433.0 billion, up approximately 18.0% compared to 2007.

**Import and Export of PRC Paper and Paperboard**

The general trend in the PRC Paper and paperboard industry is to consistently decrease imported paper volumes and increase paper exports, even though the export volume was lower in 2008, compared to 2007, due to the impact of global financial crisis. In 2008, the PRC imported approximately 3.6 million tonnes and exported approximately 4.0 million tonnes of paper and paperboard, representing approximately 4.5% and 5.0% of total paper and paperboard consumption and production, respectively. The chart below sets forth the imports and exports of paper and paperboard products in the PRC from 2004 to 2008.




*Source: China Paper Association, April 2009*

### Major Paper and Paperboard Manufacturing Provinces

In 2008, there were 13 provinces in the PRC with annual paper and paperboard output exceeding one million tonnes, which in aggregate accounted for approximately 91.6% of the PRC total output during the same year. The following table sets forth the production of paper and paperboard for each of the aforementioned 13 provinces from 2006 to 2008.

| | 2006 | 2007 | 2008 | 2006-2008 CAGR |
|---|---|---|---|---|
| | (in thousands of tonnes) | | | |
| Shandong Province | 12,726 | 14,063 | 15,269 | 10% |
| Zhejiang Province | 10,228 | 12,186 | 12,828 | 12% |
| Guangdong Province | 9,344 | 9,302 | 11,540 | 11% |
| Henan Province | 8,225 | 9,397 | 9,890 | 10% |
| Jiangsu Province | 7,838 | 9,750 | 9,843 | 12% |
| Hebei Province | 3,896 | 4,749 | 3,787 | -1% |
| Fujian Province | 2,014 | 2,379 | 2,965 | 21% |
| Hunan Province | 2,170 | 2,241 | 2,805 | 14% |
| Sichuan Province | 1,479 | 1,907 | 2,112 | 19% |
| Anhui Province | 1,250 | 1,413 | 1,851 | 22% |
| Guangxi Zhuang Autonomous Region | 1,180 | 1,344 | 1,497 | 13% |
| Hubei Province | 1,170 | 1,222 | 1,322 | 6% |
| Jiangxi Province | 937 | 1,109 | 1,137 | 10% |

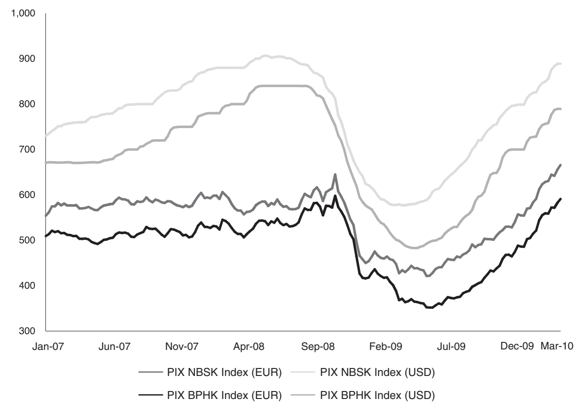
*Source: National Bureau of Statistics of China, October 2009*

### Raw Materials

Pulp is the main raw material for paper production. According to the China Paper Association, pulp consumption in the PRC hit approximately 73.6 million tonnes in 2008, representing an increase of approximately 8.7% over 2007, of which wood pulp and recycled pulp (made from recovered paper) each accounted for approximately 22% and approximately 60%, respectively, of the total pulp consumption.

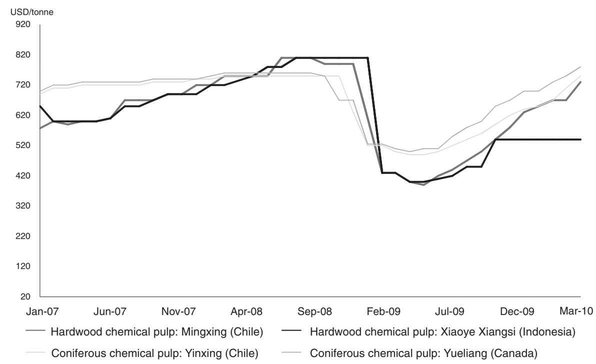
On the supply side, the PRC still relies heavily on imported raw materials for paper production. In 2008, approximately 58.6% and 43.6% of the respective total PRC wood pulp and recycled pulp consumptions were sourced from overseas. The charts below provide selective benchmark prices for wood pulp and recovered paper in both the PRC and international markets from January 2007 to March 2010.[1,2] The charts show that the prices for both wood pulp and recovered paper in the PRC and international markets followed an upward trend through 2007, then fell significantly during the fourth quarter of 2008 and first half of 2009 due to global financial crisis. The prices began to recover since the second half of 2009.

**PIX Pulp Benchmark Indexes — Europe (weekly)**



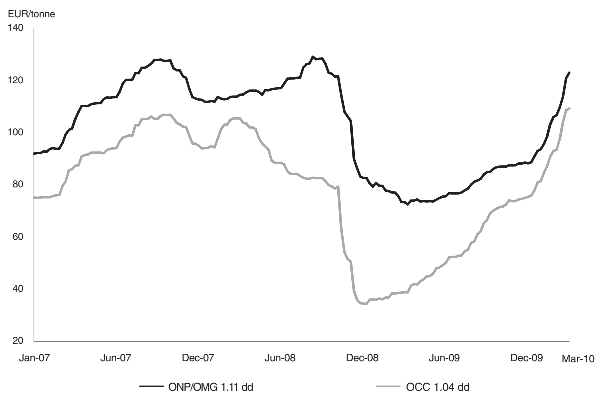

*Sources:* *Bloomberg, northern bleached softwood kraft pulp (NBSK) price and bleached hardwood kraft pulp (BHKP) price, May 2010*

**PRC Wood Pulp Import Price Trend (monthly)**



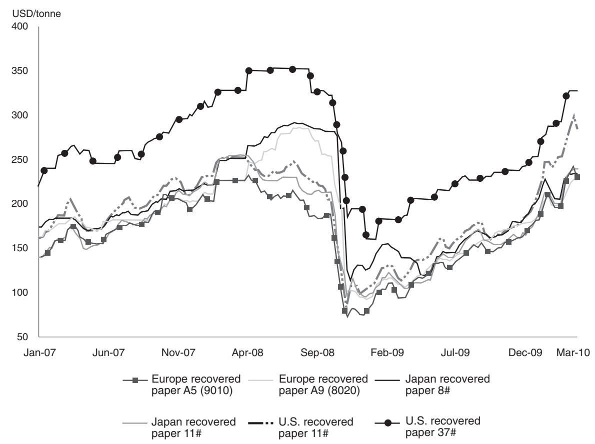

*Sources:* *Wind [3], hardwood chemical pulp prices under the brands of Mingxing* (明星) and Xiaoye Xiangsi* (小葉相思), coniferous chemical pulp prices quoted by Yinxing* (銀星) and Yueliang* (月亮), May 2010*

**PIX Recovered Paper Indexes — Europe (weekly)**




*Sources:* *Bloomberg, old corrugated containers (OCC) 1.04dd price and old newspapers and magazines (ONP/OMG) 1.11dd price, May 2010*

**PRC Recovered Paper Import Price Trend (Weekly)**




*Source:* *Wind, prices quoted for Europe recovered paper A5 (9010), Europe recovered paper A9 (8020), Japan recovered paper 8#, Japan recovered paper 11#, U.S. recovered paper 11#, U.S. recovered paper 37#, May 2010*

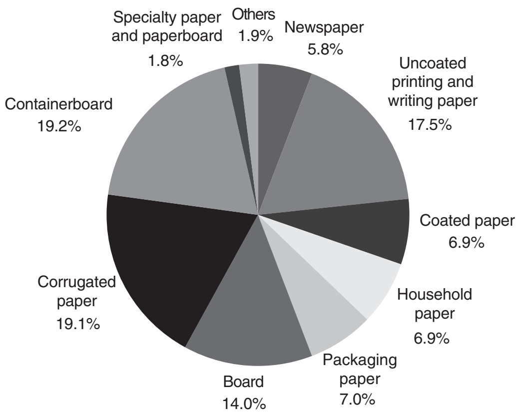
[1] The charts are produced based on the information obtained by the Sole Sponsor from Bloomberg and Wind with their consent. The Sole Sponsor is a usual subscriber of Bloomberg and Wind and apart from the usual subscription payable by the Sole Sponsor, neither the Sole Sponsor or the Company has paid any commission to Bloomberg or Wind for such information.

[2] Because the prices for wood pulp and recovered paper vary depending on factors such as sources and quality, the data presented in this section are not indicative of our Company's actual raw material costs. However, the Directors believe that the various prices presented in the chart titled PRC Wood Pulp Import Price Trend (monthly) and the U.S recovered paper 37# price presented in the chart entitled PRC Recovered Paper Import Price Trend (Weekly) have some reference value on the raw materials prices paid by the Company as some of the wood pulp and recovered paper we use is of the same or similar types as presented in the charts. For information with respect to our Company's raw material costs, please refer to "Management's Discussion and Analysis of Financial Condition and Results of Operations — Factors Affecting Results of Operations — Cost of Wood Pulp, Reclaimed Pulp, De-inked Pulp and Recycled White Paper" in this prospectus.

[3] Wind is a provider of the PRC financial data headquartered in Shanghai, the PRC. Its clients include large PRC and international financial institutions. Its data is often quoted by Chinese and English media, research reports, and academic publications.

### Segmentation of the PRC Paper and Paperboard Industry

According to the China Paper Association, paper and paperboard products can be categorised into nine main categories based on their different usage and production techniques, newsprint, uncoated printing and writing paper, coated paper, household paper, packaging paper, board, corrugated paper, containerboard, and specialty paper and paperboard. The chart below shows the breakdown of the PRC paper and paperboard production by different paper categories in 2008.

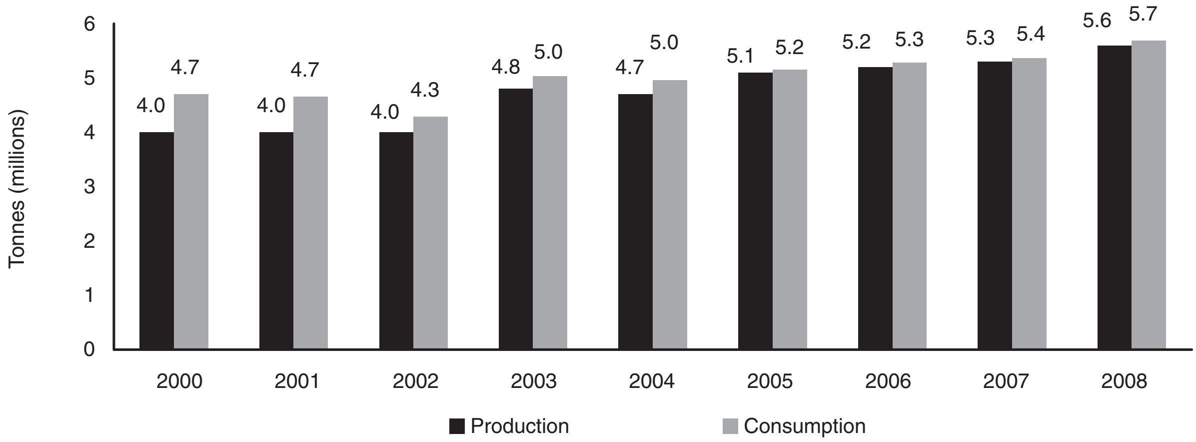



*Source: China Paper Association, April 2009*

## OVERVIEW OF THE PRC PACKAGING PAPER MARKET

Packaging paper is one segment of the paper and paperboard industry. In 2008, the PRC produced approximately 5.6 million tonnes and consumed approximately 5.7 million tonnes of packaging paper, which accounted for approximately 7.0% and approximately 7.2%, respectively, of the aggregate PRC paper and paperboard production and consumption. Along with the economic growth in the PRC, production and consumption of packaging paper have steadily increased over the last few years. In 2008, production of packaging paper grew approximately 5.7% and consumption grew approximately 6.0%, respectively, compared to 2007.

The following table shows the PRC production and consumption of packaging paper from 2000 to 2008.




*Source: China Paper Association, April 2009*

Presently, packaging paper products in the PRC are mainly produced and consumed domestically. According to the China Paper Association, in 2008, the PRC imported approximately 0.1 million tonnes of packaging paper, representing approximately 2.1% of the PRC's total packaging paper consumption, while the PRC exported approximately 0.03 million tonnes of packaging paper, representing approximately 0.5% of the PRC's total packaging paper production.

The market trend in packaging materials development is producing mid-to-high end, diversified and multi-coloured products. Compared with other packaging materials such as plastics, wood, metal and glass, paper-based packaging materials offer advantages in terms of cost and production efficiency and comport better with increasingly stringent environmental regulations.

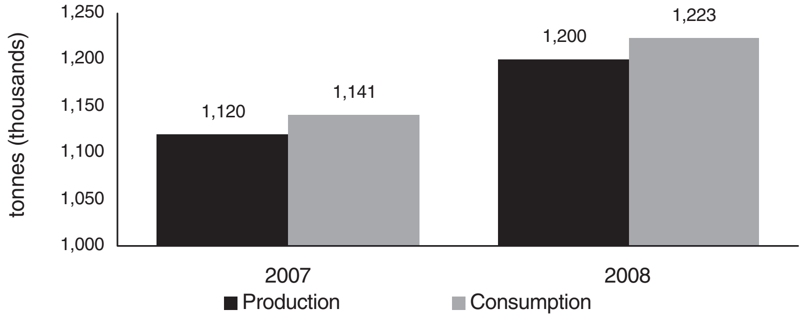
## OVERVIEW OF THE PRC WRAPPING TISSUE PAPER MARKET

### Growth of Wrapping Tissue Paper Market in the PRC

Wrapping tissue paper is a type of tissue paper which forms a sub-category of packaging paper. It accounts for approximately 21.4% of the total packaging paper production volume in 2008. Wrapping tissue paper products usually have grammage of less than $40g/m^2$ and are much lighter than most types of paper and paperboard product. As a result, wrapping tissue paper represents a relatively smaller share of total paper and paperboard market in terms of its output weight. Wrapping tissue paper is commonly used to package clothing, footwear, fruit, alcohol bottles, books, glass or ceramic items, toys, holiday gifts and other consumer goods.

The sustainable economic development over the past few years in the PRC has improved the living standards of PRC consumers, whose increased attention to product packaging has fueled the demand for wrapping tissue paper due to its aesthetic appeal and ability to highlight a product's quality and visual appeal. As wrapping tissue paper has increasingly become the ideal packaging option for many consumer goods, its growth potential also has expanded.

According to the China Paper Association, the global production of wrapping tissue paper reached approximately 8 million tonnes in 2008 and the PRC accounted for approximately 15% of the world's total production, or approximately 1.2 million tonnes, representing an increase of approximately 7.1% over 2007. During the same year, the PRC consumed approximately 1.2 million tonnes of wrapping tissue paper, representing an increase of approximately 7.2% over 2007. The following chart sets forth the PRC's production and consumption of wrapping tissue paper in 2007 and 2008.

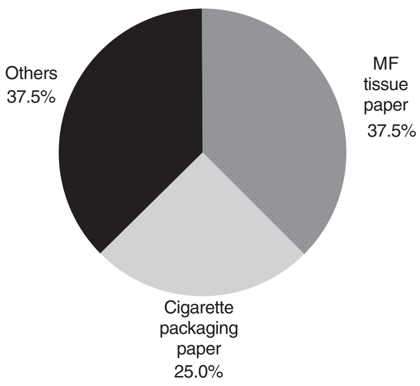



*Source: China Paper Association, May 2010*

According to the statistics issued by the National Bureau of Statistics of China and the General Administration of Customs, as well as analysis conducted by the China Paper Association, packaging paper in the PRC has maintained a growth rate of 2% to 5% in recent years, while wrapping tissue paper has maintained a growth rate of approximately 8% per annum. In the future, growing environmental awareness among consumers and increased restrictions against the use of plastic packaging material are expected to promote the use of wrapping tissue paper as the packaging material for many types of merchandise and further facilitate the growth of wrapping tissue paper consumption, and therefore, according to the China Paper Association, the market for wrapping tissue paper is expected to grow continuously at a similar speed.

**Categories of Wrapping Tissue Paper**

There are two main categories of wrapping tissue paper: MF tissue paper that are mainly used to package general consumer goods, and cigarette packaging paper including cigarette paper, filter tip paper, cigar wrapping paper, and other types of wrapping paper that more specifically cater to cigarette packaging. The two categories, in aggregate, represent more than 60% of the total wrapping tissue paper production, with the remainder consisting of rust inhibiting paper, grease proof paper, cellophane, tea bag filter paper, ultrafine parchment paper, crepe paper and stripe kraft paper. In 2008, the PRC produced approximately 450 thousand tonnes and approximately 300 thousand tonnes of MF tissue paper and cigarette paper, respectively. The following chart shows 2008 production breakdown of wrapping tissue paper in terms of production output.




*Source: China Paper Association, May 2010*

**Competition Landscape of PRC Wrapping Tissue Paper Industry**

Presently, wrapping tissue paper products in the PRC are manufactured mainly domestically. According to the China Paper Association, the PRC imported approximately 42 thousand tonnes of wrapping tissue paper in 2008, representing approximately only 3.4% of the total wrapping tissue paper consumption in the PRC. During the same year, exports of wrapping tissue paper amounted to approximately 19 thousand tonnes, representing approximately only 1.6% of the total domestic production. Because the import and export volumes of wrapping tissue paper are relatively low in the PRC, which our Directors believe is mainly attributed to the expensive cost of transporting paper products, the domestic wrapping tissue paper market encounters less competition from overseas manufacturers. The China Paper Association expects export volumes to rise, as PRC wrapping tissue paper production continues to grow.

Data compiled by the China Paper Association on domestic production output by the leading PRC wrapping tissue paper manufacturers in 2008 suggests that competition within the wrapping tissue market is characterised by a limited number of large players. The increasing demand from both domestic and overseas markets, the continuous improvement of production machines and technology and the higher profit margin of wrapping tissue paper business have facilitated the growth of the wrapping tissue paper industry in the PRC.

*MF tissue paper*

In 2008, only two MF tissue paper manufacturers, including our Group, had production output that exceeded 60 thousand tonnes, and the ten leading manufacturers together accounted for 43% of total MF tissue paper production in the PRC. The leading two MF tissue paper manufacturers differentiate themselves from other market players in terms of production technology and capacity. The table below shows the major MF tissue paper manufacturers as ranked by the China Paper Association based on their production output in 2008. All ten MF tissue paper manufacturers are subject to the Paper Making Industry Development Policy.

| Rank | Paper Manufacturer | Product | 2008 Production |
|---|---|---|---|
| 1 | Our Group | MF tissue paper, including semi-transparent paper | 63,000 tonnes |
| 2 | Fujian Naoshan Paper* (福建鐃山紙業) | MF tissue paper, including semi-transparent paper | 60,000 tonnes |
| 3 | Guilin Qifeng Paper* (桂林奇峰紙業) | MF tissue paper, banknote paper | 21,000 tonnes |
| 4 | Hunan Qidu Paper* (湖南祁都紙業) | MF tissue paper, including semi-transparent paper | 11,000 tonnes |
| 5 | Shandong Linyi Dongda Paper* (山東臨沂東大紙業) | MF tissue paper | 9,000 tonnes |
| 6 | Hunan Dongjiang Paper* (湖南洞江紙業) | MF tissue paper, including semi-transparent paper | 8,000 tonnes |
| 7 | Hunan Shaoyang Paper* (湖南邵陽紙業) | MF tissue paper, including semi-transparent paper | 6,000 tonnes |
| 8 | Hunan Xianfeng Paper* (湖南先峰紙業) | MF tissue paper, including semi-transparent paper | 5,000 tonnes |
| 9 | Guangxi Hezhou Hongxing Paper* (廣西賀州紅星紙業) | MF tissue paper | 5,000 tonnes |
| 10 | Hunan Baichuan Paper* (湖南百川紙業) | MF tissue paper | 5,000 tonnes |
| | | Total | 193,000 tonnes |

*Source: China Paper Association, May 2010*

For the year ended 31 December 2008, our Group achieved approximately 14.0%, 5.3%, 1.1% and 0.1% market share by production output for the MF tissue paper segment, the wrapping tissue paper segment, the packaging paper segment and the paper and paperboard industry, respectively within the PRC, according to the China Paper Association.

*Cigarette packaging paper*

In 2008, there were only two cigarette packaging paper manufacturers with production output exceeding 50 thousand tonnes, and the eight leading manufacturers together accounted for approximately 63% of total cigarette packaging paper production in the PRC. The table below shows the major cigarette packaging paper manufacturers as ranked by the China Paper Association based on their production output in 2008.

| Rank | Paper Manufacturer | Product | 2008 Production |
|---|---|---|---|
| 1 | Mudanjiang Hengfeng Paper* (牡丹江恒豐紙業) | Cigarette paper, aluminum foil backing paper, cigarette filter rod | 56,000 tonnes |
| 2 | Jiaxing Minfeng Paper* (嘉興民豐特紙) | Cigarette paper, aluminum foil backing paper, cigarette filter rod | 52,000 tonnes |
| 3 | Hangzhou Huafeng Paper* （杭州華豐紙業） | Cigarette paper, cigarette filter rod | 35,000 tonnes |
| 4 | Yunnan Hongta Lanying Paper* (雲南紅塔蘭鷹紙業) | Cigarette paper, cigarette filter rod | 21,000 tonnes |
| 5 | Sichuan Jinfeng Paper* (四川錦豐紙業) | Cigarette paper, cigarette filter rod | 10,000 tonnes |
| 6 | Hunan Xiangfeng Paper* (湖南湘豐紙業) | Cigarette paper, cigarette filter rod | 10,000 tonnes |
| 7 | Henan Mifeng Paper* (河南密豐紙業) | Cigarette paper, cigarette filter rod | 2,000 tonnes |
| 8 | Anhui Jingfeng Paper* (安徽景豐紙業) | Cigarette paper | 3,000 tonnes |
| | | Total | 189,000 tonnes |

*Source: China Paper Association, May 2010*

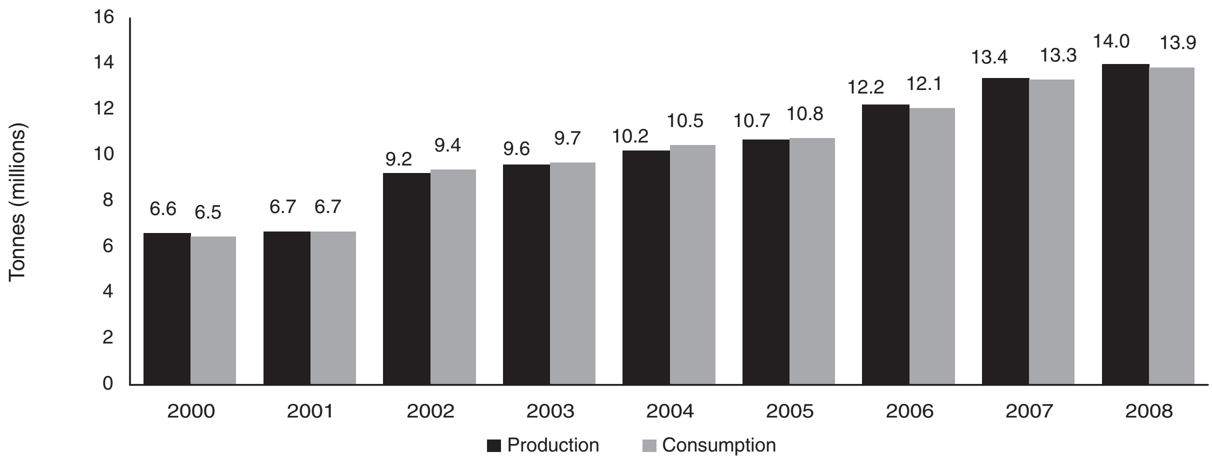
### Machines and Key Raw Materials used for Wrapping Tissue Paper Manufacturing

Given market demand for wrapping tissue paper often varies in terms of paper quality and intended function, the wrapping tissue paper market places more emphasis on product variety and less on the total production output. Therefore, the production scale of a wrapping paper machine is smaller compared to machines used for mass production of other paper products. The production technology employed by PRC wrapping tissue paper manufacturers are more or less in line with international standards, though greater differences exist with respect to the equipment used by PRC manufacturers to maintain production stability. According to the China Paper Association, the prevalent papermaking width in the international market for wrapping tissue paper machines is approximately 4 metres or less. In contrast, machines in the PRC produce approximately 3-metre wide paper or less. The more advanced machines in the PRC have a maximum design speed of 200 - 300 metres per minute. Most PRC paper manufacturers are equipped with machines that run below 100 metres per minute.

Most of the wrapping tissue paper manufacturers in the PRC purchase pulp from the market with only a few producing their own pulp. In recent years, some PRC manufacturers have begun to use de-inked pulp made from recovered paper in their production of wrapping tissue paper to reduce production costs and strengthen competitiveness.

## OVERVIEW OF THE PRC UNCOATED PRINTING AND WRITING PAPER MARKET (INCLUDING COPY PAPER)

The following table shows production and consumption growth of uncoated printing and writing paper, which demonstrates a CAGR of 9.9% and 9.9%, respectively, from 2000 to 2008.

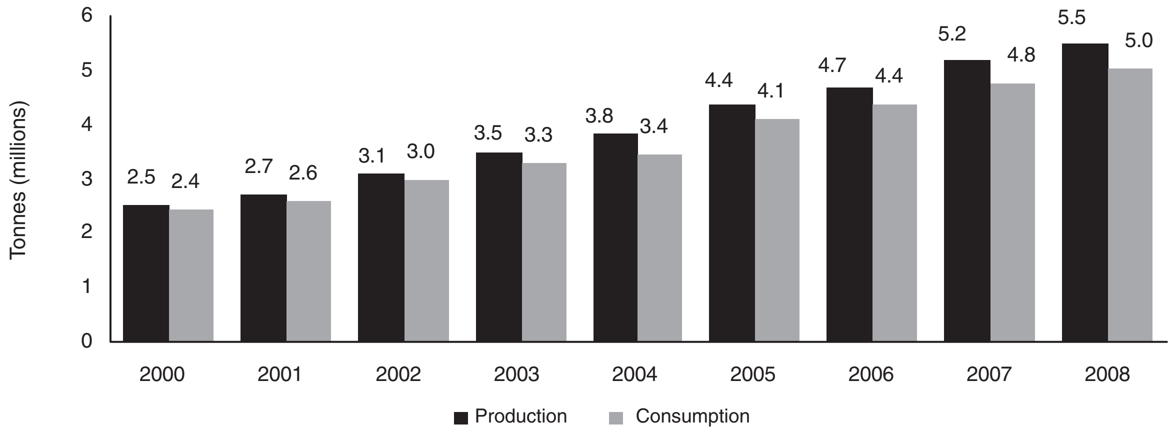



*Source: China Paper Association, April 2009*

According to the China Paper Association, the PRC imported approximately 390 thousand tonnes of uncoated printing and writing paper in 2008, representing approximately only 2.8% of the total consumption in the PRC. During the same year, exports of uncoated printing and writing paper amounted to approximately 540 thousand tonnes, representing approximately only 3.9% of the total domestic production.

*Overview of the PRC Household Paper Market (including paper towel)*

The following table shows production and consumption growth of household paper, which demonstrates a CAGR of 10.4% and 9.5%, respectively from 2000 to 2008.




*Source: China Paper Association, April 2009*

According to the China Paper Association, the PRC imported approximately 50 thousand tonnes of household paper in 2008, representing approximately only 1.0% of the total consumption in the PRC. During the same year, exports of household paper reached approximately 520 thousand tonnes, representing approximately 9.5% of the total domestic production.

**Regulations regarding the foreign investment in papermaking industry**

In order to regulate foreign investment in certain industries in the PRC, the PRC government promulgates the Catalogue of Industry Guidelines for Foreign Investment Industries* (外商投資產業指導目錄) from time to time. Over the past years, there have been several changes in the policies and regulations on foreign investment in the papermaking industry in the PRC.

On 31 October 2007, MOFCOM and the NDRC promulgated the Revised Guiding Catalogue of Industries for Foreign Investment* (外商投資產業指導目錄(2007)) (the "Revised Catalogue"), which became effective on 1 December 2007 and replaces the 2004 version of the Guiding Catalogue of Industries for Foreign Investment. According to the Revised Catalogue, foreign investment is encouraged in the construction of forest and paper integration project with annual chemical wood pulp production capacity of 300,000 tonnes or more for a single production line, and annual chemical mechanical wood pulp production capacity of 100,000 tonnes or more for a single production line and the simultaneous construction for the manufacture of high-grade paper and paperboards. However, foreign investment in this encouraged industry is only allowed in the form of equity joint ventures or co-operative joint ventures. Foreign investment in manufacture of rice paper is prohibited, while foreign investment in other paper manufacturing project is permitted.

According to the China's 11th Five-Year Plan, the following proposals have been made: "adjusting structure of materials of the paper making industry; reducing water consumption and pollutants emission; eliminating obsolete straw pulp production lines; implementing forest-paper integration in suitable regions". In light of the above proposals, the NDRC promulgated the "Paper Making Industry Development Policy* (造紙產業發展政策)" on 15 October 2007, in which the following policies are advocated: (1) using wood fibers and recovered paper as the major raw materials for paper manufacturing; (2) raising the utilisation rate and recycling rate of recovered paper; (3) reducing the number of small-scaled paper manufacturing enterprises; (4) introducing environmentally friendly technologies and skills in paper manufacturing enterprises to achieve the purpose of reducing pollutants; (5) using recovered paper to manufacture newsprint paper and wrapping paper. "Scale and environment" will be a major index for development of the paper making industry and will subsequently pose a considerable impact on the management and development of paper manufacturers.

**Law of the PRC on Wholly Foreign-owned Enterprises**

On 12 April 1986, 4th Meeting of the Sixth NPC adopted The Law of the PRC on Wholly Foreign-owned Enterprises* (中華人民共和國外資企業法) (the "Wholly Foreign-owned Enterprises Law"), and was amended on 31 October 2000 in accordance with the Decision on Modifying the Law of the People's Republic of China on Foreign-funded Enterprises adopted at 18th Meeting of the Standing Committee of the Ninth NPC on 31 October 2000.

*General*

Pursuant to the Wholly Foreign-owned Enterprises Law, "Wholly Foreign-owned Enterprises" (the "WFOE") refers to those enterprises established in the PRC, exclusively, by foreign investors, in accordance with the relevant PRC laws and regulations. The term does not include branches set up in the PRC by foreign enterprises and other foreign economic organisations.

A WFOE shall take the form of a limited liability company. It may also take other forms of organisation with approval. Where a wholly foreign-owned enterprise is a limited liability company, the foreign investors shall be liable to the enterprise within the limit of the capital subscribed by it. Where a WFOE takes other forms of organisation, the liability of the foreign investor to the enterprise shall be determined according to the PRC laws and regulations.

*Approval and Registration*

Pursuant to the Wholly Foreign-owned Enterprises Law, the application to incorporate a WFOE shall be submitted for examination and approval to the competent PRC foreign investment administrative authorities (the "Approval Authority") which shall within 90 days from the date of receiving such incorporation application, decide whether or not to grant the approval. After the application for incorporation of a WFOE has been approved, the foreign investor shall, within 30 days from the date of receiving a certificate of approval, apply to the AIC for registration and obtain a business license. The date of issuance of the business license shall be the date of the incorporation of the WFOE.

When a WFOE is split up, merged with others or has its registered capital changed due to other reasons, it shall apply to the Approval Authority for approval with a certificate of verification provided by an accountant registered in China. And then registration procedures for changes shall be followed at the competent AIC.

*Registered Capital*

Pursuant to the Wholly Foreign-owned Enterprises Law, the registered capital of a WFOE refers to the total amount of capital registered at the competent AIC when applying for the establishment of the enterprise, i.e. all the capital subscribed by the foreign investor and the registered capital of a WFOE shall be appropriate to its business scale, and the ratio between its registered capital and total amount of investment shall be in conformity with the relevant provisions of China.

Capital contribution

The time limit for a foreign investor to contribute the capital it subscribed shall be stipulated in the application for establishing the WFOE and the WFOE's articles of association. The foreign investor may contribute the capital by installments. However the last installment shall be paid within 3 years from the date of the issuance of the WFOE's business license. The first installment by a foreign investor shall be no less than 15% of the total amount of the capital it has subscribed and paid within 90 days from the date on which the WFOE's business license is issued.

If the foreign investor fails to make the first installment within the time limit described in the preceding paragraph, the approval certificate for the WFOE shall become invalid automatically, and the WFOE shall go through the procedures for cancellation of registration and hand in the business license for cancellation with the competent AIC, if not, the competent AIC will revoke the business license of the WFOE and announce it to the public. But such time limit on capital contribution can be extended subject to Approval Authority's consent.

Increase of registered capital

Pursuant to the Wholly Foreign-owned Enterprises Law, where a WFOE increases its registered capital, resolutions shall be passed by the authority of the company, i.e. the shareholders or the board of directors in accordance with the Articles of Association of such WFOE. After the resolution is passed, the WFOE shall submit an application regarding the increase in registered capital to the competent Approval Authority for examination and approval. Then, after obtaining the approval, the WFOE shall go through the procedures for alternation of registration with the competent AIC.

Reduction of registered capital

Pursuant to the Wholly Foreign-owned Enterprises Law, a wholly foreign-owned enterprise shall not reduce its registered capital during its term of operation. If however, it is really necessary for the WFOE to make such reduction due to some changes such as those in the total amount of investment or production scale, it may be reduced upon the approval by the Approval Authority. After obtaining the approval, the WFOE shall go through the procedures for alternation of registration with the competent AIC.

*Transfer of Shares*

Pursuant to the Wholly Foreign-owned Enterprises Law, any assignment of the registered capital of a WFOE shall be approved by the competent Approval Authority and go through the procedures for alternation of registration with the competent AIC.

*Profit distribution*

The Wholly Foreign-owned Enterprises Law provides that after payment of taxes, a WFOE must make contributions to a reserve fund, an employee bonus and welfare fund. The allocation ratio for the employee bonus and welfare fund may be determined by the WFOE. However, at least 10% of the after-tax profits must be allocated to the reserve fund. If the cumulative amount of allocated reserve funds reaches 50% of a WFOE's registered capital, the WFOE will not be required to make any additional contribution. The reserve fund may be used by a WFOE to make up its losses and with the consent of the Approval Authority, can also be used to increase its capital. The WFOE is prohibited from distributing dividends unless the losses (if any) of previous years have been made up. The employee bonus and welfare fund can only be used for the collective benefit and facilities of the employees of the WFOE.

*Term of Operation*

The term of operation of a WFOE shall be, according to its particular line of business and its concrete conditions, stipulated by the foreign investor in its application for establishing the enterprise, and approved by the Approval Authority. And the term of operation of a WFOE shall begin from the date on which the business license of the enterprise is issued. In case an extension for term of operation is required upon the expiration, a WFOE shall submit an application for extension of the term to the Approval Authority 180 days before the expiration. Upon the approval of extension of the term, the WFOE shall go through procedures for the alteration of registration with the competent AIC.

*Amendment of articles of association*

Any amendments to the articles of association must be made in accordance with the procedures set forth in applicable laws, regulations and the articles of association. Any amendment of provisions incorporated in the articles of association will only be effective after approved by the Approval Authority. After the amendment to the articles of association is approved, the WFOE shall file the newly adopted articles of association with the competent AIC.

*Termination and liquidation*

A WFOE shall be terminated in any of the following situations:

(i) Expiration of the term of operation;

(ii) Dissolution decided by the foreign investor due to the poor operation and heavy losses of the WFOE;

(iii) Inability to continue the operation due to heavy losses caused by force majeure such as natural calamity, war, etc.;

(iv) Bankruptcy;

(v) Revocation made by the authorities concerned due to the violation of Chinese laws and regulations and harm to the public interests; and

(vi) Occurrence of other reasons of dissolution stipulated in the articles of association of the WFOE.

In the event of (ii), (iii) and (iv) above, the WFOE shall submit an application for termination by itself to the Approval Authority for verification and approval. The date of termination shall begin from the date of verification and approval by the Approval Authority.

In the event of (i), (ii), (iii) and (vi) above, the WFOE shall make a public announcement and notify the creditors within 15 days from the date of termination. It shall, within 15 days from the day on which the announcement of termination is issued, put forward the procedures and principles for liquidation, nominate the candidates for the liquidation committee and, submit them to the Approval Authority, and then carry out liquidation after the examination and verification by the Approval Authority.

Before the completion of the liquidation of a WFOE, the foreign investor shall not remit or carry the funds of the WFOE abroad or dispose of the property of the WFOE by itself. If the net assets and remaining property exceed the registered capital of a WFOE upon completion of the liquidation, such exceeding part is regarded as the profit on which income taxes shall be levied in accordance with the relevant laws of the PRC.

Upon the completion of liquidation of a WFOE, the foreign investor shall go through the formalities for nullifying its registration and canceling its business license with the competent AIC.

**Laws and regulations regarding environmental protection**

The PRC has implemented strict environmental protection regulations on the papermaking industry. Papermakers should comply with the relevant environmental protection regulations for various papermaking phases, including the construction of production project, completion of the construction, daily operation and manufacture of paper.

***Summary***

According to the Environmental Protection Law of the PRC* (中華人民共和國環境保護法) promulgated on 26 December 1989 by the Standing Committee of the NPC ("NPC Standing Committee") and the regulations of the State Council issued thereunder, the Law of the PRC on the Prevention and Treatment of Water Pollution* (中華人民共和國水污染防治法) approved by the NPC Standing Committee on 11 May 1984, amended on 28 February 2008 and implemented on 1 June 2008, the State Environmental Protection Bureau of the PRC implements unified supervision and management of national environmental protection. The environmental protection bureaus at or above the county level are responsible for the environmental administration within their respective jurisdictions. According to the national environmental laws, the Ministry of Environmental Protection* (環境保護部) sets national standards for pollutants emission and local environmental protection bureaus may set stricter local standards. Enterprises are required to comply with the stricter of the two standards.

Enterprises that cause pollution and other public hazards shall adopt environmental protection measures into their plans and establish a system for taking responsibility for environmental protection. Such enterprises shall also take effective measures to prevent and control the pollution and harms caused to the environment by waste gas, waste water, waste residues, dust, malodorous gases, radioactive substances, noise, vibration and radiation generated in the course of production, construction or other activities. Enterprises discharging pollutants shall apply for registration in accordance with the requirements stipulated by the administration department of environmental protection of the State Council. Enterprises discharging pollutants in excess of the national or local prescribed standards shall be fined according to state provisions.

The PRC government may, according to the circumstances and the extent of the pollution, impose administrative penalties of different types and degrees on the violators (enterprises or individuals) of the relevant national environmental laws. Such penalties include warnings, fines, orders to make rectification within a specific period, orders to suspend production, orders to reinstall and put to use pollution treatment facilities that have been dismantled or left idle without prior approval, administrative sanctions on relevant responsible personnel and orders to close the business. The PRC government may also impose fines together with any of the abovementioned administrative penalties. The enterprises or individuals that have caused environmental hazards may be responsible to compensate the victim, and depending on the seriousness of the case, the personnel directly responsible may be investigated for criminal liability.

***Environmental Impact Appraisal***

On 29 November 1998, the State Council promulgated the Ordinance of Environmental Protection Management for the Construction Project* (建設項目環境保護管理條例). On 28 October 2002, the Standing Committee of NPC approved the Law of the People's Republic of China on Appraising of Environmental Impacts* (中華人民共和國環境影響評價法) which became effective on 1 September 2003. According to such laws, the PRC government has set up a system to appraise the environmental impact from construction of project, and classify and administer the environmental impact appraisals in accordance with the degree of the environmental impact. For any project the construction of which may result in a material impact on the environment, an environmental impact report which thoroughly appraises the environmental impact is required; for any project which may result in a slight impact on the environment, an environmental impact record analyzing or appraising the specific environmental impact is required; and for any project which may result in minimal impact on the environment, an environmental impact appraisal is not required but filing an environmental impact form is required. Enterprises responsible for construction of the project must submit the aforesaid environmental impact appraisal documents to the relevant administrative departments of environmental protection for examination and approval. For any enterprise which fails to submit the aforesaid environmental impact appraisal documents according to PRC laws and regulations or if the documents are not approved after examination by the relevant administrative departments, the departments responsible for approving the relevant project shall not approve such project and the enterprise shall not commence the construction of the project.

***Pollutant Discharge***

According to the relevant provisions of the Law of the People's Republic of China on Prevention and Control of Water Pollution* (中華人民共和國水污染防治法) approved by the NPC Standing Committee on 11 May 1984, amended on 28 February 2008 and implemented on 1 June 2008, the building, rebuilding and expansion of construction projects and other aquatic facilities which directly or indirectly discharge sewage to the water shall conduct environmental impact appraisal according to law. The State implements a pollution discharge permit system. Enterprises and institutions which directly or indirectly discharge industrial waste water into the water or are required by law to obtain the pollution discharge permit before discharging waste water or sewage shall obtain the pollution discharge permit.

As required under the Environmental Protection Law of the PRC* (中華人民共和國環境保護法) promulgated on 26 December 1989 by the Standing Committee of NPC, enterprises discharging any pollutants in their daily operations and manufacture shall observe the national discharge standards which are regulated by SEPA. In accordance with the aforesaid law, SEPA has established various discharge standards, as amended and revised from time to time, with regards to each of the discharge of water pollutants, solid pollutants, gas exhaust, noises and other pollutants. Since papermaking enterprises discharge pollutants in their daily operations, they are required to observe the pollutants discharge standards as regulated by SEPA from time to time.

***Tort Liability Law***

On 26 December 2009, the Standing Committee of the National People's Congress of the PRC promulgated the PRC Tort Liability Law* (中華人民共和國侵權責任法), which would come into effect on 1 July 2010. With respect to the environment, the law highlighted the principle that polluters are to assume liability in respect of harm caused by environmental pollution, irrespective of whether they have breached national environmental protection regulations. Under the new Tort Liability Law, the party that discharged the polluting substance bears the evidentiary burden of demonstrating that it is not liable for the harm in accordance with relevant provisions of the law, or that there is no causative link between its conduct and the harm caused to the victim. The law also provides that where the relevant environmental pollution was the fault of a third party, the person suffering harm as a consequence can claim compensation from either the third party itself or the party which actually discharged the polluting substance, with the polluter able to recover any damages paid to the victim from the third party if it can demonstrate that the environmental pollution was the third party's fault.

**Restrictions on production and use of plastic shopping bags**

As a mean of conserving energy and resources and curbing pollution, the General Office of the State Council announced the Circular on Restricting the Production, Sales, and Use of Plastic Shopping Bags* (關於限制生產銷售使用塑料購物袋的通知) on 31 December 2007, pursuant to which, the production, sales and use of plastic bags thinner than 0.025 mm are prohibited and retailers are required to charge consumers for any plastic shopping bags provided by such retailers, effective from 1 June 2008. Further, on 15 May 2008, the Ministry of Commerce, the NDRC, and the State Administration for Industry and Commerce released the Administrative Measures for the Compensational Use of Plastic Shopping Bags in Commodity Retailing Locations* (商品零售場所塑料購物袋有償使用管理辦法), The Measures highlighted the ban on providing free or substandard plastic shopping bags, introduced fines on retailers for non-compliance, and encouraged all retailers to provide eco-friendly substitutes of plastic bags to consumers.

**Laws and regulations regarding the social welfare**

China has established a social security system providing people with social security services. China's social security system includes social insurance, social welfare, the special care and placement system, social relief and housing services. As the core of the social security system, social insurance is composed of five parts: pension insurance, medical insurance, unemployment insurance, work-related injury insurance and maternity insurance (details of which vary with the legal requirements of different regions). An employer is obligated to pay its social security premiums and to withhold and pay its employees' portions to the relevant administrative authorities of the PRC Ministry of Human Resources and Social Security* (人力資源和社會保障部).

China has improved the social security policy and established a system of laws and regulations related. In recent years, China successively promulgated the PRC Labour Law* (中華人民共和國勞動法) (the "Labor Law"), the PRC Labour Contract Law* (中華人民共和國勞動合同法) (the "Labour Contract Law"), the Interim Regulations on the Collection and Payment of Social Insurance Premiums* (社會保險費徵繳暫行條例), Regulations on Work Injury Insurance* (工傷保險條例), Regulations on Unemployment Insurance* (失業保險條例), Trial Measures for Maternity Insurance of the Staff and Workers in Enterprises* (企業職工生育保險試行辦法) and many other regulations.

As for the legal liability of employers, any employer who fails to pay its social insurance premiums or withhold payment of the employee's portion may be ordered by the relevant PRC labour authority or the PRC Tax Bureau to make such payments within a statutory period, and may be liable to pay a penalty.

**Labor and Production Safety**

Effective as of 1 January 2008, labor contracts shall be concluded in writing if labor relationships are to be or have been established between enterprises or institutions and the laborers under The Labor Contract Law of the PRC* (中華人民共和國勞動合同法) (the "Labor Contract Law"). Enterprises and institutions are forbidden to force the laborers to work beyond the time limit and the employers shall pay laborers overtime work in accordance with national regulations. In addition, the labor wages shall not be lower than local standards on minimum wages and shall be paid to the laborers timely. According to The Labor Law of the PRC* (中華人民共和國勞動法) effective as of 1 January 1995, enterprises and institutions shall establish and perfect its system of work place safety and sanitation, strictly abide by State rules and standards on work place safety and sanitation, educate laborers of work place safety and sanitation. Work place safety and sanitation facilities shall comply with State-fixed standards. The enterprises and institutions shall provide laborers with work place safety and sanitation conditions which are in compliance with State stipulations and relevant articles of labor protection.

Effective as of 1 November 2002, enterprises and institutions shall be equipped with the measures for safe production as provided in the Production Safety Law and other relevant laws, administrative regulations, national standards and industrial standards under The PRC Production Safety Law* (中華人民共和國安全生產法) (the "Production Safety Law"). Any entity that is not equipped with the measures for safe production is not allowed to engage in production and business operation activities. Enterprises and institutions shall offer education and training programs to the employees thereof regarding production safety. The design, manufacture, installation, use, checking, maintenance, repair and disposal of safety equipments shall be in conformity with the national standards or industrial standards. In addition, enterprises and institutions shall provide personal protective equipments that reach the national standards or industrial standards to the employees thereof, supervise and educate them to use these equipments according to the prescribed rules.

According to The Employment Promotion Law of the PRC* (中華人民共和國就業促進法) (the "Employment Promotion Law") which became effective on 1 January 2008, the State seeks to create more jobs by encouraging various types of enterprises to, inter alia, expand its existing businesses. In addition, the PRC Government will establish an unemployment insurance system to protect the livelihoods of unemployed persons and assist them in finding employment. The PRC Government at and above the county level shall also establish a public employment service system and public employment service agencies to provide free services to laborers such as announcing information on supply and demand of jobs, market wage levels, vocational training and job recommendations.

**The New Enterprise Income Tax Law of PRC and its implementing rules**

Prior to 1 January 2008, income tax payable by foreign-invested enterprises in the PRC was governed by the Foreign-Invested Enterprise and Foreign Enterprise Income Tax Law of the PRC* (中華人民共和國外商投資企業和外國企業所得稅法) ("FIE Tax Law") promulgated on 9 April 1991 and became effective on 1 July 1991 and the related implementation rules. According to the FIE Tax Law and the relevant implementation rules, foreign-invested enterprises (engaging in the production of goods/services with an expected business life of over 10 years) were to enjoy full exemption from income tax for two years from the year of achieving profitability, and then enjoy a 50% discount in income tax for following three years, that is the third to fifth year from the year of achieving profitability. However, under the Enterprise Income Tax Law of the PRC* (中華人民共和國企業所得稅法) ("New Tax Law"), which was promulgated on 16 March 2007 and became effective on 1 January 2008, income tax rates applicable to both domestic and foreign-invested enterprises were unified at 25% effective from 1 January 2008. Enterprises which enjoyed income tax rates lower than the standard rate of 25% are given a five-year transitional period. Such enterprises will continue to enjoy the lower tax rate before they are gradually subject to the tax rate of 25% within the transitional period. Enterprises which were entitled to two years of 100% exemption and three years of 50% reduction on tax payments before the New Tax Law was promulgated may continue to enjoy such exemption and reduction until the term of such privilege expires.

**High and New Technology Enterprises**

According to The Management and Measures for the Designation of High and New Technology Enterprises* (高新技術企業認定管理辦法) (the "Management and Measures"), effective as of 1 January 2008, the eight high and new technology fields supported by the PRC Government include: (1) electronic information technology; (2) biology and new medical technology; (3) aerospace and aeronautical technology; (4) new materials technology; (5) high technology services; (6) new energy and energy conservation technology; (7) resources and environmental technology; and (8) high and new technology used on traditional industries' reconstructure.

The Management and Measures was enacted to elaborate the high-tech enterprises recognition procedures stipulated under The Enterprise Income Tax Law of the PRC* (中華人民共和國企業所得稅法》) and The Implementation Regulations of Enterprise Income Tax Law of the PRC* (中華人民共和國企業所得稅法實施條例). Under these laws and regulations, PRC-based enterprises that meet the requirements stipulated in the Management and Measures may apply to the applicable governmental authority for a "High and New Technology Enterprises Certificate" which will be valid for three years from the date of issuance. A PRC-based enterprise that has obtained such certificate and recognised as a high-tech enterprise may apply with the applicable tax authority to obtain applicable tax exemptions and reductions.

**Foreign Exchange**

Major reforms have been introduced to the foreign exchange control system of the PRC since 1993. On 28 December 1993, the People's Bank of China ("PBOC"), with the authorisation from the State Council issued The Notice on Further Reform of the Foreign Exchange Control System* (中國人民銀行關於進一步改革外匯管理體制的公告) which came into effect on 1 January 1994. Other new regulations and implementation measures include The Regulations on the Foreign Exchange Settlement, Sale and Payments* (結匯、售匯及付匯管理規定) which were promulgated on 20 June 1996 and took effect on 1 July 1996 and which contain detailed provisions regulating the settlement, sale and payment of foreign exchange by enterprises, individuals, foreign organisations and visitors in the PRC and The Regulations of the PRC on Foreign Exchange Control* (中華人民共和國外匯管理條例) ("New Foreign Exchange Regulation") which were promulgated on 29 January 1996, amended on 14 January 1997 and 1 August 2008 and which contain detailed provisions in relation to foreign exchange control.

Before 5 August 2008, the foreign exchange earnings of all PRC enterprises, other than those foreign-invested enterprises, who were allowed to retain a part of their regular foreign exchange earnings or specifically exempted under the relevant regulations, were to be sold to designated banks. According to the New Foreign Exchange Regulation, the foreign exchange earnings of domestic institutions and domestic individuals can be repatriated or deposited abroad, and the specific conditions and time limits are to be prescribed by the foreign exchange authority under the State Council pursuant to the balance of payments and the need of foreign exchange control. Foreign exchange earnings obtained from current account transactions can be retained or sold to the banks conducting the sale and purchase of foreign exchange. The retaining or selling of the foreign exchange earnings obtained from capital account shall be subject to the approval of foreign exchange authorities, unless the state provides that no approval is needed.

At present, control of the purchase of foreign exchange is relaxed. Enterprises within the PRC which require foreign exchange for their ordinary trading and non-trading activities, import activities and repayment of foreign debts may purchase foreign exchange from designated banks if the application is supported by the relevant documents. Furthermore, FIEs may distribute profit to their foreign investors with funds in their foreign exchange bank accounts kept with designated banks. Should such foreign exchange be insufficient, enterprises may purchase foreign exchange from designated banks upon the presentation of the resolutions of the directors on the profit distribution plan of the particular enterprise.

On 21 July 2005, The Public Announcement of the People's Bank of China of Reforming the RMB Exchange Rate Regime* (中國人民銀行關於完善人民幣匯率形成機制改革的公告) was promulgated and RMB will no longer be pegged to the US$ accordingly. The RMB exchange rate system will be improved with reference to a basket of currencies and with greater flexibility.

On 21 October 2005, the SAFE issued The Notice of the SAFE on Relevant Issues concerning Foreign Exchange Administration for Domestic Residents to Engage in Financing and in Return Investment via Overseas Special Purpose Companies* (國家外匯管理局關於境內居民通過境外特殊目的公司融資及返程投資外匯管理有關問題的通知) (the "SAFE Notice"), which became effective on 1 November 2005. The SAFE Notice requires PRC domestic residents who may either be domestic resident legal entities or domestic resident individuals to register with the local SAFE branches before setting up or controlling special purpose companies overseas. As defined in the SAFE Notice, a domestic resident individual is a natural person who holds a resident identity card, a passport or other lawful identity certificate of the PRC, or a natural person who has no legal identity within the PRC but habitually resides inside the PRC due to reasons of economic interests.

**Intellectual Property Rights**

According to The Patent Law of the PRC* (中華人民共和國專利法) (the "Patent Law") amended as of 25 August 2000 and came into effect on 1 July 2001, the patent right for inventions will be protected for 20 years and the patent right for utility models and designs shall be protected for ten years, commencing on their application dates, respectively. Any persons and entities using a patent without authorisation from the patent owner or conducting other activities which infringe upon patent rights will be held liable for compensations to the patent owner, be subject to fines charged by relevant administrative authorities and even face criminal punishments.

According to The Trade Mark Law of the PRC* (中華人民共和國商標法) (the "Trade Mark Law") amended as of 27 October 2001 and came into effect on 1 December 2001, the period of validity of a registered trademark is (ten) 10 years from the date of registration, renewal is allowed thereafter and the period of validity of each renewal of registration is (ten) 10 years. The administrative authority for industry and commerce has the power to investigate and handle any act of infringement of the exclusive right to use a registered trademark according to law. Where the case is so serious as to constitute a crime, it shall be transferred to the judicial authority for handling.

**Properties**

The PRC Ministry of Land and Resources promulgated the Regulations on the Assignment of State-owned Construction Land Use Rights Through Competitive Bidding, Auction and Listing-for-Sale* (招標拍賣掛牌出讓國有建設用地使用權規定) (the "Regulations on the Assignment of State-owned Construction Land Use Rights") on 28 September 2007, which became effective on 1 November 2007. The Regulations stipulated the methods and procedures for the acquisition of State-owned land use rights.

According to the Urban and Rural Area Planning Law of the PRC* (中華人民共和國城鄉規劃法) (the "Planning Law") promulgated by the Standing Committee of the National People's Congress on 28 October 2007 and implemented on 1 January 2008, before land use rights are granted by the PRC Government, the relevant urban and rural planning authority will stipulate the requirements. If the land use rights for a project are obtained through grant, the relevant construction entity is required to obtain the Construction Land Planning Permit from the relevant planning administration authority after signing the land grant contract. A construction entity is also required to apply to the department of urban and rural planning for a Construction Works Planning Permit before commencing construction, otherwise penalties will be imposed. Upon completion of each phase of a project, a construction entity is required to submit all relevant information to the relevant state land and resources bureau within 6 months after the inspection of the project had been completed; failure to do so within the stipulated time will lead to penalties. Approval from the relevant urban and rural planning authority must be obtained for temporary constructions. All temporary constructions must be demolished before the expiry of the approved time limit, otherwise penalties will be imposed.

**Compliance with PRC Laws and Regulations**

Substantially all of our business and assets are based in the PRC, and we have established three foreign-invested enterprises in the PRC to conduct our operations. We are required to comply with the laws, regulations and measures in the PRC which are relevant to our operations and business. As confirmed by our PRC counsel, King and Wood, except as disclosed in "Risk Factors — Risk Relating to Our Business and Our Group — We have not obtained property title for some of our properties, which could adversely affect our rights to use such properties" and "Business — Property, Plant and Equipment", we have complied with such relevant laws and regulations in all material respects and have obtained all necessary licenses, approvals and permits from relevant regulatory authorities which are material for our operations in the PRC.

## IMPORTANT MILESTONES

The following are the important milestones in our history to date:

- In 1994, Youlanfa was incorporated and started to manufacture paper products.
- In 2001, our first production line designed for the production of copy paper was introduced.
- In 2002, we first obtained accreditation of ISO 9001 in respect of our quality control system.
- In 2002, Youlanfa obtained ISO 14001 certification for our environmental management standards.
- In 2003, our first production line designed for the production of double-sided MF tissue paper was introduced.
- In 2006, Xiyuan and Huaxiang were incorporated and were engaged in the production of MF tissue paper.
- In 2006, our first de-inking facility and first production line designed for the production of single-sided MF tissue paper were introduced.
- In 2006, we entered into an exclusive supply agreement with a Xiamen-based recycling company for the supply of reclaimed pulp and successfully used reclaimed pulp in the production of wrapping tissue paper.
- In 2008, we obtained ISO 10012 certification for our measurement management system.
- In 2009, we started producing semi-transparent paper.

## OUR HISTORY

The history of our Group could be traced back to 1994 when the first company of our Group, Youlanfa, was established in November 1994 as a sino-foreign joint venture company in the PRC. A brief history of our development is set out below.

### Our initial structure

The first company in our Group, Youlanfa, was established in November 1994 as a sino-foreign joint venture company in the PRC, which was then owned as to 23.3% and 76.7% by YLF Trading and Uniland, respectively. At the relevant time, YLF Trading was beneficially wholly owned by Mr Ke, and Uniland was then a sole proprietorship of Mr Henry Ong, an Independent Third Party. At the relevant time, Mr Ke was engaged in paper manufacturing through YLF Trading, which was then engaged in manufacturing of paper products, and Mr Ong was engaged in paper manufacturing in the Philippines through Uniland. Youlanfa mainly manufactured copy paper and double-sided MF tissue paper.

In 1998, Mr Ke acquired the interest of Uniland from Mr Henry Ong, the sole proprietor of Uniland at that time, for a total consideration of PHP200,000 as Mr Henry Ong decided to exit from his investment in paper manufacturing. Such consideration was determined after arm's length negotiation between Mr Ke and Mr Henry Ong, and was fully settled by cash. Youlanfa was then owned as to approximately 5.08% by YLF Trading and as to approximately 94.92% by Uniland, which were both beneficially owned by Mr Ke.

**Our expansion**

With the growth of our business and as part of our strategic development, we established Sunwell in Hong Kong in 2005, and Xiyuan and Huaxiang in the PRC in 2006.

Sunwell was established under the laws of Hong Kong on 13 September 2005 and was then wholly owned by Mr Ke. Sunwell was an investment holding company with no business operations.

In January 2006, Xiyuan was established as a sino-foreign joint venture company in the PRC, which was then owned as to approximately 3.5% by Zhangzhou Shunxiong Trading Co., Ltd* (漳州順雄貿易有限公司) (which was then known as Zhangzhou Huayou Trading Co., Ltd.* (漳州華優貿易有限公司)) ("Zhangzhou Shunxiong") and as to approximately 96.5% by Sunwell. At the relevant time, Zhangzhou Shunxiong was owned as to approximately 86.25% by Mr Wang Kuannai (王寬耐), an Independent Third Party, and as to approximately 13.75% by Mr Zhuang Sixiong (莊思雄), a nephew of Mr Ke. Xiyuan mainly manufactured MF tissue paper.

In March 2006, Huaxiang was established and was then owned as to 5% by YLF Industry (which in turn was then owned as to 20% by Mr Cai Qingjiang (蔡清江), the brother-in-law of Mr Ke, and 80% by Mr Ke), and as to 95% by Sunwell. Huaxiang mainly manufactured single-sided MF tissue paper and double-sided MF tissue paper.

**Our historical restructuring**

In order to streamline our corporate structure and business operations, we restructured our corporate structure as follows:

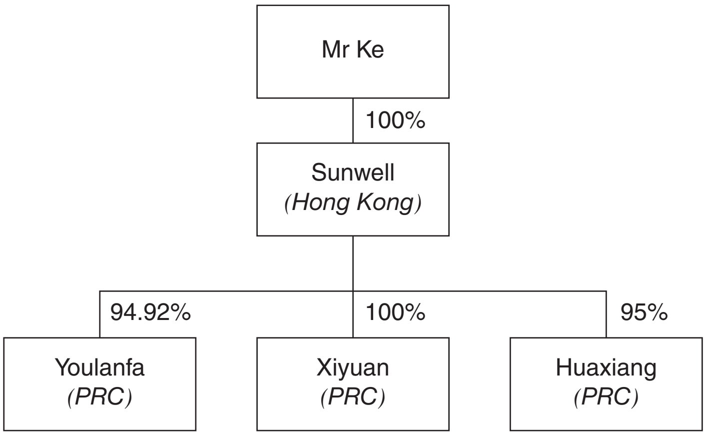
On 23 July 2008, among others, Sunwell as buyer and Uniland as seller entered into an equity transfer agreement, pursuant to which Uniland agreed to transfer its entire equity interest of approximately 94.92% in Youlanfa to Sunwell for a consideration of US$1.00. As both Sunwell and Uniland were then wholly-owned by Mr Ke and such transfer did not involve any change of beneficial interest, a nominal consideration of US$1.00 was used for the transfer. The consideration for such transfer has been fully settled in cash.

On 26 December 2008, Sunwell as buyer and Zhangzhou Shunxiong as seller entered into an equity transfer agreement to acquire the remaining 3.5% interest in Xiyuan from its then minority shareholder in order to have complete control of Xiyuan, pursuant to which Zhangzhou Shunxiong agreed to transfer its entire equity interest of approximately 3.5% in Xiyuan to Sunwell for a consideration of HK$2,414,300, which was based on the initial investment of Xiyuan contributed by Zhangzhou Shunxiong. At the relevant time, Zhangzhou Shunxiong was owned as to approximately 86.25% by Mr

Wang Kuannai (王寬耐), an Independent Third Party, and as to approximately 13.75% by Mr Zhuang Sixiong (莊思雄), a nephew of Mr Ke. The consideration for such transfer has been fully settled by bank transfer. After such transfer, Xiyuan became wholly-owned by Sunwell and became a wholly foreign owned enterprise in the PRC.

## REORGANISATION

Set out below is the shareholding structure of Sunwell and the PRC subsidiaries controlled by Sunwell immediately prior to the Reorganisation:




Our Group underwent the Reorganisation prior to the Listing which involve the following steps:

A. establishment of our offshore shareholding structure;

B. restructuring of our PRC operating subsidiaries; and

C. repurchase of the Smart Port Preferred Shares and ordinary shares of Smart Port held by each of Denron, Everproud, Giantwish, Grand Earning and Best Believe by Smart Port.

### Establishment of our offshore shareholding structure

We streamlined our offshore holding structure in 2009 in preparation for the investment by Cathay Special Paper in our Group and in contemplation of the Global Offering.

#### *Smart Port*

Smart Port was incorporated in the BVI on 20 July 2009. On 14 August 2009, one share of US$1.00 in the capital of Smart Port was issued to Mr Ke. In connection with the investment by Cathay Special Paper in our Group, 1,178 Smart Port Preferred Shares were issued to Cathay Special Paper on 1 September 2009. In order to achieve the desired shareholding proportion in Smart Port between Mr Ke and Cathay Special Paper, on the same day, 8,821 ordinary shares in Smart Port were also issued to Mr Ke. As a result, Smart Port was held as to 88.22% by Mr Ke in the form of ordinary shares and as to 11.78% by Cathay Special Paper in the form of Smart Port Preferred Shares.

On 14 January 2010, Mr Ke, Denron, Everproud, Giantwish, Grand Earning, Best Believe and Cathay Special Paper entered into a deed of share transfer, pursuant to which Mr Ke transferred 316 ordinary shares, 415 ordinary shares, 316 ordinary shares, 316 ordinary shares and 125 ordinary shares in Smart Port to each of Denron, Everproud, Giantwish, Grand Earning and Best Believe, respectively for nil consideration. The transfers under the said deed of share transfer were completed on the same date.

As of the Latest Practical Date, the principal business activities of each of Denron, Everproud, Giantwish, Grand Earning and Best Believe is the holding of the Shares.

Denron is wholly owned by Ms Cai Lishuang, the spouse of Mr Ke and the mother of Mr Ke Jixiong, Ms Ke Jinzhen and Ms Ke Jinzhi. Everproud is wholly owned by Mr Ke Jixiong. Giantwish is owned by Ms Ke Jinzhen, a daughter of Mr Ke and Ms Cai Lishuang, and the sister of Mr Ke Jixiong and Ms Ke Jinzhi. Grand Earning is wholly owned by Ms Ke Jinzhi, another daughter of Mr Ke and Ms Cai Lishuang, and the sister of Mr Ke Jixiong and Ms Ke Jinzhen. Each of Denron, Everproud, Giantwish and Grand Earning is an investment holding company. The transfers to each of Denron, Everproud, Giantwish and Grand Earning were for the purpose of distributing part of the interest of Mr Ke in our Group to his family members.

Best Believe is held in equal shares by Mr Johnny Chen and Mr Li Ho Tan, who are also the sole shareholders of Fortune China Financial Advisory Limited ("Fortune China"). Each of Fortune China, Mr Johnny Chen and Mr Li Ho Tan is not a licensed person under the SFO. As confirmed by each of Fortune China, Mr Johnny Chen and Mr Li Ho Tan, each of them has not provided any service which is a regulated activity (namely, dealing in securities, dealing in future contracts, leveraged foreign exchange trading, advising on securities, advising on future contracts, advising on corporate finance, providing automated trading services, securities margin financing and asset management) which requires a license under the SFO and has not engaged and/or provided any service that is to be provided by a sponsor to a listing applicant. We engaged Fortune China as our advisor to prepare us for and assist us in the Listing for matters involving internal coordination within the Company and which fall outside the normal responsibilities and services of the Sole Sponsor as required under the Listing Rules. Our appointment of Fortune China and the Sole Sponsor took effect from 13 August 2009 and 11 August 2009, respectively. Notwithstanding the proximity on the dates of appointment, the appointment and services provided by Fortune China were separate and independent from those of the Sole Sponsor. The services provided by Fortune China include financial consultancy, strategic planning and secondment of staff to our Company to assist us in administrative and other support services, namely, the collection, organisation and distribution of information and documents prepared and provided by the management of our Group in response to the requests addressed to our Group from various professional parties involved in the listing application. Such administrative and other support services do not involve any allocation of work amongst or making arrangement with our external advisers involved in the application for the Listing and are not typically performed by a sponsor to a listing application. Given that such administrative and other support services could have been performed by our own administrative staff if we have not engaged Fortune China, both our Directors and the Sole Sponsor consider that the appointment of Fortune China has not in any way undermined the Sole Sponsor's duties and responsibilities under the Listing Rules.

As the business of our Group is rapidly growing, which requires the undivided attention of our management, our Directors believe it is beneficial to our Group to engage Fortune China which offered its assistance by seconding its staff to our Company to assist in administrative and other support services relating to the listing application. Our Directors consider that our Company could easily hire additional staff to provide such administrative and support services. However, given that the management of our Company consider that the additional manpower would likely be redundant to our Group after completion of the Listing, it is preferable to engage Fortune China to provide seconded staff on a project basis. Further, as the fees paid to Fortune China include the provision of the secondment of staff, the management of our Group could better control the cost of the listing application and at the same time minimise the diversion of the attention of the management of our Group from our business. The above services provided by Fortune China to us were completely independent from the services provided by the Sole Sponsor in connection with the Listing, which were prescribed under the Listing Rules. HSBC is acting as the Sole Sponsor in our listing application and will take full responsibility in performing its duties in accordance with the Listing Rules. As each of Fortune China and the Sole Sponsor discharges its respective duties independently, from different roles and perspective and none of them has relied on the work done or service provided by each other, our engagement of Fortune China has not affected the impartiality and independence of the Sole Sponsor required by the Listing Rules and the services provided by the Sole Sponsor to us in connection with the Listing.

In consideration for the services provided by Fortune China, we have paid an initial fee of RMB300,000 and a 1.25% of the total interest of our Group to Fortune China (or its nominee). The transfer of shares in Smart Port from Mr Ke to Best Believe, the nominee of Fortune China, was to give effect to such arrangement. Further, if Fortune China assists us to obtain private equity investment prior to the Listing, Fortune China will be entitled to receive a fee equivalent to 2% of the total funds raised through such investment, which was determined after arm's length negotiations. As Fortune China has assisted us to obtain the investment from Cathay Special Paper, we have paid a total of US$411,600 to Fortune China, being 2% of the funds raised from the subscription by Cathay Special Paper. Please refer to "Investment by Cathay Special Paper" in this section for details of the subscription by Cathay Special Paper. As we do not anticipate any further private equity investment will be made in our Company prior to the Listing, no further fees will be paid to Fortune China (or its nominee) for assisting us in obtaining private equity investment. Except as disclosed above, Fortune China (or its nominees) will not be entitled to any other fees or any other benefits in kind in relation to the services referred to above. In addition, we have not agreed with Fortune China for any fee arrangement in relation to any external financing that it may assist the Company to obtain after Listing.

Upon completion of such share transfers, Smart Port became owned as to approximately 73.34% by Mr Ke, as to 3.16% by Denron, as to 4.15% by Everproud, as to 3.16% by Giantwish, as to 3.16% by Grand Earning, as to 1.25% by Best Believe and as to 11.78% by Cathay Special Paper.

***Our Company***

Our Company was incorporated as an exempted company in the Cayman Islands on 12 October 2009 to act as the ultimate holding company of the subsidiaries in our Group. At the time of its incorporation, one initial subscriber Share was issued to Codan Trust Company (Cayman) Limited, which was subsequently transferred to Smart Port on the same day.

***Xi Yuan BVI***

Xi Yuan BVI was incorporated in the BVI on 10 July 2009. On 14 August 2009, one share of US$1.00 in the capital of Xi Yuan BVI was issued to Smart Port.

On 14 January 2010, as part of the Reorganisation, our Company, Mr Ke and Smart Port entered into a share transfer agreement, pursuant to which Smart Port transferred its entire shareholding in Xi Yuan BVI to our Company in consideration of our Company issuing 9,999 Shares to Smart Port credited as fully paid. As a result of such transfer, the entire issued share capital of our Company increased to 10,000 Shares and Xi Yuan BVI became a wholly-owned subsidiary of our Company.

***Sunwell***

As at 27 August 2009, Sunwell had an issued share capital of HK$10,000 divided into 10,000 shares of HK$1.00 each held by Mr Ke. In connection with the investment by Cathay Special Paper in our Group, the issued share capital of Sunwell was increased to HK$10,000,000 by the creation of an additional 9,990,000 shares of HK$1.00 each, all of which were subscribed by Xi Yuan BVI on 28 August 2009. As a result, Sunwell was held as to 0.10% by Mr Ke, and as to 99.90% by Xi Yuan BVI. To complete the Reorganisation, the 10,000 shares of HK$1.00 each in Sunwell held by Mr Ke were subsequently transferred to Xi Yuan BVI on 2 October 2009 for a total consideration of HK$10,000, equivalent to the par value of the shares of Sunwell being transferred. After such transfer, Sunwell became a wholly owned subsidiary of Xi Yuan BVI.

**Restructuring of our PRC operating subsidiaries**

***Youlanfa***

On 15 July 2009, as part of the Reorganisation, Sunwell as the buyer and YLF Trading as seller entered into an equity transfer agreement, pursuant to which YLF Trading agreed to sell a 5.08% equity interest in Youlanfa, being its entire equity interest in Youlanfa, to Sunwell for a consideration of approximately RMB10.6 million, which was based on the net asset value of Youlanfa as at 30 June 2009. YLF Trading was then owned as to approximately 16.67% by Ms Cai Lishuang, the spouse of Mr Ke and the mother of Mr Ke Jixiong, and as to approximately 83.33% by YLF Industry, which was then owned as to 20% by Mr Cai Qingjiang (蔡清江), brother-in-law of Mr Ke and brother of Ms Cai Lishuang, and as to 80% by Mr Ke Jixiong. The consideration of such transfer has been fully settled by bank transfer. After such transfer, Youlanfa became a wholly foreign owned enterprise in the PRC and a wholly-owned subsidiary of Sunwell.

Pursuant to an agreement dated 25 August 2009 and a supplemental agreement dated 25 December 2009, Youlanfa acquired certain assets from YLF Leathercover at the total consideration of approximately RMB21.7 million, which was determined by reference to a valuation report prepared by Fujian Lianhe Zhonghe Asset Valuation Co., Ltd.* (福建聯合中和資產評估有限公司). The acquired assets include the land use rights for a piece of land located at Xibin Farm Industrial Zone, Xibin Town, Jinjiang, Fujian, the PRC* (中國福建晉江市西濱鎮西濱農場工業區) with an area of 15,432 sq.m., and the title to six buildings with a total gross floor area of 4,956.32 sq.m.

***Huaxiang***

On 13 August 2009, as part of the Reorganisation, YLF Industry as the seller and Sunwell as the buyer entered into an equity transfer agreement whereby YLF Industry agreed to sell 5% equity interest, being its entire equity interest in Huaxiang, to Sunwell for a consideration of approximately RMB8.8 million, which was determined based on the net asset value of Huaxiang as at 30 June 2009. The consideration of such transfer has been fully settled by bank transfer.

Pursuant to an agreement dated 25 May 2009, Huaxiang acquired three pieces of land located at Xibin Farm Industrial Zone, Xibin Town, Jinjiang, Fujian, the PRC* (中國福建晉江市西濱鎮西濱農場工業區) with a total area of 43,082 sq.m. from YLF Industry for a consideration of approximately RMB32.3 million, which was determined with reference to a property valuation report prepared by Fujian Lianhe Zhonghe Asset Valuation Co., Ltd.* (福建聯合中和資產評估有限公司).

Pursuant to an agreement dated 1 July 2009, Huaxiang acquired the land use rights for a piece of land located at Xibin Farm Industrial Zone, Xibin Town, Jinjiang, Fujian, the PRC* (中國福建晉江市西濱鎮西濱農場工業區) from YLF Leathercover with a total gross floor area of 7,434.6 sq.m. for a total consideration of approximately RMB5.55 million, which was determined with reference to a property valuation report prepared by Fujian Lianhe Zhonghe Asset Valuation Co., Ltd.* (福建聯合中和資產評估有限公司).

**Repurchase of Smart Port Preferred Shares and ordinary shares of Smart Port held by each of Denron, Everproud, Giantwish, Grand Earning and Best Believe by Smart Port**

On 8 April 2010, Smart Port, Cathay Special Paper, Denron, Everproud, Giantwish, Grand Earning and Best Believe entered into a share repurchase agreement pursuant to which Smart Port repurchased all the Smart Port Preferred Shares from Cathay Special Paper and the ordinary shares of Smart Port held by each of Denron, Everproud, Giantwish, Grand Earning and Best Believe. As consideration of such repurchases, Smart Port transferred 1,178 Shares to Cathay Special Paper, 316 Shares to Denron, 415 Shares to Everproud, 316 Shares to Giantwish, 316 Shares to Grand Earning and 125 Shares to Best Believe. After such repurchases, each of Cathay Special Paper, Denron, Everproud, Giantwish, Grand Earning and Best Believe became a shareholder of our Company and ceased to have any interest in Smart Port, and Smart Port became wholly-owned by Mr Ke accordingly. Each of the transfer of the Shares from Smart Port to Denron, Everproud, Giantwish, Grand Earning, Best Believe and Cathay Special Paper were completed on 8 April 2010. None of the Shares held by Smart Port, Denron, Everproud, Giantwish, Grand Earning and Cathay Special Paper will be treated as part of the public float, whilst the Shares held by Best Believe will be treated as part of the public float. For details of the investments by Cathay Special Paper, please refer to "Investment by Cathay Special Paper" in this section.

## INVESTMENT BY CATHAY SPECIAL PAPER

### Cathay Subscription Agreement

On 19 August 2009, Cathay Special Paper, a company wholly-owned by Cathay Capital Holdings II, L.P., entered into the Cathay Subscription Agreement (as supplemented by the Supplemental Deed) pursuant to which Cathay Special Paper agreed to subscribe for the Smart Port Preferred Shares, representing 11.78% of the total issued share capital of Smart Port after such subscription, for a total consideration of RMB139.95 million, which is to be used for the expansion of the production capacity of the products currently produced, made or sold by the subsidiaries of the Company in the PRC and/or providing capital of the Group as a whole. Such consideration was determined based on the valuation of the Group after the investment of Cathay Special Paper on a fully diluted basis of RMB1,188 million, which was calculated based on an estimated audited net profit of the Group for the year ended 31 December 2009 of approximately RMB165 million and a price/ earnings ratio of 7.2 times.

Under the Cathay Subscription Agreement, the payment by Cathay Special Paper was to be made in two tranches, with the first tranche of RMB equivalent of US$10 million paid on 28 August 2009 against the issuance of the 1,178 Smart Port Preferred Shares to Cathay Special Paper, and the second tranche of approximately RMB139.95 million less the RMB equivalent of the first tranche payment of US$10 million would become payable upon the reasonable satisfaction of all post-closing conditions ("Cathay Second Tranche Payment"). Such post-closing conditions (as supplemented by a deed of undertaking from Mr Ke, Mr Ke Jixiong and Smart Port in favour of Cathay Special Paper dated 28 August 2009) include: (1) the completion of acquisitions, and the government formalities in the PRC, by Sunwell of 5.08% equity interest in Youlanfa from YLF Trading and 5% equity interest in Huaxiang from YLF Industry; (2) the completion of all formalities in the PRC relating to the acquisitions of the land use rights by Xiyuan from Zhangzhou Huarong Paper Co., Ltd.* (漳州華榮紙業有限公司) on 18 January 2009, by Huaxiang from YLF Industry on 28 June 2007, and by Huaxiang from YLF Industry on 25 May 2009; (3) the release of all guarantees provided to related parties of Mr Ke and Mr Ke Jixiong; (4) the release of mortgage created over properties of the subsidiaries of our Company in the PRC to secure indebtedness of YLF Leathercover; (5) the acknowledgement of the SAFE registration application for the interest of Mr Ke in our Group pursuant to the Notice on Issues Relating to the Administration of Foreign Exchange in Fund-raising and Return Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Vehicle* (關於境內居民通過特殊目的公司融資及返程投資外匯管理有關問題的通知) (the "SAFE Circular 75"), which was issued by SAFE on 21 October 2005, and effective on 1 November 2005; (6) the provision of a business plan of the Group prepared by Mr Ke and Mr Ke Jixiong to the satisfaction of Cathay Special Paper; (7) the completion of the transfer of Sunwell to Xi Yuan BVI; (8) the obtainment of confirmations from the relevant government authorities in the PRC certifying the subsidiaries of our Company in the PRC have duly satisfied or discharged their respective obligations regarding payment of social security contribution funds as employers; (9) the full payment of the unpaid registered capital of Youlanfa of RMB60 million, which was to be fully paid within 12 months after the completion of registration procedure that Sunwell became a sole shareholder of Youlanfa; and (10) the production of original land use rights grant contracts for certain parcels of land of the Group made with the relevant land bureau and evidence of substantiating payment of the related land use rights premium (the "Post-closing Conditions"). The Cathay Second Tranche Payment paid by Cathay Special Paper to Smart Port was settled on 19 January 2010. Please refer to "Smart Port Loan Agreement" in this section for details.

Pursuant to the Cathay Subscription Agreement, Smart Port has undertaken that the Smart Port Preferred Shares issued to Cathay Special Paper would be substituted by Shares in our Company. Further, under the terms of the Cathay Subscription Agreement, Cathay Special Paper was granted certain minority protection rights, including pre-emptive rights to purchase new shares of Smart Port, a right of first refusal for shares of Smart Port proposed to be disposed by other shareholders, a tag-along right for shares of Smart Port to be transferred by Mr Ke, the right to appoint one director to the board of directors of Smart Port and other members of our Group, and prior approval rights with respect to certain corporate actions that we may undertake in the future. Such corporate actions include actions that will dilute the interest of the shareholders of our Group, commencing or acquiring a new line of business that is not currently being undertaken by our Group, and borrowing and providing security interest in excess of RMB5 million. Cathay Special Paper ceased to be a holder of the Smart Port Preferred Shares and became a Shareholder on 8 April 2010 and thereafter, Cathay Special Paper ceased to enjoy the above-mentioned minority protection rights.

As at the Latest Practicable Date, out of eight Directors of our Board of Directors, Cathay Special Paper has one representative, namely Mr Paul Steven Wolansky, on our Board of Directors. There is no outstanding obligations on the part of our Group under the Cathay Subscription Agreement as at the Latest Practicable Date.

***Repurchase of the Smart Port Preferred Shares and transfer of our Shares to Cathay Special Paper***

As disclosed under the subsection headed "Reorganisation" above, on 8 April 2010, Smart Port repurchased all of the Smart Port Preferred Shares held by Cathay Special Paper and transferred 1,178 Shares to Cathay Special Paper as consideration. As a result, Cathay Special Paper ceased to hold any Smart Port Preferred Shares and became a direct shareholder of our Company upon such repurchase and transfer. Further, the Shares held by Cathay Special Paper in the Company, including Shares to be issued under the Capitalisation Issue, will not be counted towards the public float.

Assuming there are no diluting issuances by our Company such as consolidation, subdivision or capitalisation of our Shares immediately upon the completion of the Capitalisation Issue and the Global Offering, Cathay Special Paper will hold a total of 88,350,000 Shares, respectively, representing a shareholding of approximately 8.84% in our Company.

The price per Share paid by Cathay Special Paper was approximately HK$1.80 (indicative exchange rate of HK$1.00 = RMB0.87898) (the "Cathay Investment Price"). Based on the indicative Offer Price range, the Cathay Investment Price represents a discount of approximately 30.2% to HK$2.58 per Share, being the lower end of the stated Offer Price range, and a discount of approximately 46.7% to HK$3.38 per Share, being the upper end of the stated Offer Price range.

The investment risks that Cathay Special Paper were subject to when making investment in our Company back in August 2009 were different from the risks which the investing public may have to bear in the context of the Global Offering. The Cathay Investment Price reflected the illiquidity of the Shares, the historical financial performance of our Group, the strategic value added by Cathay Special Paper to our Company, the lock-up arrangement applicable to the Shares held by Cathay Special Paper, as set out below and the bargaining positions of the parties at that time.

The proceeds from the investment by Cathay Special Paper in our Company were used as our working capital for the expansion of our business and for our internal restructuring. We believe that the presence of Cathay Special Paper as our Shareholder has added strategic value to our Group including boosting the profile of our Company and our shareholder base, reinforcing good corporate governance practices and generally enhancing accountability and transparency of our Company. In addition, our Directors believe that Cathay Special Paper and the Cathay Capital Group's experience in previous investments will also benefit the development of our Group.

***Lock-up***

Cathay Special Paper and its shareholder, namely Cathay Holdings II, L.P. have provided an undertaking to our Company, the Sole Global Coordinator, the Hong Kong Underwriters and the Sole Sponsor in relation to the non-disposal of the Shares during the period of six months from the Listing Date. For more information, please see the section headed "Underwriting — Underwriting Arrangements and Expenses — Other undertakings" in this prospectus.

***Share adjustment mechanism***

Under the Cathay Subscription Agreement (as amended by the Supplemental Deed), the shareholding proportion of Cathay Special Paper in our Group is subject to adjustment depending on the financial performance of our Group for the years ending 31 December 2009 and 2010. If the audited net profit of our Group, including minority interest but excluding, among others, legal and underwriting expenses incurred by our Company in relation to the Listing, is less than 2009 Performance Benchmark and 2010 Performance Benchmark, respectively, the shareholding of Cathay Special Paper in our Group shall be adjusted in accordance with the following pre-determined adjustment formula as stipulated in the Cathay Subscription Agreement:

(a) where our Group fails to achieve the 2009 Performance Benchmark[1], the equity ratio held by Cathay Special Paper shall be adjusted by the 2009 Adjusted Equity Ratio, which is to be computed by the following formula ("2009 Adjustment"):

PA1 = P / (A1 / B1)

where:

PA1 = the equity ratio of Cathay Special Paper in our Group immediately after 2009 Adjustment

P = 11.78%

A1 = the actual audited net profit[2] of our Group as stated in the accountants report for the year ending 31 December 2009

B1 = 2009 Performance Benchmark (i.e., RMB165 million)

(b) where our Group fails to achieve the 2010 Performance Benchmark, the equity ratio held by Cathay Special Paper shall be adjusted by the 2010 Adjusted Equity Ratio, which is to be computed by the following formula ("2010 Adjustment"):

PA2 = P / (A2 / B2)

where:

PA2 = equity ratio of Cathay Special Paper in our Group immediately after 2010 Adjustment

P = 11.78%

A2 = the actual audited net profit[2] of our Group as stated in the accountants report for the year ending 31 December 2010

B2 = 2010 Performance Benchmark (i.e., RMB220 million)

---

*Note 1:* As the audited net profit of our Group for the year ended 31 December 2009 as disclosed in the Accountants' Report to Appendix I of this prospectus amounted to approximately RMB170.7 million, our Group has met the 2009 Performance Benchmark, and no share adjustment or Performance Benchmarks Cash Compensation will be made for the year ended 31 December 2009.

*Note 2:* The actual audited net profit of our Group would correspond to the line item "Profit and total comprehensive income for the year" in the "Combined Statement of Comprehensive Income" to the Accountants' Report to Appendix I of this prospectus for 2009, or for 2010, similar line item in the audited report of our Group for the year ending 31 December 2010 but excluding, among others, legal and underwriting expenses for the Listing.

In the event that Cathay Special Paper becomes entitled to share adjustment pursuant to the above-mentioned pre-determined formulae, Cathay Special Paper may require Mr Ke to transfer part of his interest in our Group to Cathay Special Paper at a nominal consideration. Such share adjustment was determined based on arm's length negotiation between Cathay Special Paper and Mr Ke with reference to the 11.78% interest held by Cathay Special Paper in our Group (without taking into account of the effect of the Global Offering), the 2009 Performance Benchmark (or the 2010 Performance Benchmark as the case may be) and the actual profits achieved in the relevant year. As agreed between Cathay

Special Paper and Mr Ke, in compliance with Rule 10.07 of the Listing Rules, in the event that Mr Ke is required to transfer Shares to Cathay Special Paper based on the above share adjustment formulae, such transfer of Shares will only take place after the expiration of the lock-up period of the Shares that Smart Port and Mr Ke are subject to. In addition, in the event that the equity ratio of Cathay Special Paper calculated in accordance with the above-mentioned pre-determined formulae shall become greater than 30%, for the portion exceeding 30%, Mr Ke shall make a cash compensation ("Performance Benchmarks Cash Compensation") to Cathay Special Paper based on the following formulae:

(a) If our Group fails to achieve the 2009 Performance Benchmark and the 2009 Adjusted Equity Ratio is greater than 30%:

a = b + b (x) c

where:

a = the Performance Benchmarks Cash Compensation for 2009 adjustment

b = (the 2009 Adjusted Equity Ratio - 30%) (x) (the actual audited net profit of our Group as stated in the accountants' report for the year ending 31 December 2009 (x) 7.2)

c = an interest rate of 20% per annum calculated from 28 August 2009 up until full payment of the Performance Benchmarks Cash Compensation

(b) If our Group fails to achieve the 2010 Performance Benchmark and the 2010 Adjusted Equity Ratio is greater than 30%:

a = b + b (x) c

where:

a = the Performance Benchmarks Cash Compensation for 2010 adjustment

b = (the 2010 Adjusted Equity Ratio - 30%) (x) (the actual audited net profit of our Group as stated in the accountants' report for the year ending 31 December 2010 (x) 5.4)

c = an interest rate of 20% per annum calculated from 28 August 2009 up until full payment of the Performance Benchmarks Cash Compensation.

If both the 2009 Adjusted Equity Ratio and the 2010 Adjusted Equity Ratio are greater than 30%, Cathay Special Paper is only entitled to receive the higher Performance Benchmarks Cash Compensation calculated by the 2 formulae above.

As the share adjustment mechanism referred to in this sub-section, if triggered, would involve the transfer of our Shares by Shareholders and any Performance Benchmarks Cash Compensation would be paid from Mr Ke personally, there would not be any accounting impact on the financial statements of our Company for such share adjustment.

The above references to the 2009 Performance Benchmark and the 2010 Performance Benchmark are simply benchmarks that Mr Ke agreed with Cathay Special Paper for the purposes of the share adjustment mechanism, which is a purely pre-determined private arrangement among the parties to the Cathay Subscription Agreement and does not constitute any guarantee or forecast of the future profitability of our Group.

As the audited net profit of our Group for the year ended 31 December 2009 as disclosed in the Accountants' Report to Appendix I of this prospectus amounted to RMB170.7 million, our Group has met the 2009 Performance Benchmark which therefore becomes lapsed, and no share adjustment or Performance Benchmarks Cash Compensation has been or will be made for the year ended 31 December 2009.

Notwithstanding the fact that the forecast for the profit of our Group for the six months ending 30 June 2010 is not less than RMB82 million, we expect, solely for the purposes of estimating the likelihood of fulfillment of the 2010 Performance Benchmark, that our full year profit for the year ending 31 December 2010 will meet the 2010 Performance Benchmark. In the event that the 2010 Performance Benchmark is not met thus triggering any share adjustment or payment of the Performance Benchmark Cash Compensation, we will duly make an announcement in accordance with the requirements of the Listing Rules.

**Special Dividend Undertaking and Deed of Release**

Pursuant to an undertaking (the "Special Dividend Undertaking") dated 28 August 2009 and entered into between Mr Ke, Smart Port (Mr Ke and Smart Port, the "Indemnifiers") and Cathay Special Paper, the Indemnifiers have undertaken to Cathay Special Paper that, among other things, if the valuation of our Group immediately prior to the Listing of our Company is less than RMB1.485 billion, the Indemnifiers shall cause our Group to declare a special dividend to our then Shareholders prior to the Listing. Such special dividend, if declared and paid, shall be the difference between RMB1.485 billion and the actual valuation of our Group immediately prior to the Listing. The purpose of the special dividend is to ensure Cathay Special Paper will receive a fixed return per annum of not less than a pre-determined percentage to their investment in our Group.

On 1 April 2010, the parties to the Special Dividend Undertaking entered into a deed of release ("Deed of Release") pursuant to which Cathay Special Paper has agreed that (i) the Indemnifiers shall be released and discharged from all of their respective obligations under the Special Dividend Undertaking absolutely; and (ii) all rights, interests and claims which Cathay may have under the Special Dividend Undertaking shall cease and terminate absolutely. No dividend has been declared by our Group pursuant to the Special Dividend Undertaking prior to the date of the Deed of Release. In addition, upon execution of the Deed of Release, no special dividend pursuant to the Special Dividend Undertaking will be declared.

**Smart Port Loan Agreement**

On 3 December 2009, Smart Port as borrower, Mr Ke as guarantor and Cathay Special Paper as lender entered into the Smart Port Loan Agreement, pursuant to which Cathay Special Paper agreed to provide a bridging loan of RMB71.95 million (payable in US dollars in the amount of US$10.58 million as agreed by the parties) to Smart Port to facilitate its completion of certain outstanding Post-closing Conditions and was repayable on demand. The post-closing conditions under the Smart Port Loan Agreement are the outstanding Post-closing Conditions as at the date of the Smart Port Loan Agreement, namely, (1) the completion of acquisitions, and the government formalities in the PRC, by Sunwell of 5.08% equity interest in Youlanfa from YLF Trading and 5% equity interest in Huaxiang from YLF Industry; (2) the completion of all formalities in the PRC relating to the acquisitions of the land use rights by Xiyuan from Zhangzhou Huarong Paper Co., Ltd. (漳州華榮紙業有限公司) on 18 January 2009, by Huaxiang from YLF Industry on 28 June 2007, and by Huaxiang from YLF Industry on 25 May 2009; (3) the release of all guarantees provided to related parties of Mr Ke and Mr Ke Jixiong; (4) the release of mortgage created over properties of the subsidiaries of our Company in the PRC to secure indebtedness of YLF Leathercover; (5) the acknowledgement of the SAFE registration application for the interest of Mr Ke in our Group pursuant to SAFE Circular 75; (6) the obtainment of confirmations from the relevant government authorities in the PRC certifying the subsidiaries of our Company in the PRC have duly satisfied or discharged their respective obligations regarding payment of social security contribution funds as employers; and (7) the provision of a new business license of Youlanfa evidencing the full payment of the unpaid registered capital of RMB60 million. Pursuant to the Smart Port Loan Agreement, an amount of US$4 million has been provided to Smart Port by Cathay Special Paper on 29 December 2009, with the balance provided to Smart Port on 19 January 2010 as the post-closing conditions under the Smart Port Loan Agreement have been satisfied.

Pursuant to the terms of the Cathay Subscription Agreement, the obligation by Cathay Special Paper to make the Cathay Second Tranche Payment would only be triggered upon completion of the Post-closing Conditions. As the funds from the Smart Port Loan Agreement were used to facilitate Smart Port to complete the Post-closing Conditions and that once the Post-closing Conditions have been completed, Cathay Special Paper has to settle the Cathay Second Tranche Payment, Smart Port and Cathay Special Paper agreed to offset the Cathay Second Tranche Payment with the outstanding loan owed by Smart Port to Cathay Special Paper under the Smart Port Loan Agreement when Smart Port completes the Post-closing Conditions. Cathay Special Paper and Smart Port agreed to such an arrangement for simplicity sake and that the purpose of the loan, which was to facilitate the completion of certain post-closing conditions, would have been satisfied.

As at 19 January 2010, as Smart Port has completed the Post-closing Conditions to the reasonable satisfaction of Cathay Special Paper as required under the Cathay Subscription Agreement, the Cathay Second Tranche Payment was offset against the outstanding loan due payable by Smart Port to Cathay Special Paper under the Smart Port Loan Agreement of RMB71.95 million. Cathay Special Paper and Smart Port have satisfied their payment obligations under the Cathay Subscription Agreement and the Smart Port Loan Agreement, respectively.

Except as disclosed in this section headed "History and corporate structure" of this prospectus, our Company has not granted any other special rights to Cathay Special Paper pursuant to the Cathay Subscription Agreement or any auxiliary documents to the Cathay Subscription Agreement. Further, as at the Latest Practicable Date, there is no outstanding obligations on the part of our Group under the Cathay Subscription Agreement.

## INFORMATION REGARDING CATHAY SPECIAL PAPER

Cathay Special Paper is a wholly-owned subsidiary of Cathay Capital Holdings II, L.P. and was a special purpose company incorporated for the purpose of investing in our Group. Prior to the completion of the Subscription Agreement, Cathay Special Paper and Cathay Capital Holdings II, L.P. were Independent Third Parties to us. Cathay Capital Holdings II, L.P. is a private equity fund and a limited partnership registered under the laws of the Cayman Islands and is a member of the Cathay Capital Group. The general partner of Cathay Capital Holdings II, L.P. is Cathay Master GP, Ltd., in which Mr Paul Steven Wolansky, our non-executive Director, controls 45%. The investment manager of Cathay Capital Holdings II, L.P. is New China Capital Management, L.P., which Mr Paul Steven Wolansky controls 50% and is its chairman, president and chief executive officer.

The Cathay Capital Group is principally engaged in investments across a broad range of sectors including property development, consumer industry, infrastructure, distribution and media, as well as both light and heavy industries in the PRC.

## SHAREHOLDER'S LOANS BETWEEN SMART PORT AND XI YUAN BVI

On 27 August 2009, Xi Yuan BVI as borrower and Smart Port as lender entered into a shareholder agreement, pursuant to which Smart Port agreed to provide an interest free shareholder's loan of US$10.00 million to Xi Yuan BVI.

Further, as funds from the Smart Port Loan Agreement were for the benefit of the Group, such as completing acquisition of minority interest in Huaxiang and Youlanfa by Sunwell and to pay the outstanding registered capital of Youlanfa, on 10 December 2009, Xi Yuan BVI as borrower and Smart Port as lender entered into a shareholder loan agreement, pursuant to which Smart Port agreed to provide an interest free shareholder's loan of US$10.58 million, repayable within 5 business days upon demand in writing.

On 5 May 2010, Smart Port entered into a deed of waiver in favour of Xi Yuan BVI, pursuant to which Smart Port agreed to unconditionally waive the shareholder's loan of US$10 million under the shareholder loan agreement entered into between Smart Port as lender and Xi Yuan BVI as borrower dated 27 August 2009 and the shareholder's loan of US$10.58 million under the shareholder loan agreement entered into between Smart Port as lender and Xi Yuan BVI as borrower dated 10 December 2009.

## SAFE REGISTRATION

According to SAFE Circular 75:

- domestic residents who plan to establish or control an offshore special purpose vehicle must conduct foreign exchange registration with the local foreign exchange authority;
- domestic residents who have contributed their assets or shares of a domestic enterprise into an offshore special purpose vehicle, or have raised funds offshore after such contribution, must conduct foreign exchange registration for the modification of the record concerning the offshore special purpose vehicle with the local foreign exchange authority; and

- domestic residents who are the shareholder of an offshore special purpose vehicle are required to go through registration for the modification of the record with the local foreign exchange authority within 30 days from the date of any major capital change event, such as an increase/decrease of capital, share transfer, share swap, merger or division, long term equity or debt investment or foreign guarantee where no round-trip investment is involved.

Our PRC legal advisers, King & Wood, have advised us that Mr Ke, Ms Cai Lishuang, Mr Ke Jixiong, Ms Ke Jinzhen and Ms Ke Jinzhi, being the beneficial shareholders of our Group and domestic residents of the PRC, have completed the related procedures for their respective foreign exchange registration of overseas investments at the local branch of SAFE on 26 February 2010 under the SAFE Circular 75.

**REORGANISATION AND THE RULES ON THE MERGER AND ACQUISITION OF DOMESTIC ENTERPRISES BY FOREIGN INVESTORS**

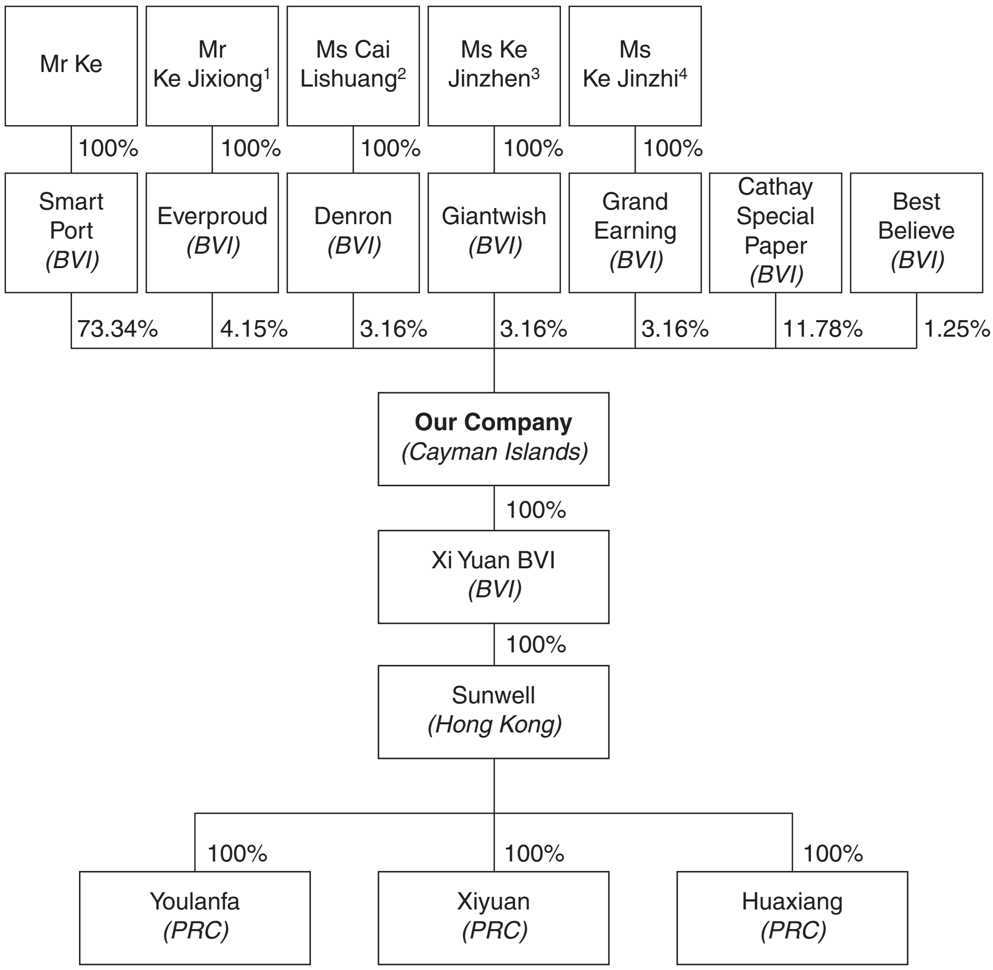
Under the Rules on the Acquisition of Domestic Enterprises by Foreign Investors in the PRC* (關於外國投資者併購境內企業的規定) (the "M&A Rules"), which became effective on 8 September 2006, a foreign investor is required to obtain necessary approvals when (i) a foreign investor acquires equity in a domestic company thereby converting it into an foreign-invested enterprise, or subscribes for new equity via an increase of registered capital thereby converting it into a foreign-invested enterprise; (ii) a foreign investor establishes a foreign-invested enterprise which purchases and operates the assets of a domestic enterprise, or which purchases the assets of a domestic enterprise and injects those assets to establish a foreign-invested enterprise. In addition, if a security offering involves a reorganisation that falls within the scope of the activities described above, approval for the offering from the CSRC is required.

King & Wood, our PRC legal advisers, have advised us that since each of Youlanfa, Huaxiang and Xiyuan is a Sino-foreign equity joint venture enterprise established in the PRC prior to 8 September 2006, the date when M&A Rules became effective, each of the acquisition of 100% equity interests of Youlanfa, the 5% equity interest in Huaxiang and the 3.5% equity interest in Xiyuan by Sunwell did not fall within the aforementioned activities as specified in the M&A Rules, and have been duly approved by the local MOFCOM pursuant to Interim Provisions Regarding Mergers and Acquisitions of Domestic Enterprises by Foreign Investor* (外商投資企業投資者股權變更的若干規定), accordingly, the M&A Rules are not applicable to the aforesaid acquisitions.

Our PRC legal advisers, King & Wood, have advised us that all material approvals or permits required under PRC laws and regulations in connection with each stage of the Reorganisation and the Listing of our Company have been obtained.

## CORPORATE AND SHAREHOLDING STRUCTURE OF OUR GROUP IMMEDIATELY BEFORE COMPLETION OF THE GLOBAL OFFERING

The following diagram sets out the shareholding structure of our Group immediately after the Reorganisation and immediately before completion of the Global Offering:




*Note 1:* Mr Ke Jixiong, an executive director, is the son of Mr Ke and Ms Cai Lishuang, and the brother to Ms Ke Jinzhen and Ms Ke Jinzhi.

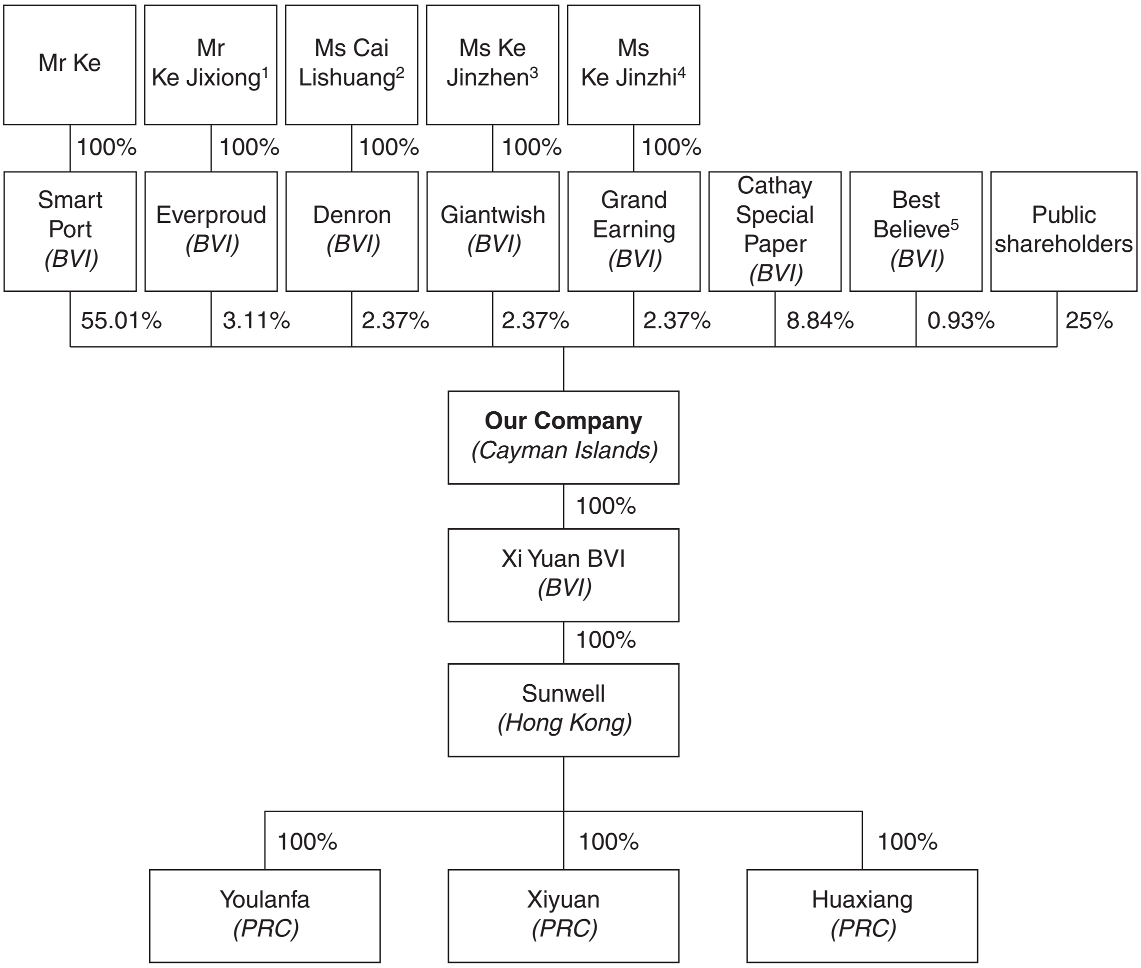
*Note 2:* Ms Cai Lishuang is the spouse of Mr Ke and the mother of Mr Ke Jixiong, Ms Ke Jinzhen and Ms Ke Jinzhi.

*Note 3:* Ms Ke Jinzhen is a daughter of Mr Ke and Ms Cai Lishuang, and the sister of Mr Ke Jixiong and Ms Ke Jinzhi.

*Note 4:* Ms Ke Jinzhi is a daughter of Mr Ke and Ms Cai Lishuang, and the sister of Mr Ke Jixiong and Ms Ke Jinzhen.

## CORPORATE AND SHAREHOLDING STRUCTURE OF OUR GROUP UPON COMPLETION OF THE GLOBAL OFFERING

The following diagram sets out the shareholding structure of our Group after the Reorganisation and immediately after the Global Offering and the Capitalisation Issue, and assuming the Over-allotment Option is not exercised:




*Note 1:* Mr Ke Jixiong, an executive director, is the son of Mr Ke and Ms Cai Lishuang, and the brother to Ms Ke Jinzhen and Ms Ke Jinzhi.

*Note 2:* Ms Cai Lishuang is the spouse of Mr Ke and the mother of Mr Ke Jixiong, Ms Ke Jinzhen and Ms Ke Jinzhi.

*Note 3:* Ms Ke Jinzhen is a daughter of Mr Ke and Ms Cai Lishuang, and the sister of Mr Ke Jixiong and Ms Ke Jinzhi.

*Note 4:* Ms Ke Jinzhi is a daughter of Mr Ke and Ms Cai Lishuang, and the sister of Mr Ke Jixiong and Ms Ke Jinzhen.

*Note 5:* The Shares held by Best Believe will be treated as part of the public float.

## THE CORPORATE PLACING

As part of the International Offering, we and the Sole Bookrunner have entered into a placing agreement with SD Family Fund L.P., or the Corporate Investor, for the subscription by the Corporate Investor at the offer price of the Global Offering with an aggregate subscription amount of approximately HK$120.0 million, or the Corporate Placing. Assuming an offer price of HK$2.98, being the mid-point of the price range set out in this prospectus, the total number of Offer Shares (rounded down to the nearest whole board lot of 1,000 shares) subscribed by the Corporate Investor would be 40,268,000, which represents approximately 4.0% of the Shares outstanding immediately following the completion of the Global Offering and approximately 16.1% of the Offer Shares, in each case, assuming that the Over-allotment Option for the Global Offering is not exercised.

SD Family Fund L.P. is a Cayman Islands exempted limited partnership established by the family trusts of Mr Hui Lin Chit and his family members. Mr Hui Lin Chit is the Deputy Chairman and Chief Executive Officer of Hengan International Group Company Limited (1044.HK), a company listed on the Main Board.

The Corporate Investor, their limited partners and respective beneficial owners are Independent Third Parties. Neither the Corporate Investor nor its beneficial owners will subscribe for any Offer Shares under the Global Offering other than pursuant to the placing agreement. The Corporate Investor will not have any board representation in the Company, nor will the Corporate Investor become a substantial shareholder of the Company immediately following the completion of the Global Offering. The Offer Shares to be subscribed for and by the Corporate Investor will not be affected by any reallocation of the Offer Shares between the International Offering and the Hong Kong Public Offering in the event of oversubscription under the Hong Kong Public Offering as described in "Structure of the Global Offering — The Hong Kong Public Offering" in this prospectus. The number of Offer Shares allocated to the Corporate Investor pursuant to the placing agreement will be disclosed in the allocation result announcement which is expected to be published on 26 May 2010. The Offer Shares to be held by the Corporate Investor will be regarded as part of the public float of the Company for the purpose of Rule 8.08 of the Listing Rules.

## CONDITIONS PRECEDENT

The subscription obligation of the Corporate Investor is conditional upon, among others, (i) the Hong Kong Underwriting Agreement and International Underwriting Agreement being entered into and having become effective and unconditional by no later than the date and time as specified in those agreements; (ii) none of the underwriting agreements mentioned in (i) above having been terminated; and (iii) the Listing Committee of the Stock Exchange having granted the listing of, and permission to deal in, the Offer Shares.

## RESTRICTIONS ON DISPOSAL BY THE CORPORATE INVESTOR

The Corporate Investor has agreed that, without the prior written consent of us and the Sole Bookrunner, it will not, whether directly or indirectly, at any time during the period of six months following the Listing Date, or the Lock-up Period, dispose of any of the Offer Shares subscribed pursuant to the Corporate Placing or any interest in any of its associates holding any of the Offer Shares subscribed pursuant to the Corporate Placing. The Corporate Investor may transfer the Offer Shares so subscribed in certain limited circumstances, such as transfer to a wholly-owned subsidiary and any such transfer can only be made when the transferee agrees to be subject to the restrictions on disposal imposed on the Corporate Investor.

## OVERVIEW

We are a leading wrapping tissue paper manufacturer in the PRC. We were the largest among the major wrapping tissue paper manufacturers by production output in 2008 and achieved approximately 14.0% and 5.3% market share by production output for MF tissue paper and wrapping tissue paper, respectively, within the PRC, according to the China Paper Association. MF tissue paper makes up a small part of the paper and paperboard products industry, falling within the tissue paper sub-category of the packaging paper segment. According to a report issued by the China Paper Association regarding domestic PRC production output of the paper and paperboard products industry in 2008, MF tissue paper accounted for approximately 37.5% of the entire wrapping tissue paper segment, which in turn, accounted for approximately 21.4% of the total packaging paper segment, which in turn, accounted for approximately 7.0% of the total paper and paperboard products industry.

We were also recognised by the China Paper Association as one of the Top 30 Pulp and Paper-making Enterprises in the PRC in 2008* (2008年度全國制漿造紙30強企業). Our principal products include double-sided and single-sided MF tissue paper with basis weights of less than $40g/m^2$ which are commonly used to wrap and cushion clothing, footwear, fruit and other consumer products. We also manufacture copy paper. We market our MF tissue paper under the brand and our copy paper under the "Scholar* (大學士學)", "Young Scholar* (小秀才秀)" and "Prodigy* (小神童神)" brands. We also commenced production of paper towels and ivory boards in January and April 2010, respectively.

Our head office is located at Xibin Industrial Zone, Jinjiang City, Fujian Province, the PRC. We have comprehensive and advanced production facilities with a large production capacity in Fujian Province, the PRC. We operate three factories: Youlanfa Factory and Huaxiang Factory, both of which are located in Jinjiang, and Xiyuan Factory, which is located in Longhai. All of our production sites are in close proximity to Xiamen Port and well-developed railway and highway transportation networks. As of 31 December 2009, we operated 16 production lines with an aggregate annual production capacity of approximately 124,440 tonnes.[1] We also have an in-house de-inking facility at our Huaxiang Factory with an annual design production capacity of 34,000 tonnes. We have our own water supply system at our Xiyuan Factory, and all of our factories have coal-fire boiler plants and wastewater treatment plants. According to the China Paper Association, most of the wrapping tissue paper manufacturers in the PRC purchase pulp from the market with only a few producing their own pulp. In recent years, some PRC manufacturers have begun to use de-inked pulp made from recovered paper in their production of wrapping tissue paper to reduce production costs and strengthen competitiveness. We are one such paper manufacturer in the PRC capable of making de-inked pulp suitable for the production of wrapping tissue paper. To capitalise on the growing demand for wrapping tissue paper, household paper and office

*Note 1:* The annual production capacity is estimated by our Directors based on the basis weight per sheet of our products and the maximum operation speed achievable when producing such products. The annual production capacity is calculated on the presumption that each paper machine operates 340 days per year.

Our production capacity is different from the design production capacity estimated by the manufacturers of our paper machines because the latter is determined with reference to the average basis weight of products each paper machine can produce. Our products carry a lighter basis weight per sheet compared to the average basis weight contemplated by the manufacturers of our paper machines when they estimated the design production capacity. As a result, when running at the same speed, our paper machines produce fewer tonnes of paper. For additional information on our paper machines, please refer to "Production — Production facilities" and "Property, Plant and Equipment — Production equipment" in this section.

paper in the PRC, we have purchased and installed one paper towel production line, one ivory board production line and two single-sided MF tissue paper production lines in 2010, all of which commenced production before the Latest Practicable Date, and we plan to add another nine paper production lines by the end of 2012. We expect these 13 new paper production lines will increase our maximum annual production capacity by 209,250 tonnes. For additional information on our new paper production lines, please refer to “Production — Production facilities” in this section.

We have a highly skilled and experienced production team. As of the Latest Practicable Date, our production team was comprised of more than 1,000 personnel led by approximately 20 experienced managerial and executive level personnel.

We have established an extensive sales and marketing network across the PRC, adopting a strategic regional distribution system pursuant to which we sell to regional distributors who either directly on-sell our products to, or further process our products in accordance with the specifications of the end-users. These end-users include clothing, footwear, hardware manufacturers or retailers, fruit growers and wine retailers. We have designated six sales regions in the PRC, based on the geographical concentration of our customers, to facilitate the management of our sales and marketing activities. As of 31 December 2009, we had 98 customers who were regional distributors, located primarily in Fujian Province, the Yangtze River Delta region and the Pearl River Delta region. Our sales activities are therefore concentrated in the East China and South China regions.

We are committed to enhancing production innovation and production efficiency through research and development. We have established technology exchange and cooperation programmes with four research and education facilities. In recognition of our research and development efforts and our market position, we have been invited by the China Standardisation Technical Committee for Paper Making Industry* (全國造紙工業標準化技術委員會) to participate in the drafting of industry standard specifications for wrapping tissue paper and semi-transparent paper, a type of double-sided MF tissue paper. In 2008, the Fujian Provincial Department of Science and Technology* (福建省科學技術廳) established the Paper-making Technology Development Base of Fujian Province* (福建省紙業技術開發基地) at our research and development centre and in 2009, Quanzhou Municipal Department of Science and Technology* (泉州市科學技術局) recognised our ultra-thin single-sided MF tissue paper product as a technologically advanced product. Youlanfa has applied to the Fujian Provincial Department of Science and Technology* (福建省科學技術廳) for a “High and New Technology Enterprises Certificate* (高新技術企業認定證書)”, which upon receipt would allow Youlanfa to enjoy a reduced PRC enterprise income tax rate. We expect to obtain such certificate by August 2010.

We place strong emphasis on environmentally responsible practices in all aspects of our operations and have endeavored to increase our use of de-inked pulp, reclaimed pulp and recycled white paper and to reduce our reliance on wood pulp in our production process. In particular, Youlanfa obtained ISO 14001 certification for our environmental management standards in 2002. We have met or exceeded the relevant standards under the PRC environmental laws and regulations.

We have achieved significant growth during the Track Record Period. For the three years ended 31 December 2009, our revenue was RMB267.6 million, RMB562.0 million and RMB724.8 million, respectively, representing a CAGR of 64.6%. Our profits for the same periods were RMB42.3 million, RMB132.6 million and RMB170.7 million, respectively, representing a CAGR of 100.9%.

## COMPETITIVE STRENGTHS

### We are a leading wrapping tissue paper manufacturer in the PRC and are well-positioned to capture future opportunities

We are a leading wrapping tissue paper manufacturer in the PRC. We were the largest among the major wrapping tissue paper manufacturers by production output in 2008 and achieved approximately 14.0% and 5.3% market share by production output for MF tissue paper and wrapping tissue paper, respectively, within the PRC, according to the China Paper Association. MF tissue paper makes up a small part of the paper and paperboard industry, falling within the tissue paper sub-category of the packaging paper segment. According to a report issued by the China Paper Association regarding domestic PRC production output of the paper and paperboard products industry in 2008, MF tissue paper accounted for approximately 37.5% of the entire wrapping tissue paper segment, which in turn, accounted for approximately 21.4% of the total packaging paper segment, which in turn, accounted for approximately 7.0% of the total paper and paperboard products industry.

For the year ended 31 December 2009, our Group had an annualised production output of approximately 92,274 tonnes of MF tissue paper, comprised of approximately 65,347 tonnes of double-sided MF tissue paper and approximately 26,927 tonnes of single-sided MF tissue paper. In addition to wrapping tissue paper, we also had an annualised production output of approximately 13,677 tonnes of copy paper for the year ended 31 December 2009. We have also commenced production of paper towels and ivory boards in January and April 2010, respectively. The China Paper Association recognised us as one of the Top 30 Pulp and Paper-making Enterprises in the PRC in 2008* (2008年度全國制漿造紙30強企業).

We have comprehensive and advanced production facilities with a large production capacity which allow us to take advantage of economies of scale and achieve a competitive cost profile. As of 31 December 2009, our production facilities, located at our Youlanfa, Huaxiang and Xiyuan Factories with an aggregate gross floor area of approximately 64,050.0 sq.m., housed 16 production lines with an aggregate annual production capacity of approximately 124,440 tonnes.[1] According to the China Paper Association, most PRC wrapping tissue paper manufacturers are equipped with machines that run at less than 100 metres per minute, with the more advanced PRC machines running at 200 to 300 metres per minute. Our MF tissue paper machines have operation speeds between 320 and 350 metres per minute so are able to produce more paper during the same time period than the machines used by our competitors, thereby enhancing our production efficiency and lowering our per unit costs. We also possess supporting facilities including a de-inking facility, coal-fired boilers and water treatment plants that further reduce our costs in relation to pulp, steam and water. Please refer to "Production" in this section for more details on our production and supporting facilities.

---

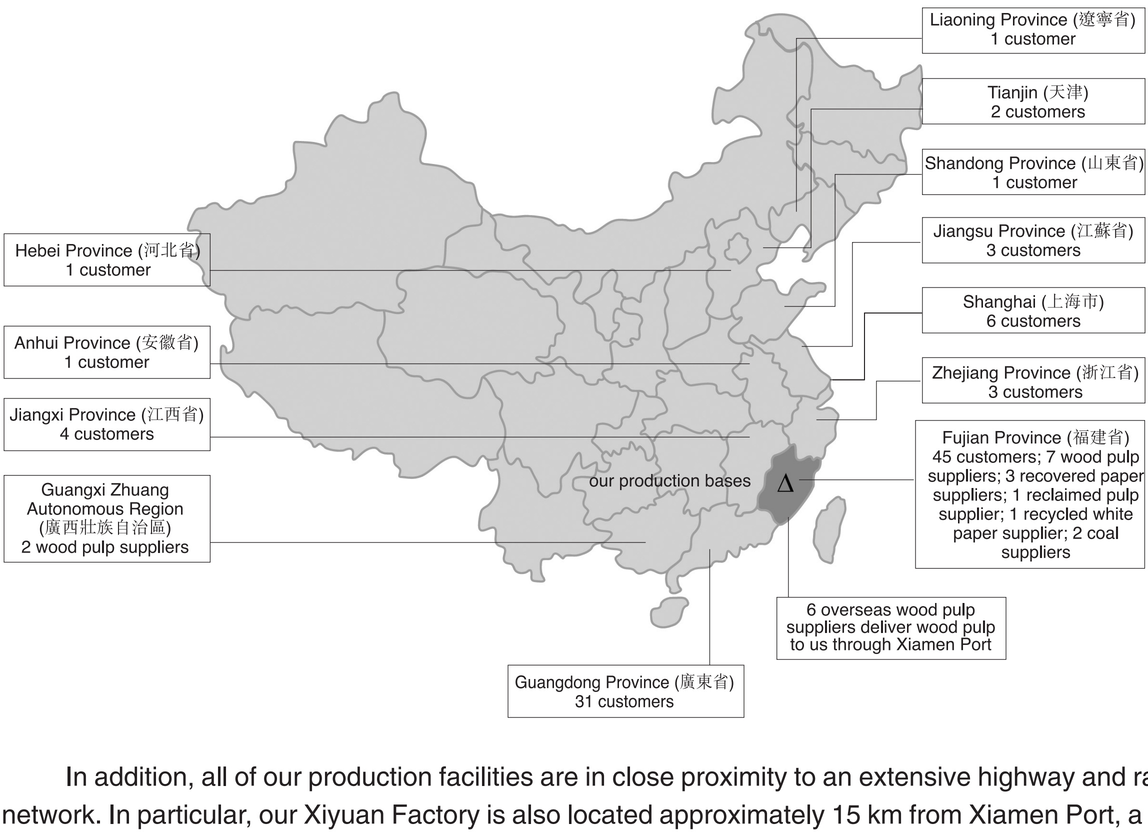
*Note 1:* The annual production capacity is estimated by our Directors based on the basis weight per sheet of our products and the maximum operation speed achievable when producing such products. The annual production capacity is calculated on the presumption that each paper machine operates 340 days per year.

Our production capacity is different from the design production capacity estimated by the manufacturers of our paper machines because the latter is determined with reference to the average basis weight of products each paper machine can produce. Our products carry a lighter basis weight per sheet compared to the average basis weight contemplated by the manufacturers of our paper machines when they estimated the design production capacity. As a result, when running at the same speed, our paper machines produce fewer tonnes of paper. For additional information on our paper machines, please refer to "Production — Production facilities" and "Property, Plant and Equipment — Production equipment" in this section.

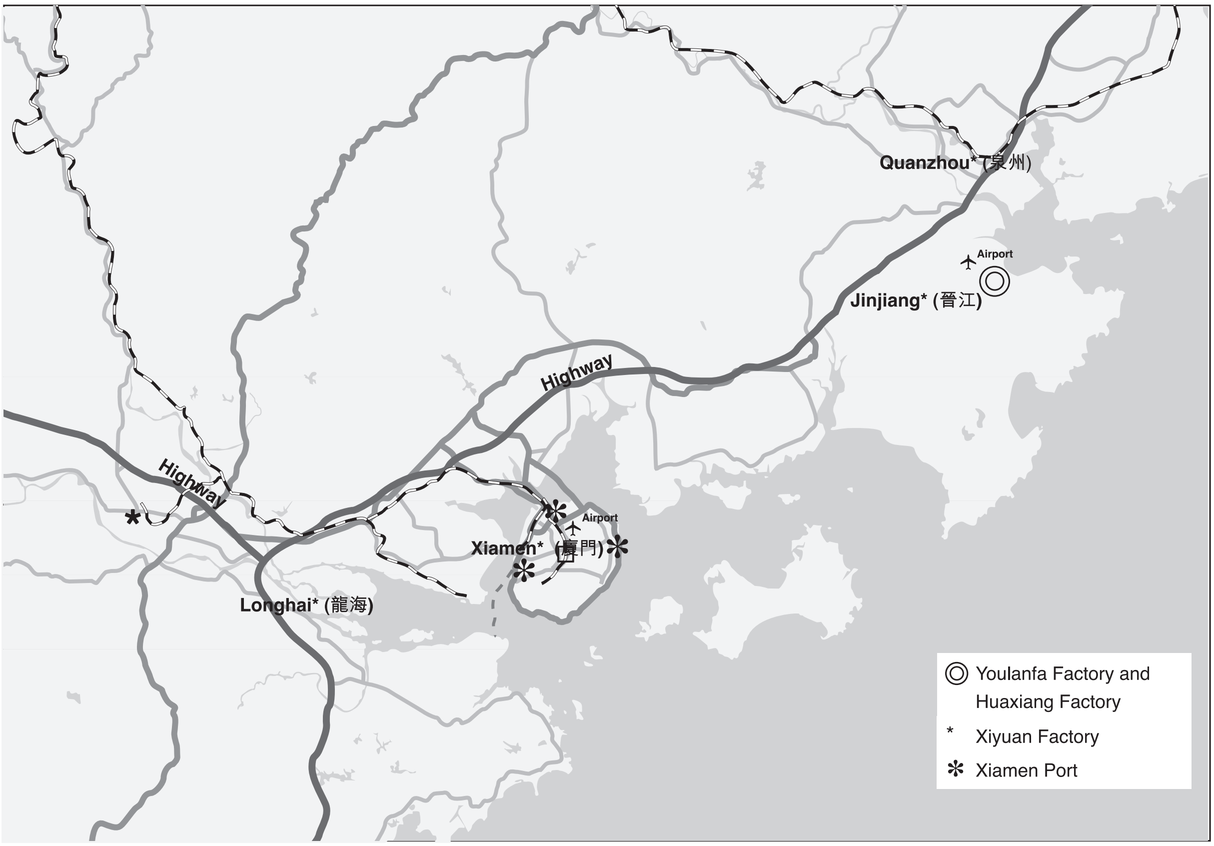
Moreover, in light of the PRC government's prohibition against the production, sale and use of ultra-thin plastic bags, we expect the demand for our products to increase as our wrapping tissue paper can serve as one of the main alternatives to plastic packaging and wrapping materials for goods such as clothing, footwear and fruit. Accordingly, we believe that we are well-positioned to capitalise on our leading market position as well as strong production capability to capture the expected continuous growth of the wrapping tissue paper market in the PRC.

**We benefit from close proximity to our customers, transportation hubs and water resources**

Our Youlanfa, Huaxiang and Xiyuan Factories are all located in Fujian Province, which is close to both the Pearl River Delta and Yangtze River Delta regions. These two regions are major manufacturing and export hubs for the PRC. A substantial majority of our customers are also located in these two regions and Fujian Province. Our proximity to our customers allows us to effectively minimise production lead-times for our goods to reach our customers. It also helps distinguish us as a more cost-effective supplier by lowering the transportation cost for our customers, who are responsible for arranging delivery of their purchased goods from our productions sites. The following diagram shows the location of all our customers, our raw material suppliers and our production bases as of 31 December 2009.




In addition, all of our production facilities are in close proximity to an extensive highway and railway network. In particular, our Xiyuan Factory is also located approximately 15 km from Xiamen Port, a major metropolitan shipping port on the south coast of Fujian Province and one of the main ports in the PRC, enabling us to utilise waterway transportation. As our suppliers transport our raw materials mainly by road and sea freight, the strategic proximity of our production facilities to a transportation network minimises delivery time and cost. Our close proximity to Xiamen Port allows us to save on transportation costs when we purchase wood pulp and recovered paper from overseas, which has, from time to time, been a cheaper source of these principal raw materials. We expect our strategic location and lower transportation costs may also benefit us in the event we export our products in the future. The following diagram shows the location of our production bases and the nearby highway and railway network and the location of Xiamen Port.




Further, water is a crucial resource in the production of paper and accordingly we require large and reliable supplies of water for our operations. The strategic location of our Xiyuan Factory provides us with immediate and inexpensive access to an abundant and reliable water supply from the adjacent Jiulong River and in turn helps us save on production costs.

**We have secured sources of high quality and price competitive raw materials**

Pulp is the principal raw material used in the production of our products. In addition to wood pulp, we use de-inked pulp, reclaimed pulp and recycled white paper to achieve greater cost-savings as well as to meet environmental objectives.

According to the China Paper Association, most of the wrapping tissue paper manufacturers in the PRC purchase pulp with only a few producing their own pulp. In recent years, some PRC manufacturers have begun to use de-inked pulp made from recovered paper in their production of wrapping tissue paper to reduce production costs and strengthen competitiveness. We are one such paper manufacturer capable of making de-inked pulp suitable for the production of wrapping tissue paper. We have produced de-inked pulp in-house since 2007 at our Huaxiang Factory where we remove printing ink and colour from recovered paper primarily originating from Australia and Japan, where paper recycling systems are well-established to gather quality recovered paper. For our cost of sales for the three years ended 31 December 2009, the cost of our de-inked pulp per tonne was approximately 41.0%, 35.9% and 34.3% lower than that of our wood pulp, respectively, and de-inked pulp represented approximately 4.6%, 15.0% and 11.7% of our total cost of sales, respectively. As of the Latest Practicable Date, we had one de-inking facility at our Huaxiang Factory with an annual production capacity of 34,000 tonnes of de-inked pulp. We plan to add two de-inking facilities with an annual capacity of 160,000 tonnes of de-inked pulp by the end of 2012 to support our future production expansion.

We source reclaimed pulp from an independent Xiamen-based recycling company with technology to produce reclaimed pulp using milkboxes and other packaging boxes. For our cost of sales for the three years ended 31 December 2009, the cost of our reclaimed pulp per tonne was approximately 39.1%, 41.3% and 33.9% lower than that of our wood pulp, respectively, and reclaimed pulp represented approximately 26.2%, 21.5% and 12.4% of our total cost of sales, respectively. We use reclaimed pulp in our production process to further lower our average pulp cost. To ensure a stable supply of quality reclaimed pulp in the future, we renewed our exclusive supply agreement with our reclaimed pulp supplier in 2009 for a term of three years for priority allocation of its reclaimed pulp.

We source recycled white paper from one supplier in Fujian Province. For our cost of sales for the three years ended 31 December 2009, the cost of our recycled white paper per tonne was approximately 46.9%, 58.2% and 43.5% lower than that of our wood pulp, respectively, and recycled white paper represented approximately 0.1%, 0.4% and 5.4% of our total cost of sales, respectively. Since recycled white paper is widely available from recycling companies, alternative suppliers are readily available in the market.

Our ability to substitute one type of pulp for another to a certain extent without compromising the quality of our products helps us reduce the impact of raw material price fluctuations and offers price stability to our customers. This has contributed to our competitiveness as a leader in the PRC MF tissue paper market. Please refer to "Procurement of Raw Materials" in this section for more details.

**We have distinguished research and development capabilities**

We are committed to enhancing product innovation and production efficiency through research and development, which is undertaken at our technology development centre located in our Huaxiang Factory. Unlike some research-intensive companies, which invest heavily in capital intensive research and development facilities and equipment in developing products and technology, our research and development activities focus on development of paper products and the improvement of our production process to enhance production efficiency and reduce production costs, which do not require large scale facilities and equipment or substantial expenses on materials.

Semi-transparent paper, a type of double-sided MF tissue paper is a product which we developed in-house and thereafter commenced production of in 2009. During the same year, the ultra-thin single-sided MF tissue paper developed by us received recognition from the Quanzhou Municipal Development of Science and Technology* (泉州市科學技術局) as a technologically advanced product. We recently developed the process and techniques for producing paper towels and ivory boards, of which we commenced production in January and April 2010, respectively. We are currently developing food wrapping paper products which are proposed to be launched in September 2010.

Apart from developing new products, our research and development department also undertakes raw materials testing to control our product quality and to lower our production costs. Based on our laboratory testing results, we managed to use bagasse pulp in our production of semi-transparent paper to increase the transparency of the final product and to also reduce the raw material costs. We have also managed to increase the maximum percentage of de-inked pulp and reclaimed pulp that we use in our production, which has further reduced our costs. In order to improve our operational efficiency, our research and development department also makes modifications to our facilities to enhance product consistency and production output. As of 31 December 2009, we had registered five patents relating to the treatment of wastewater, modification of our paper machines and our production process.

In recognition of our research and development efforts and our market position, we have been invited by the China Standardisation Technical Committee for Paper Making Industry* (全國造紙工業標準化技術委員會) to participate in the drafting of industry standard specifications for wrapping tissue paper and semi-transparent paper. Moreover, the Fujian Provincial Department of Science and Technology* (福建省科學技術廳) established the Paper-making Technology Development Base of Fujian Province* (福建省紙業技術開發基地) at our research and development centre in 2008, which has served as a platform for collaboration with experts and academic institutions. Youlanfa has applied to the Fujian Provincial Department of Science and Technology* (福建省科學技術廳) for a "High and New Technology Enterprises Certificate* (高新技術企業認定證書)", which upon receipt would allow Youlanfa to enjoy a reduced PRC enterprise income tax rate. We expect to obtain such certificate by August 2010. We believe that our commitment to research and development helps to keep us abreast of the latest developments in production technology, thus ensuring that we remain competitive in the industry.

We have established a research and development committee consisting of six members, most of whom are technical and managerial personnel from our major departments such as production and sales. The committee is further assisted by a team comprised of three technicians and 15 staff from different departments which is in charge of implementing the research plans. We have also established technology exchange and cooperation programmes with four research and education institutions. For the three years ended 31 December 2009, our research and development expenses were approximately RMB0.1 million, RMB0.2 million and RMB0.4 million, respectively.

**We are committed to environmentally responsible practices**

We place strong emphasis on environmentally responsible practices in all aspects of our operations. In 2008, we were awarded as a Top 10 Environmentally Friendly Paper-making Enterprise of Fujian Province* (福建省造紙行業環境友好型十佳企業) by the Paper Association of Fujian Province* (福建省造紙行業協會). Youlanfa obtained ISO 14001 certification for our environmental management standards in 2002. We have met or exceeded the relevant standards under the PRC environmental laws and regulations, and we believe that our history of compliance will help expedite additional required regulatory approvals necessary for our future production capacity expansion. We have used de-inked pulp, reclaimed pulp and recycled white paper, which together accounted for approximately 30.9%, 36.9% and 29.5% of our total cost of sales for the three years ended 31 December 2009, respectively, which helped to reduce our impact on forest resources. To minimise our impact on water resources, we have installed water recycling and conservation systems and wastewater treatment facilities at each of our factories to substantially reduce our water consumption. These systems allow us to conserve water and recycle pulp debris in white water generated from production, thereby reducing both the amount of waste materials generated and raw materials required by our manufacturing processes. Please refer to "Environmental Matters" in this section for more details.

**We have an experienced management team and a highly skilled workforce**

We have an experienced management team with solid industry knowledge, extensive operational experience and a proven track record of generating rapid growth for our Group. More notably, our founding shareholder and Chairman Mr Ke was recognised by the China Paper Association as an Outstanding Entrepreneur in the Field of Pulp and Paper Making for the Year of 2008* (2008年度全國製漿造紙行業優秀企業家). He was also named a Model Entrepreneur in the Light Industry Segment* (全國輕工行業勞動模範) in 2007 by the Ministry of Personnel of the PRC* (中華人民共和國人事部), China National Light Industry Council (中國輕工業聯合會) and All China Federation of Handicraft Industrial Cooperatives (中華全國手工業合作總社). Together with Mr Ke, Mr Cao Xu (曹旭), Mr Zhang Guoduan (張國端), Mr Ke Jixiong and the rest of our management team have guided us through our rapid growth and expansion. Our Group has also retained Mr Wong Yat Sum (黃一心) who holds professional qualifications in Hong Kong to comprise part of our senior management team. With an average of over 14 years of experience in the paper making industry, our management team is able to identify and pursue market opportunities and formulate and implement development strategies effectively.

We also have a highly skilled and experienced production team. As of the Latest Practicable Date, our Group had a production team comprised of more than 1,000 personnel led by a team of approximately 20 experienced managerial and executive level personnel in the production department. Through our management and employees' efforts to implement national best practices, we have become a leading wrapping tissue paper manufacturer in the PRC.

**BUSINESS STRATEGIES**

We aim to maintain our position as a leading manufacturer of wrapping tissue paper products in the PRC. We will continue to seek opportunities to realise sustainable growth of our business and increase shareholder value. To achieve this, we plan to focus on the following strategies:

**Continue to expand our production capacity to maintain our market leadership position in the PRC**

We seek to maintain our leadership position and grow our market share in the PRC by continuing to expand our production capacity. As of the Latest Practicable Date, we have added four paper production lines in 2010 and plan to add another nine paper production lines by the end of 2012. These 13 new production lines include nine MF tissue paper production lines (of which two are for the manufacture of food wrapping paper), one copy paper production line, two paper towel production lines and one ivory board production line. For further information on our expansion plans please refer to "Production — Production facilities" in this section.

Considering that a single-sided MF tissue paper production line is expected to commence operation in August 2012 and given its utilisation rate will be low during the trial period, our Directors expect our production output of MF tissue paper for the year ending 31 December 2012 to be approximately 207,000 tonnes. In 2008, the PRC produced approximately 450,000 tonnes of MF tissue paper and the growth of wrapping tissue paper consumption in the PRC is expected to continue at a rate of approximately 8% per annum, according to a report prepared by the China Paper Association. Assuming MF tissue paper production output in the PRC grows at the same rate, it will reach approximately 612,000 tonnes in 2012. Comparing our expected production output of MF tissue paper and the expected total production output MF tissue paper in the PRC in 2012, we will achieve approximately 33.8% market share for MF tissue paper by production output within the PRC.

We acquired 19 parcels of land in Jinjiang and Longhai in 2009. As of the Latest Practicable Date, we possess approximately 324,245.3 sq.m. of land in Jinjiang and Longhai to support our future capacity expansion.

**Expand and diversify product offerings**

Our Group is actively exploring opportunities to diversify our product lines to offer a broader range of products to our customers. We plan to achieve this by both diversifying our existing wrapping tissue paper products to include higher profit margin products, such as coloured single-sided MF tissue paper and food wrapping paper, a type of double-sided MF tissue paper, and developing new paper products such as paper towels and ivory boards, all of which can be readily produced from the same raw materials we use in making our wrapping tissue paper. Our research and development department has already developed the process and techniques for producing paper towels and ivory boards and we commenced production of them in January and April 2010, respectively. We believe that these new product lines will allow us to enter new high-growth domestic markets and increase our profit margins, as well as raise consumer awareness of our “Youlanfa” brand. To achieve this end, we plan to leverage our existing production expertise and distribution network and further improve our research and development capabilities.

**Enhance supporting facilities to support our future production expansion**

In order to ensure an effective implementation of our expansion plans and continuous improvement of our production efficiency, we intend to upgrade our supporting facilities. We currently plan to construct a cogeneration plant at our Xiyuan Factory, which upon completion will significantly reduce our Xiyuan Factory’s reliance on local utilities for the supply of electricity. We also plan to add two de-inking facilities with an aggregate annual capacity of 160,000 tonnes of de-inked pulp by the end of 2012, with one at our Xiyuan Factory and the other at our Huaxiang Factory. We intend to utilise the added capacity to meet our increasing demand for de-inked pulp, gradually replacing reclaimed pulp with de-inked pulp and reducing the percentage of wood pulp we use in our production, thereby further lowering our production costs. We also plan to install facilities to produce blue top linerboards, the packaging materials we use to pack our own products.

**Enhance the brand awareness of our wrapping tissue paper products marketed under the “Youlanfa” trademark**

All of our wrapping tissue paper products are marketed under the “Youlanfa” trademark. We recognise the importance of developing public awareness of our brand and corporate image under the “Youlanfa” trademark, and of cultivating customer loyalty among not only our regional distributor customers but also the end-users. Currently, we market our products through outdoor billboards in Fujian Province and on our website at www.youyuan.com.hk. To enhance brand awareness, we are in the process of registering our "Youlanfa" trademark as a "Famous Trademark of China* (中國馳名商標)". We also plan to increase advertising and promotional activities of our products under the "Youlanfa" trademark. We intend to maintain our reputation as a premium wrapping tissue paper manufacturer by consistently improving the quality of our products.

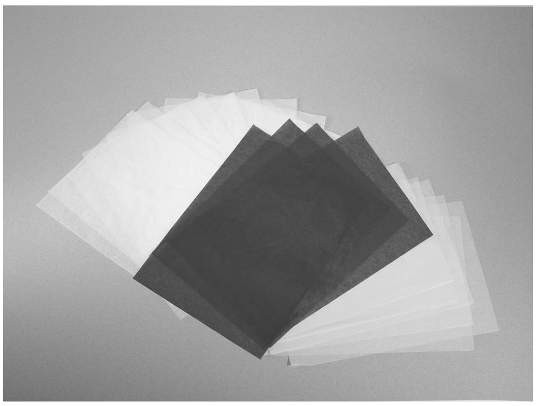
We believe that enhancing the brand awareness of our "Youlanfa" trademark will allow us to expand our customer base and increase our geographic coverage, as well as increase the future sales of our new products to existing customers. We plan to promote our products in regions such as Western China and Central China, where demand for packing materials has increased due to the local economic development. We intend to increase the number of sales personnel we employ and engage more distributors in those targeted regions. We also intend to strengthen the training that we provide to both sales personnel and customers in order to better familiarise them with our products.

## PRODUCTS

Our Group manufactures MF tissue paper, including double-sided MF tissue paper and single-sided MF tissue paper, and copy paper. We also commenced production of paper towels and ivory boards in January and April 2010, respectively.

The following is a brief description of our products:

- **Wrapping Tissue Paper.** We produce double-sided and single-sided MF tissue paper, both of which are wrapping tissue paper. Wrapping tissue paper is a thin, translucent paper with a basis weight of less than $40g/m^2$ and primarily used for wrapping and cushioning goods. Both our double-sided and single-sided MF tissue paper are commonly used to wrap clothing, footwear, fruit and other consumer products. They may also be used to wrap delicate merchandise in folded or crumpled layers to protect the merchandise before being placed into bags or boxes. Our wrapping tissue paper is marketed under our "Youlanfa" brand and is offered in various sizes according to customer specifications.



— double-sided MF tissue paper usually has a basis weight of 17 $g/m^2$. We have also developed semi-transparent paper in white and red colours as a special type of double-sided MF tissue paper primarily used for packaging fruit and clothes. Double-sided MF tissue paper constitutes our biggest product category by production capacity and sales volume. In order to meet the market demand, we also plan to launch food wrapping paper, another type of semi-transparent paper, in 2010.

— single-sided MF tissue paper usually has a basis weight of 14 g/m$^2$. Unlike double-sided MF tissue paper, it has a smooth glazed side and a rough back side. We plan to launch coloured single-sided MF tissue paper by the end of 2010.

- **Copy paper.** Copy paper usually has a basis weight of 70 g/m$^2$ and is used in photocopiers and computer printers. We market our copy paper in six different sizes under our "Scholar* (大學士學)", "Young Scholar* (小秀才秀)" and "Prodigy* (小神童神)" brands.


The following table sets forth our revenue, sales volume and average sales prices for our products for the periods indicated.

| | Year ended 31 December | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2007 | | | 2008 | | | 2009 | | |
| | Revenue | Sales volume | Average sales price | Revenue | Sales volume | Average sales price | Revenue | Sales volume | Average sales price |
| | (RMB in MN) | (tonnes) | (RMB/ tonne) | (RMB in MN) | (tonnes) | (RMB/ tonne) | (RMB in MN) | (tonnes) | (RMB/ tonne) |
| Double-sided MF tissue paper . . . | 147.9 | 18,697.2 | 7,909.7 | 299.4 | 38,079.2 | 7,863.6 | 470.4 | 65,848.3 | 7,144.1 |
| Single-sided MF tissue paper . . . | 46.0 | 6,878.4 | 6,693.3 | 171.5 | 24,754.4 | 6,926.0 | 168.6 | 26,845.2 | 6,280.8 |
| Copy paper . . . . . | 73.7 | 11,448.4 | 6,433.8 | 91.1 | 12,867.5 | 7,082.3 | 85.8 | 13,373.9 | 6,412.3 |
| Total . . . . . . . . . | 267.6 | 37,024.0 | | 562.0 | 75,701.1 | | 724.8 | 106,067.4 | |

Despite the global economic crisis in the second half of 2008, our product sales were not materially affected because domestic demand for wrapping tissue paper in the PRC market remained strong. For each of the two years ended 31 December 2009, our revenue increased by approximately RMB294 million and RMB163 million, respectively, which amounted to 110.0% and 29.0% growth, respectively, while we maintained relatively stable gross profit margins of 33.5% and 33.2%, respectively. The large increase in our revenue in 2008 resulted from the commencement of operation of six paper production lines in Huaxiang Factory in the second half of 2007, when our Huaxiang Factory was put into use and the commencement of operation of two paper production lines in Xiyuan Factory in 2008, when our Xiyuan Factory was put into use.

Our Group is actively exploring opportunities to diversify our product lines to offer a broader range of products. We have commenced production of paper towels and ivory boards since January and April 2010, respectively. Paper towels are a type of tissue paper made from absorbent paper rather than cloth, and are mostly used for hygienic and cleaning purposes. They usually have a basis weight between 30 $g/m^2$ and 45 $g/m^2$. Ivory boards are a type of highly finished cardboard that is sometimes clay-coated on one or both sides. They are mainly used for art printing, menu cards and price tags for clothing and other goods. They usually have a basis weight between 200 $g/m^2$ and 400 $g/m^2$.

Our research and development department is currently developing the process and techniques for producing food wrapping paper products, which are proposed to be completed in 2010. Food wrapping paper, which is a type of semi-transparent paper with higher hygienic requirements, usually has a basis weight between 24 $g/m^2$ and 28 $g/m^2$. We expect to launch production of food wrapping paper in September 2010.

## PRODUCTION

### Production Base

Our operations are based in Fujian Province, the PRC. We operate three production bases located in Jinjiang and Longhai. Our Youlanfa and Huaxiang Factories are located in Jinjiang, and our Xiyuan Factory is located in Longhai. All of our production sites are in close proximity to Xiamen Port and well-developed railway and highway transportation networks. We believe that our integrated operations, which combine paper production along with de-inked pulp and other supporting facilities, and our strategic location provide for significant production efficiencies.

## Production Facilities

As of 31 December 2009, our Group operated 16 paper production lines with an aggregate annual production capacity of 124,440 tonnes[1]. Of the 16 production lines, four are housed in our Youlanfa Factory, eight are in our Huaxiang Factory and the remaining four are in our Xiyuan Factory. According to the China Paper Association, the paper machines used to produce wrapping tissue paper in the PRC usually have maximum speeds below 100 metres per minute, with more advanced machines running at 200 to 300 metres per minute. Our MF tissue paper machines have operation speeds between 320 and 350 metres per minute, putting them amongst the most advanced in the PRC for the production of wrapping tissue paper.

The following table sets forth certain production data relating to our paper machines:

| Paper machine | Model | Product | Annual design capacity[2] (tonnes) | Annual production capacity[1] (tonnes) |
|---|---|---|---|---|
| PM1 (Youlanfa) | 1880/mm | double-sided MF tissue paper/ Semi-transparent paper | 5,780 | 5,100 |
| PM2 (Youlanfa) | 1880/mm | double-sided MF tissue paper/ Semi-transparent paper | 5,780 | 5,100 |
| PM3 (Youlanfa) | 2640/mm | double-sided MF tissue paper | 10,200 | 8,160 |
| PM4 (Youlanfa) | 2460/mm | copy paper | 17,000 | 13,600 |
| PM1 (Huaxiang) | 2640/mm | double-sided MF tissue paper | 10,200 | 8,160 |
| PM2 (Huaxiang) | 2640/mm | double-sided MF tissue paper | 10,200 | 8,160 |
| PM3 (Huaxiang) | 2640/mm | single-sided MF tissue paper | 10,200 | 6,800 |
| PM4 (Huaxiang) | 2640/mm | single-sided MF tissue paper | 10,200 | 6,800 |
| PM5 (Huaxiang) | 2640/mm | single-sided MF tissue paper | 10,200 | 6,800 |
| PM6 (Huaxiang) | 2640/mm | single-sided MF tissue paper | 10,200 | 6,800 |
| PM7 (Huaxiang) | 2640/mm | double-sided MF tissue paper | 10,200 | 8,160 |
| PM8 (Huaxiang) | 2640/mm | double-sided MF tissue paper | 10,200 | 8,160 |
| PM1 (Xiyuan) | 2640/mm | double-sided MF tissue paper | 10,200 | 8,160 |
| PM2 (Xiyuan) | 2640/mm | double-sided MF tissue paper | 10,200 | 8,160 |
| PM3 (Xiyuan) | 2640/mm | double-sided MF tissue paper | 10,200 | 8,160 |
| PM4 (Xiyuan) | 2640/mm | double-sided MF tissue paper | 10,200 | 8,160 |
| | | Total | 161,160 | 124,440 |

*Note 1:* The annual production capacity is estimated by our Directors based on the basis weight per sheet of our products and the maximum operation speed achievable when producing such products. The annual production capacity is calculated on the presumption that each paper machine operates 340 days per year.

*Note 2:* The annual design production capacity was calculated by multiplying 340 by the daily design production capacity estimated by the manufacturers of our paper machines with reference to the average basis weight of products each paper machine can produce. Our annual production capacity will differ from the annual design capacity because our products carry a lighter basis weight per sheet compared to the average basis weight contemplated by the manufacturers of our paper machines when they estimated the daily design production capacity. As a result, when running at the same speed, our paper machines produce fewer tonnes of paper.

For additional information on our paper machines, please refer to "Property, Plant and Equipment — Production equipment" in this section for more details.

To capitalise on the growing demand for wrapping tissue paper, household paper and office paper in the PRC, we have added four paper production lines in 2010 and plan to add another nine paper production lines by the end of 2012. The following table sets forth details, including their annual production capacity estimated by the Directors, of these 13 new paper production lines.

| No. | Location | Products | Planned annual production capacity | Planned/Actual* commencement of operation |
|---|---|---|---|---|
| | | | (tonnes) | |
| 1 | Youlanfa Factory | paper towels | 6,000 | January 2010* |
| 2 | Youlanfa Factory | ivory boards | 20,000 | April 2010* |
| 3 | Youlanfa Factory | coloured single-sided MF tissue paper | 4,000 | October 2010 |
| 4 | Youlanfa Factory | coloured single-sided MF tissue paper | 4,000 | November 2010 |
| 5 | Huaxiang Factory | paper towels | 8,250 | June 2010 |
| 6 | Huaxiang Factory | double-sided MF tissue paper | 25,000 | October 2011 |
| 7 | Huaxiang Factory | double-sided MF tissue paper | 30,000 | December 2011 |
| 8 | Huaxiang Factory | single-sided MF tissue paper | 50,000 | August 2012 |
| 9 | Xiyuan Factory | single-sided MF tissue paper | 9,000 | January 2010* |
| 10 | Xiyuan Factory | single-sided MF tissue paper | 9,000 | January 2010* |
| 11 | Xiyuan Factory | food wrapping paper | 7,000 | September 2010 |
| 12 | Xiyuan Factory | food wrapping paper | 7,000 | September 2010 |
| 13 | Xiyuan Factory | copy paper | 30,000 | September 2010 |
| | | Total | 209,250 | |

Of the above 13 new paper production lines, our Youlanfa Factory has purchased and installed one production line for the production of paper towels which has a design capacity of 25 tonnes per day and has a maximum design speed of 220 metres per minute. It can produce paper towels with a maximum paper width of 2.8 metres. Our Youlanfa Factory also purchased and installed one production line for the production of ivory boards which has a design capacity of 70 tonnes per day and has a maximum design speed of 380 metres per minute. It can produce ivory boards with a maximum paper width of 2.75 metres. Our Xiyuan Factory has purchased and installed two production lines for the production of single-sided MF tissue paper, each of which has a design capacity of 30 tonnes per day and a maximum design speed of 450 metres per minute. These single-sided MF tissue paper machines can produce tissue paper with a maximum paper width of 2.9 metres. Each of these paper towels, ivory boards and single-sided MF tissue paper production lines commenced production before the Latest Practicable Date.

Our production lines normally operate on a continuous and uninterrupted basis, except for temporary stoppages for machine cleaning, periodic inspection and maintenance work, which lasts for approximately 24 to 36 hours each month and annual maintenance which lasts for approximately one week. Please refer to "Property, Plant and Equipment — Maintenance of production equipment" in this section for more details. During the Track Record Period, there was no disruption to our business operations as a result of any malfunctioning of our production equipment.

We operated our wrapping tissue paper machines at speeds which we considered to be optimum during the Track Record Period and we do not believe we currently have the ability to increase such speeds significantly in the future.

The following table sets forth information on the utilisation rates of our production lines, which are determined by the actual running hours of our paper machines against the planned, or optimum, running hours, for the periods indicated.

| | Year ended 31 December | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2007 | | | 2008 | | | 2009 | | |
| | Equipment utilisation[1] | Actual hours of operation | Planned hours of operation[2] | Equipment utilisation[1] | Actual hours of operation | Planned hours of operation[2] | Equipment utilisation[1] | Actual hours of operation | Planned hours of operation[2] |
| | (%) | | | (%) | | | (%) | | |
| PM1(Youlanfa) | 102.6 | 8,376 | 8,160 | 101.2 | 8,256 | 8,160 | 99.4 | 8,112 | 8,160 |
| PM2 (Youlanfa) | 102.6 | 8,376 | 8,160 | 101.2 | 8,256 | 8,160 | 99.4 | 8,112 | 8,160 |
| PM3 (Youlanfa) | 102.6 | 8,376 | 8,160 | 101.2 | 8,256 | 8,160 | 99.4 | 8,112 | 8,160 |
| PM4 (Youlanfa) | 102.9 | 8,400 | 8,160 | 97.9 | 7,992 | 8,160 | 99.1 | 8,088 | 8,160 |
| PM1 (Huaxiang) | 85.0 | 2,040 | 2,400 | 97.6 | 7,968 | 8,160 | 99.1 | 8,088 | 8,160 |
| PM2 (Huaxiang) | 85.0 | 2,040 | 2,400 | 97.6 | 7,968 | 8,160 | 99.1 | 8,088 | 8,160 |
| PM3 (Huaxiang) | 87.5 | 2,952 | 3,372 | 99.1 | 8,088 | 8,160 | 98.8 | 8,064 | 8,160 |
| PM4 (Huaxiang) | 87.5 | 2,952 | 3,372 | 99.1 | 8,088 | 8,160 | 98.8 | 8,064 | 8,160 |
| PM5 (Huaxiang) | 101.2 | 4,032 | 3,984 | 99.7 | 8,136 | 8,160 | 99.1 | 8,088 | 8,160 |
| PM6 (Huaxiang) | 101.2 | 4,032 | 3,984 | 99.7 | 8,136 | 8,160 | 99.1 | 8,088 | 8,160 |
| PM7 (Huaxiang) | — | — | — | — | — | — | 90.5 | 2,520 | 2,784 |
| PM8 (Huaxiang) | — | — | — | — | — | — | 90.5 | 2,520 | 2,784 |
| PM1 (Xiyuan) | — | — | — | 97.2 | 4,536 | 4,668 | 98.2 | 8,016 | 8,160 |
| PM2 (Xiyuan) | — | — | — | 97.2 | 4,536 | 4,668 | 98.5 | 8,040 | 8,160 |
| PM3 (Xiyuan) | — | — | — | — | — | — | 97.9 | 7,296 | 7,452 |
| PM4 (Xiyuan) | — | — | — | — | — | — | 97.6 | 7,272 | 7,452 |

*Notes:*

1 Our utilisation rates remain fairly constant even during the trial period which is typically the first four months from commencement of operation, even though we may operate our machines at slower speeds, which is not reflected in the above utilisation rates.

2 Planned hours of operation takes into account, among others, planned maintenance shutdowns and shutdowns in connection with equipment optimisation.

The following table sets forth the capacity utilisation rates of our production lines, which are determined by the actual production output of our production lines against the annual production capacity for the periods indicated.

| | | | Year ended 31 December | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | 2007 | | 2008 | | 2009 | |
| | Commencement of operation | Annual production capacity[1] | Production output | Capacity utilisation[2] | Production output | Capacity utilisation[2] | Production output | Capacity utilisation[2] |
| | | (tonnes) | (tonnes) | (%) | (tonnes) | (%) | (tonnes) | (%) |
| PM1 (Youlanfa)[3] | Before 2007 | 5,100 | 4,746.1 | 93.1 | 4,673.7 | 91.6 | 4,488.9 | 88.0 |
| PM2 (Youlanfa)[3] | Before 2007 | 5,100 | 4,746.1 | 93.1 | 4,673.7 | 91.6 | 4,488.9 | 88.0 |
| PM3 (Youlanfa)[3] | Before 2007 | 8,160 | 7,708.4 | 94.5 | 7,606.1 | 93.2 | 7,214.8 | 88.4 |
| PM4 (Youlanfa) | Before 2007 | 13,600 | 11,603.1 | 85.3 | 13,271.7 | 97.6 | 13,677.4 | 100.6 |
| PM1 (Huaxiang)[4] | September 2007 | 8,160 | 824.1 | 30.3 | 7,252.7 | 88.9 | 7,996.9 | 98.0 |
| PM2 (Huaxiang)[4] | September 2007 | 8,160 | 723.4 | 26.6 | 7,453.2 | 91.3 | 7,933.9 | 97.2 |
| PM3 (Huaxiang)[4] | August 2007 | 6,800 | 1,903.3 | 67.2 | 6,080.9 | 89.4 | 6,437.9 | 94.7 |
| PM4 (Huaxiang)[4] | August 2007 | 6,800 | 1,633.4 | 57.6 | 6,123.8 | 90.1 | 7,040.7 | 103.5 |
| PM5 (Huaxiang)[4] | July 2007 | 6,800 | 2,045.1 | 60.2 | 6,154.5 | 90.5 | 6,768.7 | 99.5 |
| PM6 (Huaxiang)[4] | July 2007 | 6,800 | 1,884.2 | 55.4 | 6,238.7 | 91.7 | 6,679.5 | 98.2 |
| PM7 (Huaxiang)[4] | September 2009 | 8,160 | — | — | — | — | 1,955.5 | 71.9 |
| PM8 (Huaxiang)[4] | September 2009 | 8,160 | — | — | — | — | 1,963.5 | 72.2 |
| PM1 (Xiyuan)[4] | June 2008 | 8,160 | — | — | 3,667.4 | 77.0 | 7,828.4 | 95.9 |
| PM2 (Xiyuan)[4] | June 2008 | 8,160 | — | — | 3,627.9 | 76.2 | 7,856.2 | 96.3 |
| PM3 (Xiyuan)[4] | February 2009 | 8,160 | — | — | — | — | 6,822.6 | 91.2 |
| PM4 (Xiyuan)[4] | February 2009 | 8,160 | — | — | — | — | 6,797.4 | 90.9 |
| Subtotal of the production volume of double-sided MF tissue paper | | | 18,748.1 | | 38,954.7 | | 65,347.0 | |
| Subtotal of the production volume of single-sided MF tissue paper | | | 7,466.0 | | 24,597.9 | | 26,926.8 | |
| Subtotal of the production volume of copy paper | | | 11,603.1 | | 13,271.7 | | 13,677.4 | |
| Total | | 124,440 | 37,817.2 | | 76,824.3 | | 105,951.2 | |

*Note 1:* The annual production capacity is estimated by our Directors based on the basis weight per sheet of our products and the maximum operation speed achievable when producing such products. The annual production capacity is calculated on the presumption that each paper machine operates 340 days per year.

*Note 2:* The capacity utilisation rates are substantially lower during the trial period which is typically during the first four months from commencement of operation.

*Note 3:* During the Track Record Period, our trial production of semi-transparent paper, or new production technologies was usually carried out on PM1, PM2 and PM3 of Youlanfa Factory. Therefore, the capacity utilisation of PM1, PM2 and PM3 of Youlanfa Factory decreased slightly during the Track Record Period as the trial production usually achieved lower production efficiency compared with formal production.

*Note 4:* The capacity utilisation rates are adjusted to reflect the actual production period during the first production year of each paper machine.

### Supporting Facilities

To support our paper production, we have installed our own supporting facilities to produce raw materials, recycle resources, provide steam, and treat waste water. As of the Latest Practicable Date, we operated the following supporting facilities:

(a) de-inking facility at our Huaxiang Factory which removes printing ink and colour from recovered paper so that it may be used as pulp in manufacturing our products. In-house de-inking capabilities help us ensure a stable and constant supply of de-inked pulp as raw material for our paper production at a lower cost. Our de-inking production line has a design production capacity of 34,000 tonnes per annum;

(b) coal-fired boiler plants at our Youlanfa, Huaxiang and Xiyuan Factories provide steam to all of our paper machines, with an aggregate installed capacity of 75 tonnes per hour, or t/h. Utilising our boiler plants for our steam needs ensures a stable and reliable source of steam for our Group. Please refer to "Property, Plant and Equipment — Boiler plants" and "Environmental matters" in this section for more details;

(c) a water supply system at our Xiyuan Factory, consisting of a reservoir with an aggregate storage capacity of more than 2,000 tonnes of water and a wastewater treatment facility with a design capacity of 10,560 tonnes of water per day. Please refer to "Utilities — Water" in this section for more details; and

(d) wastewater treatment plants at our Youlanfa, Huaxiang and Xiyuan Factories and a water treatment and recycling system connecting each of our production lines reduces our water consumption. Please refer to "Environmental Matters" in this section for more details.

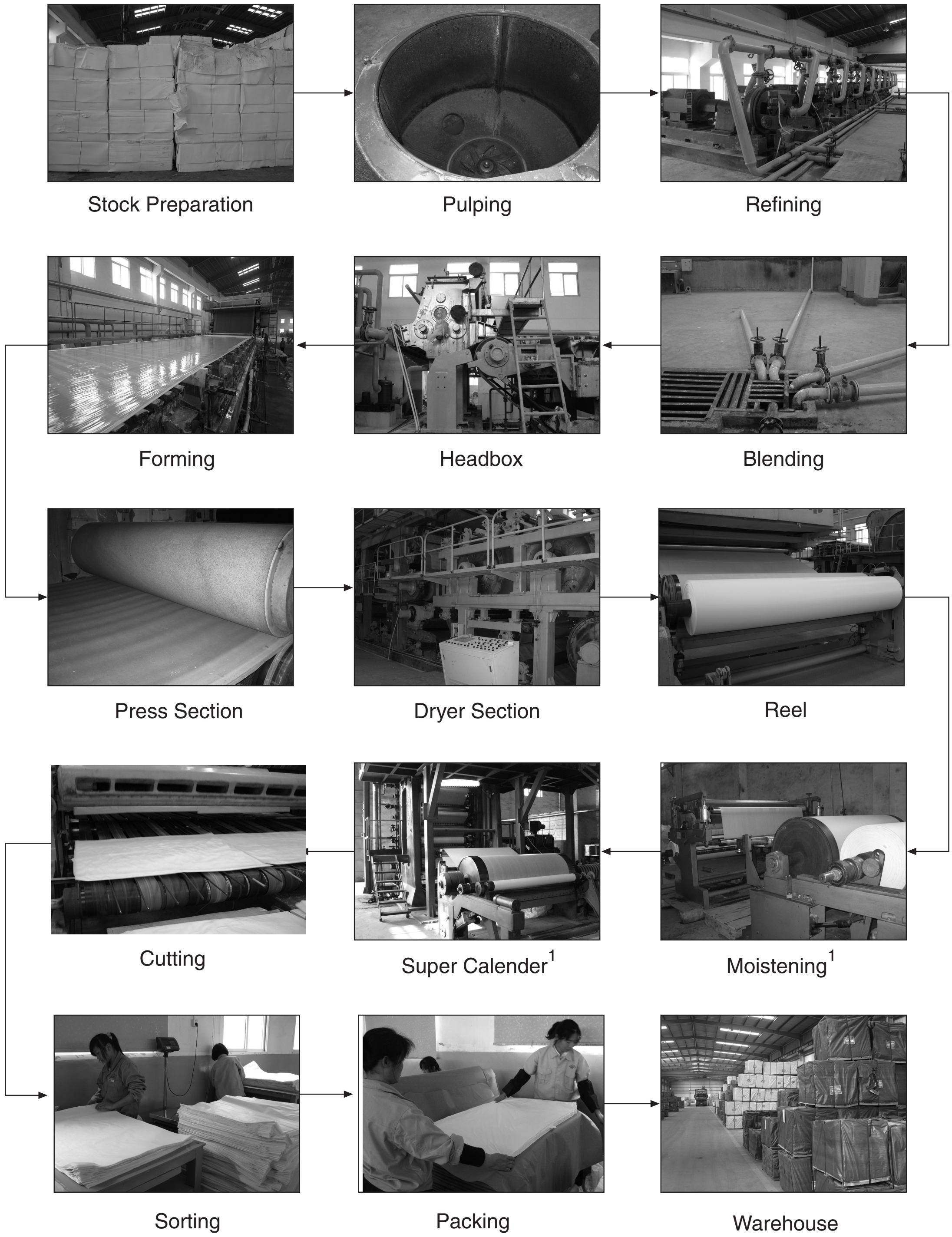
The integration of these facilities maximises our cost-savings, increases our flexibility and control over our business and enables us to serve our customers reliably and efficiently.

### Production Process

Our production process utilises technologically advanced production machinery and inspecting and testing equipment which plays a significant role in maintaining the efficiency of our production and enhancing our product quality. All of our machinery and equipment were purchased in the PRC between 2001 and 2009.

The following flow charts provide an overview of the major steps involved in the production process for our principal products.

*Wrapping Tissue Paper*




*Note 1:* The moistening and super calender steps apply to the manufacture of semi-transparent paper only.

*Copy paper*


Stock Preparation
Pulping
Refining
Blending
Headbox
Forming
Press Section
Dryer Section
Size Press
Dryer Section
Calender
Reel
Cutting
Packing
Warehouse

*Stock Preparation*

We use wood pulp, reclaimed pulp and recycled white paper sourced from independent third parties and de-inked pulp produced at our Huaxiang Factory for our paper-making processes.

De-inking is the process of removing ink and colour from printed and coloured recovered paper for the production of de-inked pulp. The first stage of de-inking involves converting recovered paper to pulp through either a mechanical or chemical process, which produces a slurry mixture. The pulp slurry then undergoes a cleaning and screening stage that removes contaminants denser than pulp fibres. A floatation process is then adopted to de-ink the pulp by using special chemicals and blowing air bubbles through the pulp to carry the inks to the surface, which forms a thick froth that can be removed. The pulp continues to be filtered by additional screening and cleaning processes for the removal of small contaminant particles, which causes it to thicken. Finally, the pulp is bleached to increase its whiteness before going through a final floatation and washing process.

*Pulping*

The raw materials, including pulp board, de-inked pulp, reclaimed pulp, recycled white paper and defective paper sheet are collected during the production process by our quality control personnel, mixed with chemicals and then loaded onto a conveyor and placed into a hydrapulper. The hydrapulper disintegrates the pulp board, reclaimed pulp, de-inked pulp and recycled white paper into smaller pieces to create a porridge-like pulp mass of requisite concentration.

*Refining and blending*

The paper stock then undergoes a beating process whereby pulp stock is placed into a conical machine, which consists of revolving disks that cut and fray the fibres. It is at this stage that fibres become more pliable, gain better bonding strength, and acquire the ultimate characteristics of the paper to be produced. Bleaching chemicals and other ingredients are then added to the stock to create the formula, or varnish, specific for each paper product. After that, the formula is diluted by a large quantity of water to achieve the desired concentration. Before reaching the paper machine, the stock is cleaned once more by centrifugal cleaners, which remove impurities such as dirt and grit, and screened for the removal of any knots to ensure uniformity of stock.

*Headbox and forming section*

After refining and blending, the stock is pumped into a headbox, which is at one end of the paper machine, where the stock runs onto a forming section. The headbox delivers fibres uniformly onto the wire, forming thin wet sheets, or webs, allowing much of the water to be drained away through the mesh and extracted by suction. The headbox and wire section determine several structural properties of the paper including basis weight variation, fibres orientation and distribution and paper uniformity.

*Press section*

The paper web then travels down the wire to the press section where the web is conveyed through a series of pressing facilities on thick felts that squeeze and soak up more water from the paper. At this stage, the paper density is improved.

*Dryer section*

After leaving the press section, the paper web is advanced to the dryer section which consists of a series of drying facilities that remove the remaining water from the web. The drying process affects the paper's surface evenness and strength.

For the production of wrapping tissue paper (apart from semi-transparent paper), the paper is now ready for reeling up into reels as described below. For the production of semi-transparent paper, the paper web is re-hydrated to a certain degree and is then moved to a super calender which compresses the paper to increase its transparency. For the production of copy paper, the paper web moves to a size press located at the end of the dryer where a coating of water mixed with sizing, or starch, is added to the web to improve the paper's strength, water repellency, and ability to receive print. The paper web then goes through a second dryer.

*Calender*

After drying, the production of copy paper and semi-transparent paper requires an additional calendering process. The paper is pulled through calender drives, which consist of stacked sets of rolls that compress the paper to smooth and polish its surface, as well as adjust the paper's density.

*Reel and cut*

Following drying or calendering, the paper comes off the paper machine and is wound onto spools to form large reels. The large reels are cut into sheets according to customer specifications.

*Sorting and packing*

The finished sheets are then sorted, labelled and then packed.

*Warehouse*

Finally, the finished sheets that meet the required standards are despatched or stored in our warehouses.

Our copy paper machine has fully automated quality control systems that monitor the entire production process. This allows us to maintain a consistent quality for our copy paper products. For the manufacture of wrapping tissue paper, we take samples from the pulp, the paper web or finished paper rolls at different stages of production for testing of various physical properties, including strength, thickness, moisture, appearance and basis weight so as to ensure that the required specifications have been met. All defective paper web or rolls are recycled as raw material for future production.

We usually receive purchase orders from customers approximately two weeks in advance and will arrange production accordingly. The actual production time for each order will depend on the purchasing volume. Generally, from stock preparation to storage in a warehouse, production for single-sided MF tissue paper takes approximately 2.5 to 3.5 hours while our production for double-sided MF tissue paper and copy paper takes approximately 3.0 to 4.0 hours.

### Production Team

As of the Latest Practicable Date, our Group had a production team comprised of more than 1,000 personnel led by a team of approximately 20 experienced managerial and executive level personnel in the production departments. We organise our production team into three eight-hour shifts. We also provide training to both new and current employees. We believe that our production team, coupled with our highly automated production facilities, will continue to play a pivotal role in the future growth of our business.

## PROPERTY, PLANT AND EQUIPMENT

We have made substantial investments in acquiring land use rights in Jinjiang and Longhai for our existing operations as well as to allow for future development and expansion. As of the Latest Practicable Date, we had obtained land use certificates for approximately 311,799.6 sq.m. of land in Jinjiang, of which approximately 212,407.0 sq.m. is currently used and 99,392.6 sq.m. is currently reserved for capacity expansion. As of the Latest Practicable Date, we had obtained land use certificates for approximately 308,627.5 sq.m. of land in Longhai, of which approximately 83,774.8 sq.m. is currently used and 224,852.7 sq.m. is currently reserved for capacity expansion. Our land use rights are granted by the government and last for terms of 50 years.

As of the Latest Practicable Date, we had not yet obtained building ownership certificates for buildings with a total gross floor area of approximately 2,832.6 sq.m. in Jinjiang, of which approximately 1,213.3 sq.m. (comprised of a car parking garage of approximately 230.0 sq.m., a waste paper warehouse of approximately 546.0 sq.m., a scrap iron warehouse of approximately 238.0 sq.m., a guard room of approximately 19.3 sq.m., a power distribution room of approximately 60.0 sq.m. and an office room for auxiliary operation purposes of approximately 120.0 sq.m.) was built on parcels for which we did not have use rights ("property A"), and approximately 1,619.3 sq.m. (comprised of a dining area of approximately 279.5 sq.m., a temporary raw materials warehouse of approximately 219.5 sq.m., a resting area of approximately 138.8 sq.m., a security guard room and utilities storage of approximately 82.0 sq.m., dormitories of approximately 514.7 sq.m., an auxiliary manufacturing area of approximately 116.5 sq.m. and an office area of approximately 268.3 sq.m.) partially encroached over property lines of others ("property B"). In addition, we had not obtained construction permits for three buildings ("property C") currently under construction (comprised of a dormitory, a factory building and a warehouse) at our Huaxiang Factory in Jinjiang.

We received a confirmation letter dated 23 December 2009 issued by the Jinjiang Construction Planning and Building Administration Bureau* (晉江市規劃建設與房產管理局) confirming that the construction of the said property C is in compliance with building and construction plans and we shall not encounter legal hindrance in obtaining title certificates after completion of the project and fulfilment of relevant required procedures. Further, due to the progress of the construction project, we expect to obtain the title certificates for property C by the end of 2010. Property C is not directly related nor crucial to the existing operations of the Group.

However, with respect to properties A and B, we will not be able to obtain the relevant land use rights and building ownership certificates and they may be subject to demolition orders by the relevant administrative authority. Properties A and B have been used by us mainly for warehousing, residential and ancillary purposes which are not directly related nor critical to our production process. In this regard, we received two confirmation letters issued by Jinjiang Xibin Town People's Government* (晉江市西濱鎮人民政府) and the Jinjiang Construction Planning and Building Administration Bureau* (晉江市規劃建設與房產管理局) dated 12 January 2010 and 13 January 2010, respectively, and two confirmation letters dated 11 April 2010 issued by each of Jinjiang Xibin Town People's Government* (晉江市西濱鎮人民政府) and the Jinjiang Construction Planning and Building Administration Bureau* (晉江市規劃建設與房產管理局), confirming that we will be allowed to continue to occupy and use properties A and B and we will not be ordered to demolish these properties and no penalty will be imposed on us for our usage of them.

We have not experienced any difficulties in our operation as a result of our occupation and usage of these properties nor has our financial position been affected thereby in the Track Record Period. Based on the above confirmations issued by the relevant administrative authorities, we believe that the likelihood of our Group being ordered to close down properties A and B and/or other buildings is minimal.

Our principal plant and equipment as of the Latest Practicable Date included the following:

- two paper production factories in Jinjiang with an aggregate gross floor area of approximately 115,626.8 sq.m. for which we have obtained building certificates, and one paper production factory in Longhai with a gross floor area of approximately 52,125.7 sq.m. for which we have obtained building certificates;

- coal-fired boiler plants and wastewater treatment plants at our three factories, and a water supply system at our Huaxiang Factory. Please refer to "Production — Supporting facilities" in this section for more details;

- raw material yards and vacant lots with an aggregate storage capacity of up to 95,000 tonnes;

- coal yards with an aggregate storage capacity of up to 10,100 tonnes;

- warehouses with an aggregate storage capacity of up to 23,500 tonnes for finished products;

- our office buildings at our Youlanfa, Huaxiang and Xiyuan Factories with an aggregate gross floor area of approximately 15,070.4 sq.m.; and

- staff quarters at our Youlanfa, Huaxiang and Xiyuan Factories with an aggregate gross floor area of approximately 43,730.6 sq.m.

## Production Equipment

Our production equipment is technologically advanced. According to the China Paper Association, most PRC wrapping tissue paper manufacturers are equipped with machines that run at less than 100 metres per minute, with the more advanced PRC machines running at 200 to 300 metres per minute. Our MF tissue paper machines have operation speeds between 320 and 350 metres per minute and therefore produce larger volumes of paper than most other machines used by our competitors, thereby enhancing our production efficiency and lowering our per unit costs. Please refer to "Production — Production facilities" in this section for further details with respect to our paper machines. The following table sets forth certain additional information on our paper machines as of 31 December 2009.

| Paper machine | Equipment/ supplier origin | Maximum design speed (metres/min) | Maximum paper width (metres) |
|---|---|---|---|
| PM1 (Youlanfa) | PRC | 420 | 1.95 |
| PM2 (Youlanfa) | PRC | 420 | 1.95 |
| PM3 (Youlanfa) | PRC | 450 | 2.8 |
| PM4 (Youlanfa) | PRC | 240 | 2.5 |
| PM1 (Huaxiang) | PRC | 450 | 2.8 |
| PM2 (Huaxiang) | PRC | 450 | 2.8 |
| PM3 (Huaxiang) | PRC | 450 | 2.9 |
| PM4 (Huaxiang) | PRC | 450 | 2.9 |
| PM5 (Huaxiang) | PRC | 450 | 2.9 |
| PM6 (Huaxiang) | PRC | 450 | 2.9 |
| PM7 (Huaxiang) | PRC | 450 | 2.8 |
| PM8 (Huaxiang) | PRC | 450 | 2.8 |
| PM1 (Xiyuan) | PRC | 450 | 2.8 |
| PM2 (Xiyuan) | PRC | 450 | 2.8 |
| PM3 (Xiyuan) | PRC | 450 | 2.8 |
| PM4 (Xiyuan) | PRC | 450 | 2.8 |

### Maintenance of Production Equipment

We had over 20 maintenance personnel responsible for periodic repair and maintenance of our paper machines as of the Latest Practicable Date. Our paper machines are subject to scheduled inspections and maintenance, which lasts for approximately 24 to 36 hours each month. In addition, we schedule inspections and maintenance for each paper machine over the Chinese New Year holidays, during which the paper machine is shut down for approximately a week. We upgrade our production equipment concurrently with our repair and maintenance from time-to-time to increase its longevity and efficiency. During the Track Record Period, we did not experience any material mechanical failures.

### De-inking Facility

Our Huaxiang Factory has been equipped with a de-inking facility since 2006 and it commenced production in 2007. This de-inking machine is capable of processing recovered paper mainly consisting of waste office paper and has a maximum design capacity of 34,000 tonnes of de-inked pulp per annum.

The utilisation rates of our de-inking facility, which are determined by the actual production volume of the de-inking facility against the maximum design capacity, for the three years ended 31 December 2009 were 27.5%, 54.5% and 66.7%, respectively.

The de-inking facility has not reached optimum utilisation for two reasons. Firstly, in order to maintain product quality the amount of de-inked pulp we can blend into our products is limited to a certain extent. Secondly, the de-inking facilities currently only supply de-inked pulp to the production in the Huaxiang Factory due to its location and therefore the de-inked pulp it produces is limited by the demand of the Huaxiang Factory. The Directors believe that with the expansion of the production capacity of the Huaxiang Factory, this de-inking facility will be better utilised in the future.

### Boiler Plants

The following table sets out the design capacities of the boiler plants installed at each of our factories.

| Boiler plant units | Installed capacity (tonnes per hour) |
|---|---|
| Youlanfa Factory | |
| Unit 1 | 20 |
| Subtotal | 20 |
| Huaxiang Factory | |
| Unit 1 | 15 |
| Unit 2 | 15 |
| Subtotal | 30 |
| Xiyuan Factory | |
| Unit 1 | 10 |
| Unit 2 | 15 |
| Subtotal | 25 |
| Total | 75 |

All of the principal components of our boilers are manufactured domestically. The following table sets forth information on the utilisation rates of our boiler plants, which are determined by the actual production volumes of the boiler plants against the installed capacity, for the periods indicated.

| | Year ended 31 December | | |
|---|---|---|---|
| **Boiler plant units** | **2007** | **2008** | **2009** |
| Unit 1 (Youlanfa) | 58.1% | 58.1% | 63.3% |
| Unit 1 (Huaxiang) | 40.1% | 97.1% | 57.8%[1] |
| Unit 2 (Huaxiang) | | | 57.8%[1] |
| Unit 1 (Xiyuan) | | 58.3% | 49.3%[1] |
| Unit 2 (Xiyuan) | | | 49.3%[1] |

*Note 1*: Huaxiang Factory and Xiyuan Factory each installed new boiler plants in 2009 and the utilisation rates of the boiler plants in each of Huaxiang Factory and Xiyuan Factory for the year ended 31 December 2009 were calculated on an aggregated basis.

Our boilers' design capacities are, without any further construction or expansion, sufficient to support an additional annual production capacity of approximately 52,700 tonnes at our Youlanfa, Huaxiang and Xiyuan Factories.

**Warehouses and Raw Material Yards**

We have warehouses at our Youlanfa, Huaxiang and Xiyuan Factories with an aggregate capacity of up to 23,500 tonnes for storage of finished products.

We also have raw material yards (together with some vacant lots at the production sites) and coal yards with an aggregate storage capacity of up to 95,000 tonnes and 10,100 tonnes, respectively.

Our raw material yards, vacant yards, and warehouses provide us with the flexibility to manage or increase our inventory at times when market conditions make it prudent to do so or in accordance with our operational requirements and to respond quickly to customer orders.

**PROCUREMENT OF RAW MATERIALS**

Our procurement department is responsible for acquiring raw materials and selecting suitable suppliers, as well as for coordinating with our quality control personnel to ensure that delivered raw materials meet our specifications. We maintain stock of raw materials based on our production schedule and typically keep two to four weeks supply for most raw materials although we follow a "just in time" policy for reclaimed pulp which we source locally and do not need to store inventory in significant quantities. From time to time we may increase our purchase of raw materials when we believe that the cost of raw materials and our estimates of production and sales make it prudent to do so. In selecting suppliers, our procurement department compares the qualities and prices of the raw materials from at least three suppliers, if possible, and considers each supplier's ability to satisfy our volume and delivery requirements. We are typically granted with credit terms of 60 to 180 days after the date of delivery by our relevant suppliers.

Wood pulp, reclaimed pulp, de-inked pulp and recycled white paper are the principal raw materials for the production of our products. Wood pulp accounts for the largest portion of our raw material costs, followed by reclaimed pulp, de-inked pulp and recycled white paper. We also use various chemicals in our production to enhance the appearance and quality of our products. Raw materials comprised 72.1%, 71.4% and 69.4% of our total cost of sales for the three years ended 31 December 2009, respectively. The following table sets forth our cost by type for our principal raw materials as well as the percentage each represents as compared to our total cost of sales for the periods indicated.

| | Year ended 31 December | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | 2008 | | 2009 | |
| | (RMB in MN) | % | (RMB in MN) | % | (RMB in MN) | % |
| Wood pulp | 71.1 | 38.0 | 119.6 | 32.0 | 180.2 | 37.2 |
| Reclaimed pulp | 49.0 | 26.2 | 80.5 | 21.5 | 60.1 | 12.4 |
| De-inked pulp[1] | 8.7 | 4.6 | 55.9 | 15.0 | 56.6 | 11.7 |
| Recycled white paper | 0.1 | 0.1 | 1.6 | 0.4 | 26.0 | 5.4 |
| Chemicals | 6.0 | 3.2 | 9.4 | 2.5 | 13.1 | 2.7 |
| Total costs of raw materials | 134.9 | 72.1 | 267.0 | 71.4 | 336.0 | 69.4 |
| Total cost of sales | 187.1 | 100.0 | 373.9 | 100.0 | 484.1 | 100.0 |

*Note 1:* De-inked pulp is a type of raw material produced by our Huaxiang Factory. The cost shown above represents sourcing costs as well as the processing costs we incurred during the relevant periods.

The following table sets forth the breakdown of the average costs of sales per tonne of our products for the periods indicated.

| | Year ended 31 December | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2007 | | | 2008 | | | 2009 | | |
| | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper |
| | average cost of sales per tonne (RMB) | | | | | | | | |
| Wood pulp | 1,972.0 | 1,114.8 | 2,318.1 | 1,821.3 | 971.8 | 2,036.0 | 1,924.9 | 1,088.6 | 1,812.6 |
| Reclaimed pulp | 1,765.4 | 1,146.0 | 711.7 | 1,717.9 | 135.1 | 910.4 | 765.5 | — | 719.6 |
| De-inked pulp[1] | — | 1,261.2 | — | 5.6 | 2,251.2 | — | 150.0 | 1,739.4 | — |
| Recycled white paper | — | — | 10.5 | 39.4 | — | 6.8 | 342.2 | 47.0 | 167.8 |
| Chemicals | 47.3 | 65.4 | 404.0 | 48.7 | 75.0 | 441.9 | 60.9 | 113.8 | 452.6 |
| Total costs of raw materials | 3,784.7 | 3,587.4 | 3,444.3 | 3,632.9 | 3,433.1 | 3,395.1 | 3,243.5 | 2,988.8 | 3,152.6 |
| Utilities | 741.2 | 536.9 | 411.9 | 841.5 | 529.4 | 480.1 | 839.5 | 529.9 | 480.8 |
| Others | 859.1 | 859.2 | 697.8 | 778.4 | 658.9 | 744.9 | 691.1 | 625.2 | 743.8 |
| Total | 5,385.0 | 4,983.5 | 4,554.0 | 5,252.8 | 4,621.4 | 4,620.1 | 4,774.1 | 4,143.9 | 4,377.2 |

*Note 1:* De-inked pulp is a type of raw material produced by our Huaxiang Factory. The cost shown above represents sourcing costs as well as the processing costs we incurred during the relevant periods.

The fluctuations in our average costs of sales per tonne of product was mainly due to the economies of scale achieved by our expansion of production, changes in our raw material prices and the different proportion of wood pulp, reclaimed pulp, de-inked pulp and recycled white paper used in the production. The average price of wood pulp, reclaimed pulp and de-inked pulp decreased during the Track Record Period, while the average price for recycled white paper decreased in 2008 but increased slightly in 2009. Our ability to use more recycled white paper in 2009 resulted mainly from our improved technology, which enabled us to apply more recycled white paper in our production while at the same time maintaining our standards of quality.

For the raw materials used in the production of double-sided MF tissue paper, we began using de-inked pulp and recycled white paper to partially replace wood pulp in 2008 to save costs. Due to the commencement of production of semi-transparent paper, which consumes more wood pulp content than the other forms of double-sided MF tissue paper, the proportion of wood pulp used in the production of double-sided MF tissue paper increased in 2009.

With respect to single-sided MF tissue paper, we increased the proportion of de-inked pulp and reduced the proportion of reclaimed pulp in 2008. De-inked pulp and reclaimed pulp can be used interchangeably and their respective proportion is adjusted based on our production plans.

As de-inked pulp was only supplied to the Huaxiang Factory, it is not used in the production of copy paper, which is produced in the Youlanfa Factory. We also increased the proportion of reclaimed pulp and reduced the proportion of wood pulp used in the production of copy paper in 2008 as compared with 2007.

We were not affected by contamination or supply shortages during the Track Record Period. For the three years ended 31 December 2009, our five largest raw material suppliers in aggregate accounted for approximately 68.1%, 55.4%, and 57.2%, respectively, of our total purchases of raw materials. Purchases from the single largest raw material supplier for the same periods accounted for approximately 25.9%, 18.6%, and 24.3%, respectively, of our total purchases. To the best knowledge of our Directors, none of our Directors, their associates or any shareholders of our Company holding more than 5% of our issued capital, held any interest in any of the above five largest raw material suppliers as at the Latest Practicable Date.

**Wood Pulp**

Our Group currently has 15 suppliers for wood pulp, all of whom are Independent Third Parties, located in the PRC or headquarted in the United States, Canada, Germany or Chile with sales offices in the PRC. For our products to meet certain specifications, wood pulp is required for most of our products and cannot be substituted completely by de-inked pulp or reclaimed pulp. A stable supply of high quality wood pulp is therefore critical to our success. We have identified multiple suppliers from which to source wood pulp, both domestic and overseas, to ensure a stable and cost competitive supply of wood pulp that meets our quality requirements.

Before 2008, we sourced all our wood pulp from domestic suppliers, but starting in 2008 we began sourcing a portion of our wood pulp requirements from overseas suppliers. For the two years ended 31 December 2009, the wood pulp we sourced from overseas accounted for approximately 12.1% and 10.2% of our total purchase of wood pulp, respectively. For the wood pulp sourced from overseas, the suppliers are responsible for providing us the products satisfying the quantity and quality levels agreed with us. We are responsible for customs clearance of such imported wood pulp which is done through independent customs brokers, namely Wukuang (Xiamen) Customs Broker Company Limited* (五礦(廈門)報關行有限責任公司) and Xiamen Guomao Customs Broker Company Limited* (廈門國貿報關行有限公司).

**Reclaimed Pulp**

We source reclaimed pulp from a Xiamen-based recycling company. We selected our reclaimed pulp supplier on account of its product quality and industry experience. We entered into an exclusive supply agreement with the supplier in 2009 which carries a term of three years. This agreement guarantees our priority allocation of its reclaimed pulp output. With respect to our cost of sales for the three years ended 31 December 2009, the cost of our reclaimed pulp per tonne was approximately 39.1%, 41.3% and 33.9% lower than that of our wood pulp, respectively, and reclaimed pulp represented approximately 26.2%, 21.5% and 12.4% of our total cost of sales, respectively, which enabled us to lower our overall cost of pulp.

**De-inked pulp**

We started to use de-inked pulp in our production in 2007 when our de-inking facility at our Huaxiang Factory commenced operation and since then all the de-inked pulp we used in our production has been produced in-house at our Huaxiang Factory. In light of our production strategy to maximise the use of recovered paper for the production of de-inked pulp so long as the product quality remains satisfactory, and to meet our cost objectives and environmental requirements, our ability to source a consistent and stable supply of recovered paper is important to our operations. With respect to our cost of sales for the three years ended 31 December 2009, the cost of our de-inked pulp per tonne was approximately 41.0%, 35.9% and 34.3% lower than that of our wood pulp, respectively, and de-inked pulp represented approximately 4.6%, 15.0% and 11.7% of our total cost of sales, respectively. We currently have 3 suppliers in Fujian Province for recovered paper, all of whom are Independent Third Parties. Currently, the majority of our recovered paper comes from Australia and Japan, as we have found the quality of such recovered paper to be relatively more consistent compared to domestic sources.

**Recycled White Paper**

Mixing recycled white paper with wood pulp, reclaimed pulp and de-inked pulp allows us to increase the overall portion of recycled paper content in our products. With respect to our cost of sales for the three years ended 31 December 2009, the cost of our recycled white paper per tonne was approximately 46.9%, 58.2% and 43.5% lower than that of our wood pulp, respectively, and recycled white paper represented approximately 0.1%, 0.4% and 5.4% of our total cost of sales, respectively. We currently source recycled white paper from one supplier in Fujian Province. Since recycled white paper is widely available from recycling companies, alternative suppliers are readily available in the market.

### Chemicals

Our Group uses various kinds of chemicals in our production process including bleach, starch, sizing agent and retention agent. Bleach is used to whiten our products, starch is used to enhance the strength of our products, a retention agent is used to increase the retention rate of stock and a sizing agent is used to increase the water repellency of our paper products. Different products require a different combination and composition of chemicals. We purchase chemicals from Independent Third Parties in the PRC.

## UTILITIES

Our Group requires a significant amount of water, steam and electricity in our production process, and we have taken a number of measures to reduce our utilities costs. During the Track Record Period, our Group did not suffer from any shortage of water, coal or electricity supply.

### Water

Both our de-inking process and production process consume large amounts of water. Excluding water recycled internally, our Youlanfa, Huaxiang and Xiyuan Factories consume approximately 841, 4,018 and 1,971 tonnes of water per day, respectively, when operating at full capacity.

We have constructed a water supply system consisting of a reservoir with an aggregate storage capacity of more than 2,000 tonnes of water and a wastewater treatment system with a design capacity of 10,560 tonnes of water per day at our Xiyuan Factory, which are located adjacent to Jiulong River. Our Youlanfa and Huaxiang Factories mainly rely on local municipalities for their supply of water. For the three years ended 31 December 2009, water accounted for RMB0.3 million, RMB1.3 million and RMB2.0 million of our total cost of sales.

To conserve water, our Group has constructed water recycling and conservation systems and wastewater treatment facilities at our three production factories to recycle wastewater from our de-inking process and white water from our production process. Wastewater generated from the de-inking process is accumulated in a waste pool and undergoes a process of air flotation whereby suspended substances in the water are removed. Thereafter, the water is sent into a recycled pool and is filtered for the removal of any pollutants and re-used in the manufacturing process. The remaining waste substances are expelled to the facility's cesspool for filter pressing treatment. Once all the moisture has been extracted, any remaining waste substances are transported to and processed by Independent Third Parties. In contrast, white water generated during the production process contains some fine fibres and pulp debris, which are extracted at various stages of filtration and purification, and are recovered and re-employed in the paper production process. The treated white water is also reprocessed and re-used.

### Steam

As a large-scale wrapping tissue paper manufacturer, we require a significant amount of steam for our operations during the stock preparation and drying processes. Our boiler plants are coal-fired and are used to provide steam to our paper machines. Our coal sourcing strategy is to use suppliers that can provide a stable and reliable supply of coal at competitive prices. To lower our coal procurement costs, we purchase all of our coal requirements directly from coal mines located in Fujian Province.

We have one coal-fired boiler unit with an aggregate installed capacity of 20 t/h at our Youlanfa Factory, two coal-fired boiler units at our Huaxiang Factory with an aggregate installed capacity of 30 t/h, and two coal-fired boiler units with an aggregate installed capacity of 25 t/h at our Xiyuan Factory. Our current installed steam generating capacity at our three factories is, without any further construction or expansion, sufficient to support annual production capacity expansions of up to an additional 52,700 tonnes approximately at our three locations. Please refer to "Property, Plant and Equipment — Boiler plants" in this section for more details.

**Electricity**

Our Group requires a significant amount of electricity in our production process. We rely on local utility suppliers for our electricity. We are currently planning to construct a cogeneration plant at our Xiyuan Factory, which is expected upon completion to significantly reduce our reliance on local utility suppliers and lower our production costs. For the three years ended 31 December 2009, electricity accounted for approximately RMB11.3 million, RMB27.2 million and RMB44.6 million of our total cost of sales, respectively.

## SALES AND MARKETING

Our sales and marketing strategy concentrates on establishing a reputation for consistent and stable production and supply of quality paper products at competitive prices, providing dependable customer support services and building stable and enduring relationships with our customers.

**Sales Network**

Our Group has established an extensive sales and marketing network across the PRC, adopting a strategic regional sales system pursuant to which we sell to regional distributors. More specifically, we have designated six sales regions in the PRC, based on the geographical concentration of our customers, to facilitate management of our sales and marketing activities. The six regions are North China, Northeast China, East China, Central China, Southwest China and South China. Our sales representatives based in Fujian Province are divided into different teams to maintain regular contact with customers in our sales regions to track product performance and customer satisfaction. We do not have sales offices in any of these sales regions.

Our sales department is responsible for coordinating with, and handling enquiries and confirming orders and product specifications from customers and providing after sales services including gathering market information and conducting surveys. All orders for our products are undertaken through our sales department located in Huaxiang Factory which then allocates the orders to our Youlanfa, Huaxiang or Xiyuan Factories for production. For any product quality complaints, our quality control department undertakes standard examination and evaluation procedures to ascertain the validity of the claims and would report its findings to the relevant production team. We may offer exchanges to our customers with regards to any products which are certified by us as being defective. As of the Latest Practicable Date, we had not encountered any material defective product claims and we did not incur any expenses for the exchange of defective products during the Track Record Period.

Our sales are concentrated in the East China region, which accounted for RMB398.3 million of our total revenue for the financial year ended 31 December 2009, or 55% of our total revenue. A considerable portion of our sales take place in the neighbouring regions of the Yangtze River Delta and the Pearl River Delta.

The following table provides a breakdown of our revenue, by product, in the six sales regions for the periods indicated.

| Region[1] | Year ended 31 December | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2007 | | | | 2008 | | | | 2009 | | | |
| | Revenue | | | | Revenue | | | | Revenue | | | |
| | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper | % of total revenue | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper | % of total revenue | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper | % of total revenue |
| | (RMB in MN, except percentages) | | | | | | | | | | | |
| North China | 4.1 | — | 1.3 | 2 | 15.7 | 11.8 | 0.6 | 5 | 17.9 | 8.5 | 1.3 | 4 |
| Northeast China | — | — | — | — | 8.5 | 8.4 | — | 3 | 8.9 | 8.4 | — | 2 |
| East China | 119.0 | 25.1 | 69.7 | 80 | 157.8 | 86.6 | 86.8 | 58 | 239.4 | 81.0 | 77.9 | 55 |
| Central China | 1.2 | 0.6 | — | 1 | 0.2 | — | — | 1 | — | — | — | — |
| Southwest China | — | — | — | — | 1.1 | 1.3 | — | 1 | 0.2 | 1.0 | — | 1 |
| South China | 23.6 | 20.3 | 2.7 | 17 | 116.1 | 63.4 | 3.7 | 32 | 204.0 | 69.7 | 6.6 | 38 |
| **Total** | 147.9 | 46.0 | 73.7 | 100 | 299.4 | 171.5 | 91.1 | 100 | 470.4 | 168.6 | 85.8 | 100 |

*Note 1:* North China mainly covers Beijing, Tianjin and Baoding. Northeast China mainly covers Dalian, Liaoyang and Shenyang. East China mainly covers Shanghai, Nanjing, Suzhou, Wenzhou, Xiamen and Quanzhou. Central China mainly covers Wuhan and Changsha. Southwest China mainly covers Guiyang and Kunming. South China mainly covers Guangzhou, Foshan, Shantou, Shenzhen and Huizhou.

As of the Latest Practicable Date, we had a sales force of more than 30 personnel based in Fujian Province. Most of our sales professionals are university graduates and on average have been part of our sales force for more than two years. We organise training sessions from time to time to educate our sales professionals on business skills and sales strategies.

**Marketing**

Our sales department is also responsible for conducting marketing activities and soliciting new customers in our six sales regions. In endeavouring to expand our business, we intend to further increase the size of our sales force as well as expand our geographical coverage.

We are aware of the importance of providing suitable products that satisfy our customers' changing demands and requirements. Therefore, our sales and marketing activities are customer-oriented. Our sales and marketing professionals visit some of our customers regularly. We believe that regular visits enable us to better respond to our customers' procurement needs and to better our understanding of their trading conditions and market information.

To attract new customers, we market our products on the Internet by maintaining a website, www.youyuan.com.hk, where we post our products. We also advertise our products on outdoor billboards. For each of the three years ended 31 December 2009, our advertising expenses were RMB0.8 million, RMB1.0 million and RMB1.4 million, respectively. We expect future expenditure on advertising to increase as we further broaden the scope of our marketing activities with new initiatives such as television advertisements.

**Customers**

We select our customers based on the scale of their businesses and reputation and we have built a large, diversified and stable customer base in the PRC. Our Group believes that this is primarily due to the high quality of our products and our ability to provide them on a consistent basis.

Historically our customer mix included both end-user customers and regional distributors, but with the expansion of our production capacity, we have found it more efficient to deal with regional distributors. We have several reasons for preferring regional distributors over end-user customers. Firstly, regional distributors usually make bulk purchases, which simplifies our production management. Secondly, regional distributors usually have a local sales network, which helps us penetrate a broader market. Thirdly, we believe that dealing with numerous end-user customers inevitably increases our financial risk as end-user customers usually lack the financial strength that is typically associated with regional distributors. Therefore, we began to terminate contracts with small scale end-user customers in 2006 and kept reputable and large scale end-user customers to maintain our revenue growth. It was not until 2009 that our sales network and business relationships with regional distributors became sufficiently well established so that the termination of contracts with all end-user customers made economic sense.

Currently, we have adopted a strategic regional distribution system connecting our regional distributors, who either directly on-sell our products to, or further process our products in accordance with the specifications of the end-users. These end-users include clothing, footwear, handware manufacturers or retailers, fruit growers and wine retailers. For each of the three years ended 31 December 2009, our sales to regional distributors were approximately RMB224.5 million, RMB552.1 million and RMB718.8 million, respectively, which accounted for approximately 83.9%, 98.2% and 99.2%, respectively, of our total sales. We sell all of our products to our customers in the PRC. As of 31 December 2009, we had 98 customers located throughout the PRC with a substantial majority concentrated in Fujian Province, the Yangtze River Delta region and the Pearl River Delta region.

Our sales and marketing professionals visit our customers bi-annually, quarterly or monthly depending on their purchase volume and business needs, to promote our products and to obtain feedback. We also inspect each customer's inventory during these visits to help prevent inventory accumulation of our products. For each of the three years ended 31 December 2009, the customers we visited contributed to 75.0%, 93.5% and 83.9%, respectively, of our total revenue. We plan to visit our major customers each month to understand, among other things, their sales of our products and their inventory levels after the Listing. To prevent inventory accumulation at our customers' level, we closely supervise their actual purchase orders and will follow up with them if their purchase volume has been substantially higher than the order forecast indicated in the "framework letters". We also conduct further investigations if a customer fails to make payments to us in time and may refuse to despatch any further orders from such a customer.

The following table sets forth the number of our customers, new customers, terminated customers and active customers for the periods indicated. Our customers include all purchasers who have previously purchased from us unless such business relationship is terminated in the corresponding year. Among our customers, we consider those who have placed purchase order(s) before and purchased from the Company again during a relevant period as active customers for that same period. New customers are those who have never purchased from the Company before and made the first purchase during the relevant period.

| | Year ended 31 December | | |
|---|---|---|---|
| | **2007** | **2008** | **2009** |
| Beginning balance | 177 | 158 | 112 |
| Number of terminated customers | 146 | 142 | 41 |
| Number of new customers | 127 | 96 | 27 |
| Ending balance | 158 | 112 | 98 |
| Number of active customers | 79 | 75 | 67 |

Of the Company's revenue of RMB267.6 million in 2007, sales to the new customers amounted to approximately RMB121.7 million while sales to the then existing customers amounted to approximately RMB145.9 million. Of the Company's revenue of RMB562.0 million in 2008, sales to the new customers amounted to approximately RMB139.6 million while sales to the then existing customers amounted to approximately RMB422.4 million. Of the Company's revenue of RMB724.8 million in 2009, sales to the new customers amounted to approximately RMB89.1 million while sales to the then existing customers amounted to approximately RMB635.7 million.

The termination of customer relationships was mainly due to our Group's plan to terminate our relationship with end-user customers and to terminate relationships with customers whose main focus was not on wrapping tissue paper or copy paper. For each of the three years ended 31 December 2009, we terminated relationships with 96, 62 and 3 customers, respectively, due to their status as end-user customers and terminated relationships with 49, 78 and 37 customers, respectively, due to their business focuses. Out of the remaining customers, we terminated one and two customers, respectively, in each of 2007 and 2008 due to their respective inadequate purchase volumes, and we terminated one customer in 2009 due to the winding-up of its business.

While we do not normally enter into long-term sales agreements with our customers, the majority of our customers had been our customers for over two years as of the Latest Practicable Date. Our Directors believe that the strong customer loyalty that we enjoy is primarily due to the quality and consistency of our products, our ability to provide stable supplies and to meet customers' needs. We will continue to focus on maintaining long-term relationships with our existing customers and on identifying and developing new relationships with potential customers.

For each of the years ended 31 December 2007, 2008 and 2009, our five largest customers in aggregate accounted for approximately 16.7%, 21.9% and 23.3%, respectively, of our sales.

**Terms of Sales and Credit Policy**

While we do not enter into long-term contracts with our customers, we generally sign "framework letters" with the existing key customers. Each "framework letter" sets out the annual or quarterly order forecasts for the relevant customer with the prices to be determined with reference to our raw materials, costs and the then market conditions at the time of actual order. We give the customers 10 days notice for any change of prices. The customers are required to arrange for delivery of our products and are also responsible for any delivery expenses. They are required to pay us within 60 days upon receipt of our products and any delay in such payments entitles us to refuse to despatch any further orders. If the products delivered are defective or different from the order placed, we will arrange for return or exchange, provided that claims are made within the time limit and are verifiable.

The "framework letters" are merely indications of the planned purchasing volumes of the relevant customers and are non-binding in nature. A customer's actual annual order volume may be different from amounts they previously estimated. Nevertheless, such order indications enable us to estimate the demand for our products ahead of the relevant period and allow us to adjust our production plan accordingly. Among the customers who have entered into such "framework letters", we further categorise them as major customers, standard customers or small customers, based on their planned purchasing volumes each year. The threshold purchase volumes set by us in categorising customers are adjusted every year in accordance with our expected revenue. For each of the three years ended 31 December 2009, we recognised customers with a planned purchasing volume of more than 500,900 and 1,400 tonnes of our products per annum as our major customers and for each of the same periods we had 10, 25 and 24 major customers, respectively. Those customers who do not enter into "framework letters" with us are generally considered as small customers.

Our sales department closely supervises the actual purchase orders made by each customer who enters into a "framework letter" with us and will follow up with the customer if its purchasing volume has been substantially higher or lower than the order forecast, which enables us to prevent any undue accumulation of our products by our customers and to deal with any customer dissatisfaction in the first instance. Each "framework letter" covers one year and as of the Latest Practicable Date, 51 "framework letters" were in place.

It is our policy to always give priority allocations to our major customers and also standard customers with whom we have entered into "framework letters" at times when demand outweighs supply. We also offer small price adjustments to our standard and major customers. Our Group reviews the categorisation of each customer on an annual basis.

We grant a credit period of 60 days to all our customers. In addition to credit periods, customers are subject to credit limits, and are required to settle their accounts before further delivery of our products can be made once the credit limits have been reached. Credit limits are determined with reference to monthly average order amounts by each customer. As of 31 December 2009, a total of RMB134 million of credit was utilised.

We have not had any substantial bad debt or doubtful accounts during the Track Record Period. We periodically review the payment status of our accounts receivables and take appropriate measures to collect overdue accounts. We typically make full provisions for bad debt if it remains overdue for more than two years.

### Revenue recognition

Our revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods sold in the normal course of business, net of discounts and sales-related taxes and without any recourse. We recognise revenue from sales of our products when goods are delivered and title has passed.

### Pricing

We set the selling prices of our products based on a variety of factors, including manufacturing costs, fluctuations in raw material prices, competition, and market conditions. We also set our prices for specific customers based on that customer's volume of purchases. Our pricing committee, which is comprised of members from our management, sales and procurement departments, meets monthly to review the selling prices of our products.

By leveraging our established reputation in the production of wrapping tissue paper, and with the benefits of our integrated manufacturing facilities and our ability to substitute one type of pulp for another to a certain extent without compromising the quality of our products, we are able to sell high quality products at competitive prices and maintain price stability for our products.

## INVENTORY MANAGEMENT

We monitor and control the inventory levels of our raw materials and finished products to optimise our operations. We utilise "U8", an enterprise resource planning system produced by UFIDA, to monitor the planning and allocation of warehouse space and stock of raw materials and finished products to coordinate with delivery requirements and schedules.

Our inventory of raw materials is primarily comprised of wood pulp, reclaimed pulp, recovered paper, recycled white paper, chemicals and packaging materials. We seek to maintain a low level of inventory of raw materials and finished products. We generally keep an inventory level of two to four weeks' supply for most raw materials, although we follow a "just in time" policy for reclaimed pulp which we source locally and do not need to inventory in significant quantities. From time to time we may increase our purchases of raw materials when we believe that the cost of raw materials and our estimates of production and sales make it prudent to do so. For example, during the fourth quarter of

2008 we began increasing our purchases of wood pulp, which caused an increase in our inventory levels starting in mid-2009 (when we began taking delivery of the larger wood pulp orders) up from approximately two to four weeks of production requirements to approximately two months of production requirements, as we considered wood pulp prices at the time to be particularly attractive.

Our inventory of finished products is comprised mainly of products awaiting delivery to customers. We have warehouses at our Youlanfa, Huaxiang and Xiyuan Factories with an aggregate storage capacity of up to 23,500 tonnes for finished products. As of 31 December 2009, our inventory of finished products amounted to RMB10.7 million.

## QUALITY CONTROL

We believe that maintaining an effective quality control programme is essential to the continuous growth of our business. We have implemented a comprehensive and effective quality control system covering every stage of procurement and production. Youlanfa first obtained the accreditation of ISO 9001 in March 2002 in respect of our quality control system.

We examine our raw materials upon arrival before they are unloaded from containers for storage in our raw material yards. We inspect the raw materials and screen out unsuitable material that does not meet our quality control standards. Samples of recovered paper are also taken to our laboratory for testing to ensure the quality of the recovered paper.

For the manufacture of wrapping tissue paper, we take samples from the pulp, the paper web and finished paper rolls at different stages of production for testing of various physical properties, including strength, thickness, moisture, whiteness and basis weight so as to ensure that the required specifications have been met.

For the manufacture of copy paper, once the raw materials are fed into the stock preparation equipment, the production process is controlled and monitored through decentralised computer controlled systems. All of the copy paper machines have fully automated quality control systems that monitor moisture, basis weight, coating weight and thickness, which allows us to maintain a consistent quality, increase production efficiency and minimise disruption of the production process.

As at the Latest Practicable Date, our quality control department, which is led by 3 engineers, employed more than 50 quality control personnel engaged in testing and quality control activities ancillary to our production process. Our quality control personnel possess an average of approximately two years of relevant experience. We provide on-the-job training for our quality control personnel from time to time to ensure that they have the requisite skills to carry out their duties competently and in compliance with our quality control policies and the principles of ISO 9001. Youlanfa's ISO 9001 certificate was renewed in 2008 by China Quality Mark Certification Group Co., Ltd., an institution approved by the former China State Bureau of Technical Supervision. The new certificate is valid for three years. We also hold monthly internal meetings amongst different departments to discuss quality control issues. Any problems encountered by production teams during the production process are discussed and appropriate steps and remedial actions are taken when necessary.

For any product quality complaints, our quality control department undertakes standard examination and evaluation procedures to ascertain the validity of the claims and reports its findings to the relevant production team. We may offer exchanges to our customers with regards to any products which are certified by us as being defective. We have not experienced any significant product returns nor received any material product quality complaints during the Track Record Period.

## RESEARCH AND DEVELOPMENT

We have remained dedicated to enhancing product innovation and production efficiency through research and development since 2000. Our dedication has been recognised by the Fujian Province Economic and Trade Commission* (福建省經濟貿易委員會) through the integration of the Provincial-level Enterprises Technology Centre of Fujian Province* (福建省省級企業技術中心) into our operations, which has provided us with a technological platform by which to reinforce our cooperation with industry experts and academic institutions. Our Group has been involved in continuing cooperation with the China National Pulp and Paper Research Institution* (中國製漿造紙研究院), the Material Engineering College of the Fujian Agriculture and Forestry University* (福建農林大學材料工程學院), Fujian Light Industry Research Institution* (福建省輕工業研究所) and the Chemistry and Materials College of the Fujian Normal University* (福建師範大學化學與材料學院) with a view to developing new products and production process for use within the industry. These four research and education institutions have agreed to assist us in the development and testing of new products, as well as with sharing current industry information. Such cooperation provides an opportunity to these research and education institutions to test their academic knowledge in practice, allowing their staff and students to gain industrial experience from us. Any intellectual property developed by us with their assistance and any profits derived therefrom will be owned exclusively by us and there is no profit-sharing arrangement in relation to such intellectual property. Apart from assisting us in developing technologies, these four research and education institutions also give us priority in applying their paper-making technologies purely developed by themselves.

During the Track Record Period, these four research and education institutions shared with us their research achievements, provided training to our staff and guided us in improving our production processes. For example, we had consulted with the Material Engineering College of the Fujian Agriculture and Forestry University* (福建農林大學材料工程學院) about the selection and use of chemicals in our de-inking process and the technologies we applied in our copy paper production, and the Chemistry and Materials College of the Fujian Normal University* (福建師範大學化學與材料學院) advised us on how to improve our wastewater treatment technologies. We do not owe any obligations to these four research and education institutions and made no payment to them during the Track Record Period.

Some of the technologies we have developed have been utilised in our production processes to achieve higher operational efficiency as well as to develop new products. Semi-transparent paper, a type of double-sided MF tissue paper, is a product which we developed in-house and thereafter commenced production in 2009. The ultra-thin single-sided MF tissue paper developed by us was recognised as a technologically advanced product by the Quanzhou Municipal Department of Science and Technology* (泉州市科學技術局) in the same year. We recently developed the process and techniques for producing paper towels and ivory boards, of which we have commenced production in January and April 2010, respectively. Apart from developing new products, our research and development department also undertakes raw materials testing to control our product quality and to lower our production costs. Based on our laboratory testing results, we managed to use bagasse pulp in our production of semi-transparent paper to increase the transparency of the finished product and to also reduce the raw material costs. We have also managed to increase the maximum percentage of de-inked pulp and reclaimed pulp that we use in our production, which has further reduced our costs. In order to improve our operational efficiency, our research and development department also makes modifications to our facilities to enhance product consistency and production output. As of 31 December 2009, we had registered five patents relating to the treatment of wastewater, modification of our paper machines and our production process.

In recognition of our research and development efforts and our market position, we have been invited by the China Standardisation Technical Committee for Paper Making Industry* (全國造紙工業標準化技術委員會) to participate in the drafting of industry standard specifications for wrapping tissue paper and semi-transparent paper. Moreover, the Fujian Provincial Department of Science and Technology* (福建省科學技術廳) established the Paper-making Technology Development Base of Fujian Province* (福建省紙業技術開發基地) at our research and development centre in 2008, which has served as a platform for collaboration with experts and academic institutions. Youlanfa has applied to the Fujian Provincial Department of Science and Technology* (福建省科學技術廳) for a "High and New Technology Enterprises Certificate* (高新技術企業認定證書)" and has passed the public notice period ended 21 January 2010. We expect to obtain such certificate by August 2010. We believe that our commitment to research and development helps to keep us abreast of the latest developments in production technology, thus ensuring that we remain competitive in the industry.

We have established a research and development committee consisting of six members, most of whom are technical and managerial personnel from our major departments such as production and sales. The committee is further assisted by a team comprised of three technicians and 15 staff from different departments which is in charge of implementing the research plans. For the three years ended 31 December 2009, our research and development expenses were approximately RMB0.1 million, RMB0.2 million and RMB0.4 million, respectively.

At present, our research efforts are focused on food wrapping paper products. Bringing these new products to the market will not only allow us to meet general market demand but will also enable us to diversify our product range. We plan to fully utilise our de-inking technology to produce de-inked pulp as the main raw material for paper towel production. This approach will reduce our production costs and give us a strategic advantage over many of our competitors. Producing paper towels using de-inked pulp would also signify our efforts to conduct our business in accordance with high standards of environmental protection, in line with our environmental policies and standards.

Consistent with the PRC government's efforts to promote more environmentally friendly packaging materials, we intend to focus on the development of paper-recycling technology in future research and development initiatives. Please refer to "Regulations" in this prospectus and "Competition" in this section for more details.

**ENVIRONMENTAL MATTERS**

We consider the implementation of environmentally responsible practices and the maintenance of high environmental standards to be a competitive strength as it reduces our risk of exposure to liability under environmental protection laws and regulations and significantly reduces the impact of our operations on the environment. Youlanfa obtained ISO 14001 certification for our environmental management standards in 2002. As part of this commitment to the environment, we have adopted the following practices and invested in the following facilities:

- We use de-inked pulp, reclaimed pulp and recycled white paper as part of our raw materials for our production. The total cost of de-inked pulp, reclaimed pulp and recycled white paper together accounted for approximately 30.9%, 36.9% and 29.5%, respectively, of our total cost of sales for each of the three years ended 31 December 2009. In addition, we recycle the pulp debris in the used white water that we generate back into our production process as raw material.

- To conserve and minimise our impact on water resources, we operate water recycling and conservation systems at our Youlanfa, Huaxiang and Xiyuan Factories that reduce our consumption of fresh water significantly.

- Our coal-fired boiler plants at our Youlanfa, Huaxiang and Xiyuan Factories are equipped with desulfuration equipment, which ensures that our emission levels remain below levels permitted under applicable PRC regulations.

We are subject to various environmental laws and regulations administered by the PRC's central and local environmental protection bureaus. If our Group is charged for any non-compliance with any PRC environmental laws or regulations, the PRC government may, according to the circumstances and the extent of the pollution, impose on us administrative penalties of different types and degrees, from warnings, fines, orders to make rectification within a specific period or orders to suspend production or to close our business, all of which could have an adverse operational and financial impact on our Company. Please refer to "Regulations" in this prospectus for more details.

Our manufacturing operations generate solid and liquid wastes, including wastewater, sludge and gaseous emissions. In compliance with applicable laws and regulations, we have obtained all required permits for wastewater discharge, airborne emissions and solid waste disposal. We are subject to government environmental inspections and we have never been found to be in material violation of any PRC environmental laws or regulations, or subject to any fine in respect thereof. We have met or exceeded the relevant standards under the PRC environmental laws and regulations. Our Directors believe that our record of environmental compliance has been and will continue to be a positive factor in obtaining regulatory approvals for our capacity expansion projects.

Our Group's environmental protection expenditures have mainly been devoted to environment monitoring and to upgrading our water recycling and conservation systems and coal-fired boiler plants. For each of the three years ended 31 December 2009, our Group spent a total of approximately RMB1.6 million, RMB3.9 million and RMB5.0 million on environmental protection, respectively. The Group expects that the cost of compliance with applicable rules and regulations in the year ending 31 December 2010 will be RMB7.5 million.

In order to ensure that we comply with the relevant PRC environmental laws and regulations, we have appointed two staff in each of our three factories to oversee our wastewater discharge and airborne emissions. These six staff members are responsible for the wastewater treatment and boiler plant operations in each of our three production bases, and they each have an average of approximately 10 years of relevant experience. We will also ensure that we comply with applicable PRC environmental laws and regulations in the future by (i) providing both regular and annual training and special training as-needed upon the promulgation of new environmental laws and regulations; (ii) conducting bi-monthly on-site inspections; (iii) providing relevant training to our staff, including but not limited to providing training to our Directors regarding compliance with PRC environmental laws and regulations; (iv) immediately reporting to our Directors any incident or non-compliance with the relevant PRC environmental laws and regulations and (v) immediately reporting to and coordinating with competent authorities in the event of any incident of non-compliance.

## TRANSPORTATION AND DELIVERY SYSTEM

Our operations are strategically located along the coastal regions of Fujian Province, within close proximity to Xiamen Port and highway networks, facilitating convenient access to both suppliers and key customers in the vicinity of the Yangtze River Delta region and the Pearl River Delta region.

While we do not take responsibility for the delivery of our products to customers and we mainly rely on our suppliers to deliver raw materials to us, our strategic location to well-developed transportation infrastructure, including Xiamen Port, minimises their delivery time and transportation costs. Our Directors believe that our advantageous location has helped and will continue to help build relationships with our customers and suppliers. During the Track Record Period, we did not experience any material disruption with respect to the transportation of our raw materials or finished products.

## AWARDS AND RECOGNITIONS

The table below sets out other major corporate awards/recognitions received by our Group or business engaged by our Group since our establishment:

| Awards/recognitions | Issuing institutions | Year |
|---|---|---|
| "Top 30 Pulp and Paper-making Enterprises in the PRC in 2008"* (2008年度全國制漿造紙30強企業) | China Paper Association* (中國造紙協會) | 2009 |
| "Top 10 Environmentally Friendly Paper-making Enterprise of Fujian Province"* (福建省造紙行業環境友好型十佳企業) | Paper Association of Fujian Province* (福建省造紙行業協會) | 2008 |
| "Paper-making Technology Development Base of Fujian Province"* (福建省紙業技術開發基地) | Fujian Province Economic and Trade Commission* (福建省經濟貿易委員會)<br>Fujian Provincial Department of Science and Technology* (福建省科學技術廳)<br>Fujian Provincial Department of Education* (福建省教育廳)<br>Fujian Provincial Department of Finance* (福建省財政廳) | 2008 |

| Awards/recognition | Issuing institutions | Year |
|---|---|---|
| "Enterprise of Outstanding Creditworthiness for Industry and Commerce"* (工商信用良好企業) | CCP Municipal Party Committee of Jinjiang City* (中共晉江市委)<br>The People's Municipal Government of Jinjiang* (晉江市人民政府) | 2007 |
| "Enterprise of Contractual Performance and Creditworthiness of Fujian Province"* (福建省守合同重信用企業) | Administration for Industry and Commerce of Fujian Province* (福建省工商行政管理局) | 2007 |
| "Provincial-level Enterprise Technology Centre of Fujian Province"* (福建省省級企業技術中心) | Fujian Province Economic and Trade Commission* (福建省經濟貿易委員會)<br>Fujian Provincial Department of Science and Technology* (福建省科學技術廳)<br>Fujian Provincial Department of Finance* (福建省財政廳)<br>Fujian National Taxation Bureau* (福建省國家税務局)<br>Fujian Local Taxation Bureau* (福建省地方税務局)<br>Fuzhou Customs* (福州海關)<br>Xiamen Customs* (廈門海關) | 2007 |
| "Famous Trademark of Fujian Province"* (福建省著名商標) | Administration for Industry and Commerce of Fujian Province* (福建省工商行政管理局) | 2007 |
| "Famous Branded Products of Fujian Province"* (福建名牌產品) | Fujian Provincial People's Government* (福建省人民政府) | 2007 |
| "National Quality Inspection-free Product"* (國家免檢產品) | The People's Municipal Government of Jinjiang* (晉江市人民政府) | 2007 |
| "Third Prize of Scientific and Technological Award of Fujian Province 2004"* (福建省2004年度科學技術三等獎) | Fujian Provincial People's Government* (福建省人民政府) | 2004 |
| "The Second Award of Top 10 Economically Beneficial Enterprises of Paper-making Industry in Fujian Province"* (福建省造紙行業第二屆十佳經濟效益企業) | Paper Association of Fujian Province* (福建省造紙行業協會) | 2001 |

## COMPETITION

Our Group is principally engaged in the manufacture and sale of MF tissue paper products. Our industry is highly competitive. We compete primarily against other PRC domestic paper manufacturers. The players in the PRC wrapping tissue paper industry usually compete on the basis of product quality, consistency, production costs, performance, product development, stability of supply, customer service and price.

The main entry barriers to large-scale paper manufacturing operations include capital requirements, environmental sensitivity and constraints in raw material supplies. However, as the PRC continues to honour its WTO obligations, an increasing number of domestic and foreign enterprises are expected to enter the PRC market. In addition to new entrants in the PRC market, competition from imported paper products is also expected to affect the PRC market, which will further intensify competition.

We strive to maintain our competitiveness through timely introduction of new products and continuous improvement of our existing products. For the year ended 31 December 2008, we achieved approximately 14.0% and 5.3% market share for MF tissue paper and wrapping tissue paper, respectively, in relation to production output within the PRC and were the largest producer by output volume of MF tissue paper in the PRC according to the China Paper Association.

The PRC government has recently promulgated policies that discourage the use of plastic packaging materials and promote more environmentally friendly packaging materials. With effect from 1 June 2008, the PRC government prohibited the production, sale and use of ultra-thin plastic bags and banned all stores, from small retailers to major supermarkets, from giving out free plastic bags to consumers. We expect the demand of our paper products to increase as our wrapping tissue paper can serve as one of the alternative wrapping materials for plastic packaging materials. In addition, we also possess a number of key strengths conducive to our continuing success, such as our strategic location and accessibility to transportation infrastructure, our economies of scale, our ability to use recycled raw materials, our efficient management structure, and our advanced production facilities. As such, we are confident of our growth potential in the paper-making industry and our ability to maintain an edge over our competitors.

## INFORMATION TECHNOLOGY

We currently utilise “U8”, an enterprise resource planning system produced by UFIDA to manage all aspects of our sales operations and financial affairs. The use of this software has enhanced our budget management, cost control and product quality control and enhances the effectiveness of our internal control system. We host our own IT systems and maintain a back-up system.

As a part of our planned information technology upgrades, we also intend to upgrade our enterprise resource planning system. The new system will provide us with a single database that integrates all functional departments involved in our operations into one system. Data maintained in this database would bridge all aspects of our business activities, providing oversight of production, supply chain management, financial management, project coordination, human resources management and customer relationship management. The software's most prominent features include manufacturing capacity and flow regulation, quality control, cost management, workflow management, inventory control, supply chain planning, product inspection and in particular, the provision of a self-service interface for customers, suppliers and employees.

## INTELLECTUAL PROPERTY RIGHTS

Our Group owns trademarks, trade names and service marks both in and outside of the PRC in connection with our business which have been duly registered or are in the process of being registered; more specifically, our Group owns 50 trademarks in the PRC and four trademarks overseas. Please refer to "Statutory and General Information" in Appendix VI to this prospectus for more details. We are also in the process of registering our "Youlanfa" trademark as a "Famous Trademark of China* (中國馳名商標)", an official PRC designation that affords additional protection to trademarks that are well-known to the public.

We seek to protect our intellectual property rights by relying on laws and regulations such as trademark and patent law of the PRC and by imposing confidentiality obligations on employees in our research and development department and on our senior staff in the sales department. As of 31 December 2009, we had registered five patents relating to the treatment of wastewater, modification of our paper machines and our production process.

Our Directors confirm that during the Track Record Period we were not involved in any proceedings in respect of, and we have not received notice of any claims of infringement of any intellectual property rights that may be threatened or pending, in which we may be involved whether as a claimant or as a respondent.

## INSURANCE

We maintain insurance in respect of our property, plant, equipment and machinery. Our insurance coverage is sufficient and in line with common commercial practice in the PRC. Our employees are provided with social insurance in conformity with PRC social security regulations, including pension insurance, medical insurance, unemployment insurance, work-related injury insurance and maternity insurance. We also maintain insurance in respect of our raw materials and finished products whereby in the event of loss or damage we will be compensated for the corresponding losses.

Consistent with customary practice in the PRC, we do not carry any business interruption insurance, third party liability insurance for personal injury or environmental damage arising from accidents at our production facilities or relating to our operations or product liability insurance against claims or liabilities that may arise from products sold by us. During the Track Record Period, we were not subject to claims for losses not covered by our insurance policies.

## LEGAL COMPLIANCE AND PROCEEDINGS

We are not currently involved in any material litigation or legal proceedings which could be expected to have a material adverse effect on our business or operations.

Since our establishment in 1994, there has not been any claim against us in relation to harmful or defective products. Our Directors attribute this principally to our success in minimising our product liability risk through stringent quality control.

***Compliance with PRC laws and regulations***

Substantially all of our business and assets are based in the PRC, and we have established three foreign-invested enterprises in the PRC to conduct our operations. We are required to comply with the laws, regulations and measures in the PRC which are relevant to our operation and business. As confirmed by our PRC counsel, King and Wood, except as disclosed in "Risk Factors — Risk Relating to Our Business and Our Group — We have not obtained property title for some of our properties, which could adversely affect our rights to use such properties" and "Property, Plant and Equipment" in this section, we have complied with such relevant laws and regulations in all material respects and have obtained all necessary licenses, approvals and permits from relevant regulatory authorities which are material for our operations in the PRC.

We will ensure that we comply with applicable PRC laws and regulations in the future by (i) establishing a legal department within the Group to be headed by a person who has obtained legal academic qualification in the PRC; (ii) empowering the said legal department to oversee and maintain our compliance with the relevant PRC laws and regulations; (iii) providing regular trainings or updates in respect of the relevant PRC laws and regulations to our Directors on a bi-annual basis and to senior management and the relevant staff on a quarterly basis; and (iv) seeking external legal advice where appropriate and necessary. Our Directors considered that the said internal control measures relating to compliance are adequate and effective.

***Non-compliance with the Companies Ordinance***

*Discovery of the non-compliance*

It was uncovered by the Reporting Accountants, Deloitte Touche Tohmatsu, during the audit on the Underlying Financial Statements on or about November 2009 that one of our subsidiaries, Sunwell, which was incorporated in Hong Kong on 13 September 2005 and has obtained its business registration for commencement of its operation on the same date, has not prepared audited accounts for each financial year since its incorporation up to the financial year ended 31 December 2008. Sunwell was an investment holding company and has no other business activities in Hong Kong at all relevant material times. Sunwell last filed its profits tax return with the Inland Revenue Department of Hong Kong on 27 April 2007 in which Sunwell reported that it has not earned any taxable income arising from Hong Kong. Based on the profits tax return submitted by Sunwell, the Inland Revenue Department of Hong Kong issued a letter to Sunwell dated 26 July 2007, which required Sunwell to report to the Inland Revenue Department of Hong Kong once it has received any taxable income in Hong Kong. Mr Ke, the then director of Sunwell, was not aware of the specific requirements under section 122 of the Companies Ordinance.

*Remedial actions*

After being informed of the omission in preparing the necessary audited accounts, the directors of Sunwell immediately engaged a local accounting firm in November 2009 to prepare its audited accounts for each financial year since its incorporation up to the financial year ended 31 December 2008. However, at that time, the directors of Sunwell were not aware of the legal implications of such non-compliance and the possible legal means to rectify the same and believed that the non-compliance should have been rectified once the audited accounts of Sunwell were finalised on 5 February 2010. Such audited accounts of Sunwell issued by the local accounting firm were qualified as to a disagreement with the directors of Sunwell in the accounting treatment of the accounts, namely, the decision of the directors of Sunwell to prepare single accounts instead of preparing consolidated accounts for Sunwell.

As confirmed by Deloitte Touche Tohmatsu, the reporting accountants of the Company, the qualification in the above-mentioned audited accounts of Sunwell for the periods 31 December 2006, 31 December 2007 and 31 December 2008 issued by the local accounting firm did not affect the audit opinion of Deloitte Touche Tohmatsu set out in the Accountants' Report.

The audited accounts of Sunwell were provided to the Hong Kong legal advisers of our Company, Orrick, Herrington & Sutcliffe ("Orrick"), on or about mid-February 2010. After reviewing the relevant accounts, Orrick informed our Company that such accounts issued in February 2010 were not in strict compliance with section 122 of the Companies Ordinance and an application to the High Court of Hong Kong is required to be made to permit Sunwell to adopt the said accounts out of time. As a result, Sunwell has applied to the High Court of Hong Kong on 15 March 2010 for an order to adopt the audited accounts for each financial year since its incorporation up to the financial year ended 31 December 2008 out of time. On 31 March 2010, Sunwell obtained an order from the High Court of Hong Kong that the requirements under section 122 of the Companies Ordinance to lay the audited accounts for the periods 31 December 2006, 31 December 2007 and 31 December 2008 in the annual general meeting of Sunwell within nine months from the respective periods be substituted with written resolutions of the shareholder of Sunwell dated 15 March 2010 and that the respective periods be extended to 15 March 2010, the date of filing of the application to the High Court. Such qualified accounts have been considered laid in the annual general meetings of Sunwell as required under section 122 of the Companies Ordinance pursuant to the court order dated 31 March 2010 from the High Court of Hong Kong.

*Potential liabilities arising out of the non-compliances*

Pursuant to section 122 of the Companies Ordinance, if a director of a company fails to take all reasonable steps to comply with the requirements under the section, such person is liable to a maximum fine of HK$300,000. However, it is a defence to prove that he or she had reasonable grounds to believe and did believe that a competent and reliable person was charged with the duty of overseeing that the provision of section 122 of the Companies Ordinance is complied with. Further, if it is proven that the breach was willfully committed, such director could be sentenced to imprisonment for up to 12 months. The Company is advised by Orrick that, while the grant of a court order in relation to section 122 of the Companies Ordinance may not by itself bar criminal enforcement by the Companies Registry of possible offences arising from past default, the likelihood of criminal enforcement by the Companies Registry is low in view of the fact that the High Court of Hong Kong granted an order based on its acceptance of evidence submitted for the court application of Sunwell, including the submission that Mr Ke, the then director of Sunwell, had reasonable grounds to believe and did believe that Ms Tse Siu Har (謝少霞), an individual introduced to Mr Ke through personal contacts who had experience in handling company secretarial matters of Hong Kong companies notwithstanding that she was not a professional secretary, could handle the company secretarial matters of Sunwell and was a competent and reliable person who was charged with the duty of overseeing compliance with section 122 of the Companies Ordinance.

*Impact on subscription by Cathay Special Paper*

Cathay Special Paper confirmed that it was not aware or informed of the non-compliance with section 122 of Companies Ordinance by Sunwell at the time of entering into the Cathay Subscription Agreement and that it has not relied on the accounting records of Sunwell in making its investment decisions. Accordingly, as confirmed by Cathay Special Paper, the above non-compliances of the Companies Ordinance by Sunwell has no impact, and will not impact, on any terms or any part of the Cathay Subscription Agreement and the Smart Port Loan Agreement.

*Preventive measures*

To avoid future occurrences of such non-compliance, our compliance adviser, Somerley Limited, and our chief financial officer and company secretary, Mr Wong Yat Sum, who is an associate member of the Hong Kong Institute of Certified Public Accountants and an Associate of Chartered Certified Accountants with extensive accounting and auditing experience, will assist us to ensure compliance with section 122 of the Companies Ordinance by Sunwell. Further, our audit committee will oversee the financial reporting and internal control procedures of our Company. Our Company also intends to engage Hong Kong legal advisers to continue to provide legal advice to us after the Listing. In addition, to further strengthen the knowledge of our Directors as to the relevant requirements of the Companies Ordinance, our Directors have attended a training in this regard provided by Orrick on 30 April 2010. After Listing, we also plan to engage a Hong Kong legal adviser to provide training on the latest developments of various compliance matters that relate to us including the Listing Rules and the Companies Ordinance, from time to time, as and when needed.

Our Directors consider that the competence and suitability of Mr Ke and the other Directors in properly discharging the duties of directors of a listed issuer will not be adversely affected notwithstanding the above-mentioned non-compliance with section 122 of the Companies Ordinance, in view that at the relevant time of committing such breach, (i) Sunwell was only an investment holding company with no substantial business in Hong Kong, and it is not uncommon for less attention to be paid to the affairs and the local legal requirements for such entities; (ii) the non-compliance did not prejudice the interests of any creditors, customers or suppliers of the Group; (iii) Mr Ke, the then director of Sunwell was primarily based in PRC, had limited knowledge regarding compliance of a Hong Kong private company and had delegated the management of secretarial matters of Sunwell to an individual introduced by a personal contact who informed Mr Ke that such individual had the experience to handle the company secretarial matters of Hong Kong companies and could help Mr Ke with handling the affairs of Sunwell.

The Sole Sponsor believes that the failure of Sunwell for preparing the necessary audited accounts is not uncommon with regard to Hong Kong incorporated companies which are purely investment-holding and that the failure of Mr Ke in this regard should not be regarded as a materially adverse factor in questioning the ability of Mr Ke in achieving a standard required for a position as a director of a listed issuer under Listing Rules 3.08 and 3.09.

## EMPLOYEES AND TRAINING

As of 31 December 2009, we had 1,443 full-time employees. The following table provides a breakdown of our employees by responsibilities as of 31 December 2009.

| | Number of employees | % of total |
|---|---|---|
| Production | 1,079 | 74.7 |
| Maintenance | 27 | 1.9 |
| Sales | 39 | 2.7 |
| Quality control | 59 | 4.1 |
| Procurement | 11 | 0.8 |
| Research and development | 4[1] | 0.3 |
| Finance | 35 | 2.4 |
| Administration and management | 107 | 7.4 |
| Supports and others | 82 | 5.7 |
| Total | 1,443 | 100.0 |

*Note 1:* We have four technicians working in our research and development department. However our research and development projects usually involve staff from other departments. We have established a committee consisting of six members, most of whom are technical and managerial personnel from our major departments such as production and sales. Apart from one technician in our research and development department who is a member of the Committee, the other three technicians, together with 15 staff from other departments, are in charge of implementing the research plans set by the committee.

The remuneration package we offer to our employees includes salary, bonuses and other cash subsidies. In general, we determine employee salaries based on each employee's qualifications, position and seniority. We have designed an annual review system to assess the performance of our employees, which forms the basis of our decisions with respect to salary raises, bonuses and promotions.

We also provide comprehensive training for our employees to improve their skills and develop their careers. We provide orientation training for newly hired employees as well as continuing training for existing employees. We organise on-the-job training on a regular basis on various topics, such as internal regulations, sales skills and career development which are designed to improve the overall quality of our employees and promote the management skills of our mid-level and senior management personnel.

## OUR CONTROLLING SHAREHOLDERS

Immediately after completion of the Global Offering and assuming the Over-allotment Option is not exercised, our Controlling Shareholders, namely Smart Port and Mr Ke, will control the exercise of approximately 55.01% of the voting rights of our Company.

## INDEPENDENCE FROM OUR CONTROLLING SHAREHOLDERS

As at the Latest Practicable Date, except as disclosed in below, none of our Controlling Shareholders nor any of their respective associates had interests in any other companies which (i) held interests in our business during the Track Record Period and ceased to hold such interests upon completion of the Global Offering; or (ii) may, directly or indirectly, compete with our Group's business.

### YLF Leathercover

YLF Leathercover was incorporated under the laws of the PRC on 25 February 1997 and is currently held as to 75% by YLF Industry and 25% by Uniland. YLF Industry is held as to approximately 20% by Mr Cai Qingjiang and approximately 80% by Mr Ke Jixiong, and Uniland is a sole proprietorship wholly-owned by Mr Ke. YLF Leathercover is mainly engaged in the business of manufacturing and sale of linerboard and corrugated paper. We used to purchased certain amount of blue top linerboard from YLF Leathercover in connection with the packaging of our wrapping tissue paper products and it was one of our suppliers. For the three financial years ended 31 December 2009, we purchased approximately RMB1.4 million, RMB4.7 million and RMB6.2 million worth of products from YLF Leathercover respectively.

The following is a summary of the revenue, the gross profit and the net profit of YLF Leathercover during the Track Record Period:

| | Year ended 31 December[1] | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB'000) | (RMB'000) | (RMB'000) |
| Revenue | 94,535 | 88,457 | 62,843 |
| Gross profit | 12,627 | 13,692 | 11,429 |
| Net profit / (loss) | 2,000 | 2,117 | (11,448)[2] |

*Note 1:* The financials of YLF Leathercover for the years ended 31 December 2007, 2008 and 2009 were based on the PRC audited reports of YLF Leathercover.

*Note 2:* The net loss for the year ended 31 December 2009 was due to the impairment loss booked for the period as YLF Leathercover has been ceasing its operations, which is planned to be completed prior to Listing.

The following is a summary of the production volume of YLF Leathercover of linerboard and corrugated paper during the Track Record Period:

| for the year ended 31 December | production volume (approx.) |
|---|---|
| 2007 | 41,000 tonnes |
| 2008 | 34,000 tonnes |
| 2009 | 34,000 tonnes |

The site area of YLF Leathercover is approximately 15,430 sq.m., which has been transferred to Youlanfa. Please refer to "History and Corporate Structure — Restructuring of Our PRC Operating Subsidiaries — Youlanfa" in this prospectus for further details.

YLF Leathercover was not included as part of our Group for the following reasons:

1. Due to fierce market competition and low profit margin, the management of YLF Leathercover plans to cease operation prior to Listing. In addition to disposing land and properties owned by YLF Leathercover to our Group, YLF Leathercover will also dispose its other fixed assets to third parties following the cessation of operation of YLF Leathercover.

2. The major products of YLF Leathercover are linerboard and corrugated paper, which are entirely different from the wrapping tissue paper products manufactured by our Group. The products of YLF Leathercover could be differentiated from the products offered by our Group as follows:

   (a) *Usage*: The linerboard and corrugated paper products manufactured by YLF Leathercover are generally used as external packaging, such as shoe boxes used in connection with storage and transit of shoes, whilst the wrapping tissue paper products manufactured by the Group are mainly used as the inner packaging of products in various industries, such as wrapping of consumer goods such as clothes and shoes.

   The copy paper manufactured by the Group is typically used for general office use, such as, printing and copying.

   (b) *Target customers*: Other than Fujian Jinjiang Daziran Colour Printing Co., Ltd.* (福建省晉江市大自然彩色印刷有限公司), which purchased both the linerboard products from YLF Leathercover and the copy paper from our Group, there were no over-lapping customers between YLF Leathercover and the Group during the Track Record Period.

Sale by YLF Leathercover to Fujian Jinjiang Daziran Colour Printing Co., Ltd.* (福建省晉江市大自然彩色印刷有限公司) for the three years ended 31 December 2009 amounted to approximately RMB7.4 million, RMB8.3 million and RMB5.9 million, respectively, representing approximately 7.8%, 9.3% and 9.4% of the total revenue of YLF Leathercover for the same period.

Sale by our Group to Fujian Jinjiang Daziran Colour Printing Co., Ltd.* (福建省晉江市大自然彩色印刷有限公司) for the three years ended 31 December 2009 amounted to nil, approximately RMB8.2 million and RMB11.7 million, respectively, representing nil, approximately 1.5% and 1.6% of the total revenue of the Group for the same period.

3. Although both the products manufactured by YLF Leathercover and our Group are mainly sold within the PRC, as the usage and the target customers of the products manufactured by YLF Leathercover and those of our Group are entirely different as referred to in paragraph 2 above, our Company considers that the fact that both YLF Leathercover and our Group target the PRC market is irrelevant.

4. Whilst we have exclusively sourced blue top linerboard from YLF Leathercover during the Track Record Period, blue top linerboard is only used for the packaging of our wrapping tissue paper products and is not a major or important component of our products. The blue top linerboard used by our Group also does not involve any sophisticated or patented production techniques which are only available from YLF Leathercover. In addition, we were only one of the customers of YLF Leathercover who have its own other customers.

5. In preparation of the Listing, we have acquired all land and properties owned by YLF Leathercover. Going forward, we plan to purchase production equipment which are more advanced than those owned by YLF Leathercover to produce blue top linerboard for our own use after Listing. As the products for this new linerboard production line is for the internal use of our Group and as one of the support facilities of our Group, this production line is planned to be an auxiliary production line and not part of the 13 new production lines planned as part of our expansion as disclosed in "Business — Business Strategies" in this prospectus. Further, this auxiliary production line has been planned as part of our expansion of our support facilities. Please refer to "Future Plans and Use of Proceeds — Use of Proceeds" in this prospectus for further details. Before we commence internal production of blue top linerboard, we plan to source the same from other suppliers after Listing. In any event, we will cease to purchase blue top linerboard from YLF Leathercover after Listing and we do not expect to encounter any difficulties in locating alternate suppliers of blue top linerboard.

6. Whilst Mr Ke is a director of YLF Leathercover, his involvement in the daily operation of YLF Leathercover has been minimal throughout the Track Record Period and none of our other Directors has been a director of YLF Leathercover throughout the Track Record Period.

Having considered the matters described above and the following factors, we believe that our Group is capable of carrying on its business independently of our Controlling Shareholders and their respective associates after Listing.

**Management Independence**

Our Board comprises four executive Directors, one non-executive Director and three independent non-executive Directors. Our Controlling Shareholder, Mr Ke, is an executive Director and the chairman of our Company.

Each of our Directors is aware of his fiduciary duties as a Director which require, among other things, that he acts for the benefit and in the best interests of our Company and does not allow any conflict between his duties as a Director and his personal interest. In the event that there is a potential conflict of interest arising out of any transaction to be entered into between our Group and our Directors or their respective associates, the interested Director(s) shall abstain from voting at the relevant board meetings of our Company in respect of such transactions and shall not be counted in the quorum. In addition, we have an independent senior management team to carry out the business decisions of our Group independently. Our Directors are satisfied that our senior management team is able to perform their roles in our Company independently, and our Directors are of the view that we are capable of managing our business independently from our Controlling Shareholders after Listing.

**Operational Independence**

We have established our own organisational structure comprised of individual departments, each with specific areas of responsibilities. Our Group has independent access to sources of supplies or raw materials for production as well as customers. We have also established various internal controls procedures to facilitate the effective operation of our business. Our Directors confirmed that our Group has no current intention to enter into any other transactions with any of our connected persons (as such term if defined under the Listing Rules) or their respective associates after the Listing that will affect our operational independence.

**Financial Independence**

Our Group has an independent financial system and makes financial decisions according to our Group's own business needs. Our Directors confirm that as of the Latest Practicable Date, all financial assistance, including amounts due to, and loans or guarantees provided by our Controlling Shareholders to our Group, have been repaid or released or otherwise settled in full. Therefore, there is no financial dependence on our Controlling Shareholders.

**DEED OF NON-COMPETITION**

Each of our Controlling Shareholders has entered into the Deed of Non-competition in favour of our Company, pursuant to which each of our Controlling Shareholders has undertaken to our Company (for itself and for the benefit of its subsidiaries) that they would not and would procure that his or its associates (except any members of our Group) would not, during the period that the Deed of Non-competition remains effective, directly or indirectly, either on their own account or in conjunction with or on behalf of any person, firm or company, among other things, carry on, participate or be interested or engaged in or acquire or hold (in each case whether as a shareholder, partner, agent, employee or otherwise) any business which is or may be in competition with the business of any member of our Group from time to time (the "Restricted Business").

The above undertaking does not apply where:

(a) the holding by our Controlling Shareholders of interests in the shares of a company other than our Group which are listed on a recognised stock exchange provided that:

(i) any Restricted Business conducted or engaged in by such company (and assets relating thereto) accounts for less than 5% of that company's consolidated turnover or consolidated assets, as shown in that company's latest audited accounts; or

(ii) the total number of the shares held by our Controlling Shareholders and/or their respective associates in aggregate does not exceed 5% of the issued shares of that class of the company in question and our Controlling Shareholders and/or their respective associates are not entitled to appoint a majority of the directors of that company and at any time there should exist at least another shareholder of that company whose shareholdings in that company should be more than the total number of shares held by our Controlling Shareholders and their respective associates in aggregate.

(b) any opportunity to invest, participate, be engaged in and/or operate any Restricted Business has first been offered or made available by our Controlling Shareholders and/or their respective associates to us, and after decision by our independent non-executive Directors and approval by our Board of Directors and/or Shareholders as required under the relevant laws and regulations (including but not limited to the Listing Rules) and in accordance with our Articles of Association, has declined in writing such opportunity to invest, participate, be engaged in or operate the Restricted Business, and that the principal terms by which our Controlling Shareholders (or their respective associates) subsequently invests, participates, engages in or operates the Restricted Business are no more favourable than those offered to the member of our Group.

Pursuant to the Deed of Non-competition, the above restrictions would only cease to have effect upon the earlier of: (i) the Shares of our Company cease to be listed on the Stock Exchange; and (ii) our Controlling Shareholders and/or their respective associates ceases to hold an equity interest in our Company and (iii) our Controlling Shareholders and/or their respective associates jointly or severally are entitled to exercise or control the exercise of less than 30% in aggregate of the voting power at general meetings of our Company and no longer the single largest shareholder of our Company.

## CORPORATE GOVERNANCE MEASURES

Our Company will adopt the following measures to manage any conflict of interests arising from the competing business of our Controlling Shareholder and to safeguard the interests of our Shareholders:

(i) the independent non-executive Directors, when considering whether to exercise the right of first refusal pursuant to the Deed of Non-competition, will consider the following factors:

   (a) whether the new opportunity in any business investment or commercial opportunity relating to the Restricted Business identified by or offered to the Controlling Shareholders (the "New Opportunity") is in line with the business development strategy of our Group;

   (b) whether the plan and development of the New Opportunity are compatible with the business focus of our Group;

   (c) the operating history, feasibility and compliance issues of the New Opportunity;

   (d) whether the terms offered are fair and reasonable by reference to the market conditions at the relevant time;

   (e) the impact of pursuing the New Opportunity on earning and liabilities of our Group;

   (f) the extent of management and control over the New Opportunity; and

   (g) whether the New Opportunity is a business in competition with the Group and the effect on the Group if not pursuing the New Opportunity;

(ii) the decision whether to exercise the right of first refusal pursuant to the Deed of Non-competition will be determined solely by the independent non-executive Directors and no approval from the Board of Directors and the Shareholders is required;

(iii) our independent non-executive Directors will review, at least on an annual basis, the compliance with the undertaking given by our Controlling Shareholder under the Deed of Non-competition, including right of first refusal for the New Opportunity;

(iv) our Controlling Shareholders has undertaken to provide all information requested by our Company which is necessary for the annual review by our independent non-executive Directors and the enforcement of the Deed of Non-competition;

(v) pursuant to the Articles of Association, a Director will not vote nor be counted as part of a quorum, and will abstain from the meeting when our Board of Directors discusses and considers any resolution relating to any contract or arrangement or any other proposal in which such Director or any of the associates of such Director is interested in more than 5% in the transaction, which has given or may give rise to actual or potential conflicts of interest, unless expressly requested by a majority of our independent non-executive Directors;

(vi) our Company will disclose decisions on matters reviewed by our independent non-executive Directors relating to compliance and enforcement of the Deed of Non-competition in the annual reports of our Company;

(vii) our Controlling Shareholders will make an annual declaration in relation to compliance with the Deed of Non-competition in the annual reports of our Company; and

(viii) the independent non-executive Directors have the right, where necessary and at our cost, to engage professional advisers, including legal advisers and independent financial advisers, to advise them on matters relating to the Deed of Non-competition, including whether to exercise the right of first refusal and the terms on which the right of first refusal should be exercised.

## BOARD OF DIRECTORS

Our Board of Directors is responsible for, and has general powers for, the management and conduct of the business of our Group. Our Board of Directors consists of eight Directors including four executive Directors, one non-executive Director and three independent non-executive Directors. The table below sets out certain information in respect of members of our Board of Directors:

| Name | Age | Position |
|---|---|---|
| Mr Ke Wentuo (柯文托) | 53 | Chairman and executive Director |
| Mr Ke Jixiong (柯吉熊) | 26 | Executive Director |
| Mr Cao Xu (曹旭) | 45 | Executive Director |
| Mr Zhang Guoduan (張國端) | 47 | Executive Director |
| Mr Paul Steven Wolansky | 54 | Non-executive Director |
| Prof. Zhang Daopei (張道沛) | 73 | Independent non-executive Director |
| Prof. Chen Lihui (陳禮輝) | 44 | Independent non-executive Director |
| Mr Chow Kwok Wai (周國偉) | 43 | Independent non-executive Director |

### Executive Directors

**Mr Ke Wentuo** (柯文托), aged 53, is the founder of our Group and the chairman of our Company. Mr Ke was appointed as an executive Director on 12 October 2009. He is primarily responsible for our overall strategies, planning and business development. Mr Ke is also a director of all the subsidiaries of our Group. Mr Ke graduated and obtained a college diploma from Fujian College of Forestry* (福建林學院) (now part of Fujian Agriculture and Forestry University* (福建農林大學)) in 1999, majoring in paper manufacturing. Mr Ke has more than 15 years of experience in paper manufacturing. From October 1994 to August 2003, he was the general manager of Youlanfa. Prior to the establishment of Youlanfa, Mr Ke has been engaged in paper manufacturing through YLF Trading, one of the founders of Youlanfa, beginning in 1993. Mr Ke has been a vice-president of the Fujian Paper Association* (福建省紙業協會) since December 1999. He was a committee member of the Quanzhou City National People's Congress Standing Committee Agricultural Economics Working Committee* (泉州市人大常委會農村經濟工作委員會) from June 2001 to December 2009. Mr Ke has been a committee member of the Jinjiang City National People's Congress Standing Committee* (晉江市人民代表大會常務委員會) since January 2004, and has been a committee member of the Tenth Quanzhou Committee of the PRC People's Political Consultative Conference* (中國人民政治協商會議第十屆泉州市委員會) since December 2009. Mr Ke was recognised by the China Paper Association as an outstanding entrepreneur in the field of pulp and paper making* (中國造紙協會製漿造紙行業優秀企業家) in 2009. He was also named as a model entrepreneur in the light industry segment* (全國輕工行業勞動模範) in December 2007. In addition, Mr Ke was named as a Philanthropist in the Quanzhou Municipality* (泉州市慈善家) in 2006. Mr Ke is committed to social charity, which was recognised by his appointment as an honorary president of Quanzhou Charity Association* (泉州市慈善總會永遠名譽會長) in September 2006 and as an honorary president of Jinjiang Charity Association* (晉江市慈善總會永遠榮譽會長) in December 2007.

**Mr Ke Jixiong** (柯吉熊), aged 26, joined our Group in 2002 and is the chief executive officer of our Company. Mr Ke Jixiong was appointed as an executive Director on 6 January 2010. Mr Ke Jixiong is the son of Mr Ke and is primarily responsible for overseeing the manufacturing and sales functions of our Group, as well as the management of the daily operations of our Group. Mr Ke Jixiong is also the deputy chairman and general manager of Youlanfa, and the general manager of Huaxiang. He completed a 4-year distance learning program at Fujian Normal University* (福建師範大學) majoring in business administration in July 2007 (Fujian Normal University is an accredited university and is authorised to grant certificates after completion of its distance learning programs by the Ministry of Education of the PRC). In 2004, Mr Ke Jixiong was awarded as the Third Jinjiang city's Young Entrepreneur award* (晉江市第三屆優秀青年企業家). He is currently a committee member of the Fujian Jinjiang PRC People's Political Consultative Conference* (中國人民政治協商會議福建省晉江市委員會). Since he joined the Group, Mr Ke Jixiong has been overseeing the daily operations of Youlanfa and Huaxiang, gaining experience in procurement and sales. He was instrumental in the formulation of various directions, targets, policies and systems regarding sales and building distribution network for our Group, and has helped to maintain stability in the supply and quality of the raw materials we source, ensuring the standards and quality of our products, and our production plans, are met. Examples of initiations led by Mr Ke Jixiong include the proposal to introduce de-inking facilities to produce de-inked pulp in house, and the negotiation with an independent Xiamen-based recycling company to exclusively supply the Group with reclaimed pulp. These are important initiatives of our Group to achieve greater cost-savings as well as to operate in a more environmentally friendly way to the environment.

**Mr Cao Xu** (曹旭), aged 45, joined our Group in 1997 and is responsible for the management of product development, technological innovation and manufacturing operations. Mr Cao was appointed as an executive Director on 6 January 2010. Mr Cao is also the deputy general manager of the production department of Youlanfa. In 1988, he graduated and obtained a college diploma from the University of Mechanical Industry Anshan* (鞍山市機械工業職工大學) majoring in mechanical engineering. From 1988 to 1997, Mr Cao worked in Metallurgical Department No. 3 Corporation* (冶金工業部第三冶金建設公司), a state-owned enterprise in the PRC, and was responsible for production machinery design and processing.

**Mr Zhang Guoduan** (張國端), aged 47, joined our Group in 2008 and was appointed as an executive Director on 6 January 2010. Mr Zhang is also the deputy production general manager of Xiyuan. Mr Zhang had 27 years of experience in paper manufacturing. From September 1982 to October 1995, Mr Zhang worked in Fujian Jianning No. 2 Paper Manufacturer, during which he worked in different posts including as its departmental head and its deputy factory director, and was responsible for manufacturing quality control management, manufacturing technology and development management, and new products development. From November 1995 to August 2002, he worked in Fujian Naoshan Paper Industry Group* (福建鐃山紙業集團) as deputy general manager. In 1998, Mr Zhang completed an 18-month course at Xiamen University (厦門大學) majoring in economics and management.

### Non-executive Director

**Mr Paul Steven Wolansky**, aged 54, joined our Group in August 2009 as a director of Sunwell and Xi Yuan BVI, and was appointed as a non-executive Director on 6 January 2010. Mr Wolansky graduated from Amherst College in 1978 with a Bachelor of Arts and subsequently obtained a Juris Doctor from Harvard Law School in 1981. Mr Wolansky is a member of the Bar Association of the State of New York. Mr Wolansky has over 19 years of experience in fund management and direct investment. Mr Wolansky is the chairman, president and chief executive officer of New China Management, Inc., the investment manager for The Cathay Investment Fund, Limited since 1994, and the chairman, president and chief executive officer of New China Capital Management, L.P., the investment manager for Cathay Capital Holdings, L.P. and Cathay Capital Holdings II, L.P. since 2004. Cathay Capital Holdings, L.P. is a limited partnership incorporated in the Cayman Islands for investment in PRC related companies and a predecessor fund to Cathay Capital Holdings II, L.P., and Cathay Capital Holdings II, L.P. is a limited partnership incorporated in the Cayman Islands for investment in PRC related companies and the sole shareholder of Cathay Special Paper, which is one of our Shareholders. In addition, Mr Wolansky effectively owns as to 50% in New China Capital Management, L.P. Mr Wolansky also controls 45% of Cathay Master GP, Ltd., the general partner of Cathay Capital Holdings, L.P. and Cathay Capital Holdings II, L.P. As at the Latest Practicable Date, Cathay Capital Holdings, L.P. owns as to 9.36% of Vinda International Holdings Limited (stock code: 3331), a company listed on the Main Board of the Stock Exchange which manufactures household paper. In addition, Mr Wolansky owns less than 1% of the shares of Vinda International Holdings Limited personally. Further, Mr Wolansky is currently a non-executive director of two companies listed on the main board of the Stock Exchange: China Aoyuan Property Group Limited (stock code: 3883) since 2006 and Centron Telecom International Holding Limited (stock code: 1155) since 2006. Mr Wolansky was a non-executive director of Warderly International Holdings Limited (stock code: 607) ("Warderly") from December 2003 to May 2007, a company listed on the Main Board of the Stock Exchange. The trading in the shares of Warderly on the Stock Exchange has been suspended since 14 May 2007 at the direction of the SFC due to insufficient level of operations or assets, during which Mr Wolansky was a non-executive director of Warderly. As at 31 December 2009, Warderly was placed into the third stage of the delisting procedures in accordance with Practice Note 17 of the Listing Rules.

Mr Wolansky was also formerly a non-executive director of CNinsure Inc., a company listed on NASDAQ, from June 2004 to May 2008 and a non-executive director of Longtop Financial Technologies Limited, a company listed on the New York Stock Exchange from June 2007 to June 2009. Further, Mr Wolansky was previously a director of Lomas Financial Corporation ("Lomas"), a company incorporated in Delaware, United States, from 1993 to 1996, which was formerly listed on the New York Stock Exchange. Lomas was in the business of mortgage servicing. On 10 October 1995, Lomas filed for bankruptcy under Chapter 11 of the Federal Bankruptcy Code of the United States. At the prevailing time, Mr Wolansky was appointed as a director of Lomas by Cold Spring Management, Inc., an investment manager for two investment funds which invested in securities of financially distressed companies and sought to profit by reorganising those companies through bankruptcy proceedings as part of their regular business, and Mr Wolansky was a managing director of Cold Spring Management, Inc. from 1990 to 1996. Pursuant to a plan of reorganisation adopted in August 1996 as part of the bankruptcy proceedings, Lomas was reorganised where bulk of its assets were sold and proceeds distributed, and at which time Mr Wolansky resigned as a director of Lomas. Lomas was cleared of its bankruptcy status on 1 October 1996.

**Independent non-executive Directors**

**Prof. Zhang Daopei** (張道沛), aged 73, was appointed as an independent non-executive Director on 6 January 2010. Prof. Zhang graduated from Dongbei Industrial College* (東北工學院) (now known as Northeastern University* (東北大學)) in 1966 majoring in mining machinery. Since the academic degree system was not established in the PRC at that time, he was not awarded a degree upon completion of the course. Since 2005, Prof. Zhang has been a professor at Henan University* (河南大學). He was also a professor at Fujian College of Forestry* (福建林學院) (now part of Fujian Agriculture and Forestry University* (福建農林大學)) from 1995 to 1997. Before becoming a professor, Prof. Zhang spent over 40 years working in paper manufacturing, such as paper products development, factory planning and management, and paper industry trading manufacturing. He worked in Fujian Paper Manufacturing Industrial Company* (福建省造紙工業公司) from 1983 to 1996, during which he carried out various roles including general manager, party secretary and head of the Fujian Paper Manufacturing Research Centre* (福建省造紙研究所). Before joining Fujian Paper Manufacturing Industrial Company*, Prof. Zhang also worked in Fujian Nanping Paper Factory* (福建省南平造紙廠) (now known as Fujian Nanping Paper Co., Ltd* (福建省南紙股份有限公司), a company listed on the Shanghai Stock Exchange) from 1963 to 1983 and in Jilin Shixian Paper Factory* (吉林省石峴造紙廠) from 1955 to 1963. Further, Prof. Zhang has obtained various awards and significant recognition for his achievements. He has been recognised by the State Council of the PRC for his outstanding contribution to the development of engineering technology in the PRC. Prof. Zhang has also been the chairman of Alkaline Recycling Special Committee of the China Technology Association of Paper Industry* (中國造紙學會) since 1990, the vice chairman of Paper History Committee, of the China Technology Association of Paper Industry* (中國造紙學會) since 1994 and the honorary chairman of the Fourth Committee of the Fujian Technology Association of Paper Industry* (福建省造紙學會) since 2007. Prof. Zhang was previously the chairman of Fujian Technology Association of Paper Industry* (福建省造紙學會) from 1994 to 2007.

**Prof. Chen Lihui** (陳禮輝), aged 44, was appointed as an independent non-executive Director on 6 January 2010. Prof. Chen graduated from Fuzhou University* (福州大學) with a bachelor of engineering majoring in machine manufacturing processes and equipment in 1987. He then obtained his master's degree in 1996 and his doctorate degree in 2003 majoring in pulp and paper engineering from South China University of Technology* (華南理工大學). From July 1987 to October 2000, Prof. Chen was with the Fujian College of Forestry* (福建林學院) (now part of Fujian Agriculture and Forestry University* (福建農林大學)), working at various times as an assistant professor, lecturer, associate professor and instructor for master's degree research students. Since November 2000, Prof. Chen was with the Material Engineering College* (材料工程學院) of the Fujian Agriculture and Forestry University* (福建農林大學), working at various times as a professor, instructor of doctorate and master degrees and dean of the college. Prof. Chen was awarded the Fujian Young Scientist Award* (福建青年科技獎) in 2006 for his outstanding achievements in technology. Furthermore, Prof. Chen has won awards for numerous of the research projects in the PRC, including the Fujian Technology Award* (福建省科學技術獎) in December 2003, 2004, 2005 and February 2009, and the Fuzhou Technological Advancement Award* (福州市科學技術進步獎) in September 2008.

**Mr Chow Kwok Wai** (周國偉), aged 43, was appointed as an independent non-executive Director on 6 January 2010. Mr Chow graduated from the University of Hong Kong with a bachelor's degree in Social Science in 1990. Mr Chow is a fellow member of the Association of Chartered Certified Accountants and a fellow member of the Hong Kong Institute of Certified Public Accountants. He has over 16 years of experience in accounting, financial management and corporate finance. Mr Chow previously worked with Price Waterhouse (now known as Price WaterhouseCoopers) where he gained his auditing experience. He then joined Silver Grant International Industries Limited (stock code: 171), a company listed on the main board of the Stock Exchange, in 1993 and was appointed as its executive director in 2004. Other than being an executive director of Silver Grant International Industries Limited, Mr Chow has also been a non-executive director of Cinda International Holdings Limited (stock code: 111) since 2008 and an independent non-executive director of Lijun International Pharmaceutical (Holding) Co., Ltd. (stock code: 2005) since 2005, both of which are listed on the Main Board of the Stock Exchange.

Please refer to "Statutory and General Information" for further information about the Directors in Appendix VI to this prospectus for details of the interest of our Directors in the Shares of our Company (within the meaning of Part XV of the SFO), including the particulars of their service contracts and remuneration.

Except as disclosed in this prospectus, each of our Directors has confirmed that there are no other matters relating to his appointment as a Director that need to be brought to the attention of the Shareholders and there is no other information, in particular, major in relation to his appointment which is required to be disclosed pursuant to Rule 13.51(2) of the Listing Rules.

## SENIOR MANAGEMENT

**Mr Lin Wenfeng** (林文峰), aged 41, is the assistant to our chairman, Mr Ke. Mr Lin joined our Group in January 2008 and is responsible for assisting our chairman in the administration and management of our Group. Mr Lin graduated with a college diploma from Anhui University of Finance & Economics* (安徽財經大學) majoring in finance and accounting in 2005 and graduated from Anhui University* (安徽大學), majoring in law in 2008. Prior to joining our Group, Mr Lin was with Bank of China Jinjiang Branch between October 1988 and May 2007, where he was responsible for bank credit management, credit limit management and overall branch management.

**Mr Wong Yat Sum** (黃一心), aged 33, is our chief financial officer and our company secretary. Mr Wong joined our Group in December 2009 and is responsible for the budget, financial management and control of our Group. Mr Wong has over seven years of experience in accounting and auditing at an international accounting firm. Mr Wong obtained a Bachelor of Science degree majoring in Accounting from the University of Hull in the United Kingdom in 2000. He is currently an associate member of the Hong Kong Institute of Certified Public Accountants and Associate of Chartered Certified Accountants. Prior to joining our Group, Mr Wong was a financial controller for A&W (Shanghai) Woods Co., Ltd., a wood-flooring company in Shanghai, the PRC from 2007 to 2009, where he was responsible for finance, treasury, business planning and risk management.

**Mr Liao Chunxiang** (廖春祥), aged 46, is the deputy general manager of Huaxiang. Mr Liao joined our Group in June 2008 and is responsible for managing the manufacturing processes of Huaxiang. As Mr Liao is also a member of our research and development centre, he participates in our research and development projects. Mr Liao obtained his business administration accreditation from Fujian Economic Management School for Officials* (福建經濟管理幹部學院) in 1998. Prior to joining our Group, Mr Liao worked in Fujian Naoshan Paper Industry Group Co., Ltd.* (福建鐃山紙業集團有限公司) as a manager in its manufacturing department between September 1983 and December 2002, where he was responsible for manufacturing management, improving manufacturing techniques and management.

**Mr Ke Hongchi** (柯鴻池), aged 35, is the sales manager of our Group and is responsible for business development and sales. Mr Ke Hongchi graduated from Jinjiang County Professional School*

(晉江縣職業學校) now known as Jinjiang Professional Technical Secondary School* (晉江職業中專學校) in 1991 and joined our Group in November 1994 as a sale representative of Youlanfa. He was subsequently promoted as an assistant to the sales manager of Youlanfa in 1996 and as a deputy sales manager of Youlanfa in 2000. Since 2005, Mr Ke Hongchi has been the sales manager of Youlanfa and is responsible for sales development and the management of the sales team of Youlanfa. Since the establishment of Xiyuan and Huaxiang in 2006, he has also been responsible for overseeing the sales development and managing the sales team of Xiyuan and Huaxiang.

**Mr Chen Changxing** (陳長興), aged 46, is the manager of our research and development centre. Mr Chen joined our Group in May 2006 and is responsible for the development, execution and management of the research and development projects of our Group. In 1996, Mr Chen graduated with a college diploma from Open University of Fujian* (福建廣播電視大學), majoring in electronic technique applications. Mr Chen also graduated from Fujian Light Industry School* (福建輕工業學校) in 1985, majoring in paper manufacturing. Prior to joining our Group, Mr Chen worked in Fujian Pulp Quality Supervision and Testing Station* (福建省漿紙質量監督檢驗站) between March 2002 and April 2006 and was responsible for research and development of paper manufacturing technology and province-wide quality control supervision and management.

**Mr Shuai Liangming** (帥亮明), aged 45, is the quality control manager of Huaxiang. Mr Shuai joined our Group in February 2008 and is responsible for the quality control of Huaxiang. As Mr Shuai is also a member of our research and development centre, he participates in our research and development projects. Mr Shuai graduated with a college diploma from Minfeng Paper Factory Workers University* (民豐造紙廠職工大學), majoring in pulp and paper manufacturing in 1990, and graduated from Party School of the Central Committee of CPC* (中共中央黨校), majoring in law in 2002. Mr Shuai has obtained various awards in relation to his work in developing new paper products. Prior to joining our Group, Mr Shuai worked in Dongguan Baoli Paper Factory* (東莞市寶力造紙廠) between August 2001 and December 2007, where he was responsible for technology development and standard setting, and product quality testing and management.

**Mr Wu Xiaoxi** (吳曉曦), aged 48, is the head of the electrical engineering department of Huaxiang. Mr Wu joined our Group in February 2000 and is responsible for the management of matters relating to electrical engineering of Huaxiang. As Mr Wu is also member of our research and development centre, he also participates in our research and development projects. Mr Wu graduated from Fuzhou University* (福州大學) in 1982 with a Bachelor's degree majoring in chemical machinery. Prior to joining our Group, Mr Wu worked in Jianning Jiaoheban Factory* (建寧縣膠合板廠) between March 1992 and December 1999, where he was responsible for manufacturing equipment and related technology improvements.

**Mr Chen Taibin** (陳太斌), aged 32, is the manager of the human resources department of Youlanfa. Mr Chen joined our Group in February 2009 and is responsible for hiring and training in Youlanfa. Mr Chen graduated and obtained a college diploma from Fujian Normal School* (福建師範專科學校) in 1995 majoring in chemistry. Prior to joining our Group, Mr Chen worked in Fujian Jinjiang Sanyuan Food Enterprise Co., Ltd.* (福建省晉江三源食品實業有限公司) as its administrative manager between July 2005 and October 2008, where he was responsible for hiring, development and management of payroll scale systems, ongoing training, and the implementation of an administration system.

**Ms Yan Yahong** (顏雅紅), aged 27, is the deputy manager of our purchasing department. Ms Yan joined our Group in September 2009 and is responsible for raw materials purchasing of our Group. Ms Yan graduated from Sun Yat-sen University* (中山大學) with a master's degree in comparative and world literature in 2006. Prior to joining our Group, Ms Yan worked in Jinjiang Panpan Food Co., Ltd.* (晉江盼盼食品有限公司) as its manager for international trade from July 2006 to July 2008, where she was responsible for international market development, the development and implementation of business strategy, and business negotiation.

Except as disclosed above, each of our senior management members has confirmed that he or she has not held any directorship in other listed public companies or major appointments in the three years preceding the Latest Practicable Date.

## COMPANY SECRETARY

Mr Wong Yat Sum is our company secretary. For details of his biography, please refer to "Senior management" in this section.

## MANAGEMENT PRESENCE IN HONG KONG

Rule 8.12 of the Listing Rules requires that a new applicant applying for a primary listing on the Stock Exchange must have a sufficient management presence in Hong Kong. This normally means that at least two of its executive directors must be ordinarily resident in Hong Kong. Since the core business operations and sale and management of our Group are located in the PRC, other than Mr Wong Yat Sum, our company secretary and our chief financial officer, other members of the senior management team of our Group are and will therefore continue to be based in the PRC. As at the Latest Practicable Date, none of our executive Directors are ordinarily resident in Hong Kong. We have applied to the Stock Exchange for, and obtained, a waiver from the strict compliance with the requirement under Rule 8.12 of the Listing Rules. For details of the waiver, please refer to "Waivers from strict compliance with the Listing Rules — Management Presence" in this prospectus.

## REMUNERATION POLICY

Our Directors and senior management receive compensation in the form of salaries, benefits in kind and discretionary bonuses related to the performance of our Group. We also reimburse them for expenses which are necessarily and reasonably incurred for providing services to us or executing their functions in relation to our operations. Our remuneration committee regularly review and determine the remuneration and compensation package of our Directors and senior management, by reference to, among other things, market level of salaries paid by comparable companies, the respective responsibilities of our Directors and the performance of our Group.

After the Listing, our Directors and senior management may receive options to be granted under the Share Option Scheme. A summary of the principal terms of the Share Option Scheme is set out in "Share Option Scheme" in Appendix VI to this prospectus.

## DIRECTORS' AND SENIOR MANAGEMENT'S REMUNERATION DURING THE TRACK RECORD PERIOD

During the years ended 31 December 2007, 2008 and 2009, the aggregate amount of remuneration, including fees, salaries, discretionary bonus, defined contribution plans (including pension), housing and other allowances, and other benefits in kind, paid to our Directors by us and our subsidiaries were approximately RMB906,000, approximately RMB907,000 and approximately RMB907,000, respectively.

Under the arrangements currently in force, we estimates the aggregate remuneration, excluding discretionary bonus, payable to our Directors for the year ended 31 December 2010 will be approximately HK$2,612,000.

During the years ended 31 December 2007, 2008 and 2009, the aggregate amount of remuneration, including fees, salaries, discretionary bonus, defined contribution plans (including pension), housing and other allowances, and other benefits in kind, paid by our Company to its five highest paid individuals, excluding two Directors who constitute two of the five highest paid individuals of our Company, were approximately RMB388,000, approximately RMB405,000 and approximately RMB358,000, respectively.

We have not paid any remuneration to our Directors or the five highest paid individuals as an inducement to join or upon joining us or as compensation for loss of office in respect of the years ended 31 December 2007, 2008 and 2009. Further, none of our Directors have waived any remuneration during the same period.

Except as disclosed above, no other payments have been made or are payable, in respect of the three years ended 31 December 2009, by us to our Directors.

## BOARD COMMITTEES

### Audit Committee

We established an audit committee pursuant to a resolution of our Directors passed on 30 April 2010 in compliance with Rule 3.21 of the Listing Rules. The primary duties of the audit committee are mainly to review the material investment, capital operation and material financial system of our Company; to review the accounting policy, financial position and financial reporting procedures of our Company; to communicate with external audit firms; to assess the performance of internal financial and audit personnel; and to assess the internal controls of our Company. At present, the audit committee of our Company consists of three members, namely Mr Chow Kwok Wai (Chairman), Mr Zhang Daopei and Mr Chen Lihui.

### Remuneration Committee

We established a remuneration committee on 30 April 2010. The primary duties of the remuneration committee are to review the terms of the remuneration package of each Director and member of senior management and making recommendations to the Board regarding any adjustment thereof. No Director shall participate in any discussion about his or her own remuneration. The remuneration committee consists of three members, namely Mr Ke Wentuo (Chairman), Mr Zhang Daopei and Mr Chen Lihui.

## COMPLIANCE ADVISER

We have appointed Somerley Limited as our compliance adviser pursuant to Rule 3A.19 of the Listing Rules. Pursuant to Rule 3A.23 of the Listing Rules, as our compliance adviser, Somerley Limited will advise us on the following matters:

(i) the publication of any regulatory announcement, circular or financial report;

(ii) where a transaction, which might be a notifiable or connected transaction, is contemplated including share issues and share repurchases;

(iii) where we propose to use the proceeds of the Global Offering in a manner different from that detailed in this prospectus or where its business activities, developments or results deviate from any forecast, estimate, or other information in this prospectus; and

(iv) where the Stock Exchange makes an inquiry of us regarding unusual movements in the price or trading volume of the Shares of our Company.

The term of appointment of Somerley Limited shall commence on the Listing Date and end on the date on which we distribute our annual report in respect of our financial results for the first full financial year commencing after the Listing Date and such appointment may be further extended subject to mutual agreement.

**Authorised share capital:**

| | | |
|---|---|---|
| 10,000,000,000 | Shares | HK$1,000,000,000 |

**Issued and to be issued, full paid or credited as fully paid upon completion of the Global Offering:**

Assuming the Over-allotment Option is not exercised at all, and without taking into account any Shares to be issued upon the exercise of any options that may be granted under the Share Option Scheme, our issued share capital immediately following the Global Offering will be as follows:

| | | HK$ | Approximate percentage of issued share capital |
|---|---|---|---|
| *(Shares)* | | | (%) |
| 10,000 | Shares in issue as of the date of this prospectus | 1,000 | 0.01 |
| 749,990,000 | Shares to be issued under the Capitalisation Issue | 74,999,000 | 74.99 |
| 250,000,000 | Shares to be issued under the Global Offering | 25,000,000 | 25.00 |
| 1,000,000,000 | Total | 100,000,000 | 100.00 |

Assuming the Over-allotment Option is exercised in full, and without taking into account any Shares to be issued upon the exercise of any options that may be granted under the Share Option Scheme, our issued share capital immediately following the Global Offering will be as follows:

| | | HK$ | Approximate percentage of issued share capital |
|---|---|---|---|
| *(Shares)* | | | (%) |
| 10,000 | Shares in issue as of the date of this prospectus | 1,000 | 0.01 |
| 749,990,000 | Shares to be issued under the Capitalisation Issue | 74,999,000 | 72.28 |
| 250,000,000 | Shares to be issued under the Global Offering | 25,000,000 | 24.10 |
| 37,500,000 | Shares to be issued upon exercise of the over-allotment option in full | 3,750,000 | 3.61 |
| 1,037,500,000 | Total | 103,750,000 | 100.00 |

**Ranking**

The Offer Shares are ordinary shares in the share capital of our Company and will rank equally in all respects with all Shares in issue or to be issued as set out in the above table, and will qualify and rank in full for all dividends or other distributions declared, made or paid after the date of this prospectus.

**Share Option Scheme**

We have conditionally approved and adopted the Share Option Scheme on 30 April 2010, the principal terms of which are summarised in the sections headed "Share Option Scheme" in Appendix VI to this prospectus.

Pursuant to the Share Option Scheme, eligible participants of the scheme (including our Directors and directors of other members of our Group, full-time and part-time employees, advisers, consultants and business partners of our Group) may be granted options which entitle them to subscribe for Shares representing (when aggregated with options granted under any other scheme) a maximum of 10% of the issued share capital of our Company as of the Listing Date. No options have been granted under the Share Option Scheme as of the Latest Practicable Date.

**General mandate to issue Shares**

Our Directors have been granted a general unconditional mandate to allot, issue and deal with Shares with an aggregate nominal value of not more than the sum of:

(i) 20% of the aggregate nominal value of the share capital of our Company in issue immediately following completion of the Global Offering and Capitalisation Issue (excluding any Shares which may be issued pursuant to the Over-allotment Option); and

(ii) the aggregate nominal value of share capital of our Company repurchased by our Company (if any) under the general mandate to repurchase Shares referred to below.

This mandate will expire at the earliest of:

(i) the conclusion of our Company's next annual general meeting; or

(ii) the expiration of the period within which our Company is required by law or the Articles of Association to hold its next annual general meeting; or

(iii) when varied, revoked or renewed by an ordinary resolution of our Company's shareholders in a general meeting.

For further details of this general mandate, please refer to "Statutory and General Information — Written resolutions of our Shareholders passed on 30 April 2010" in Appendix VI to this prospectus.

**General mandate to repurchase Shares**

Our Directors have been granted a general unconditional mandate to exercise all the powers of our Company to repurchase Shares with a total nominal value of not more than 10% of the aggregate nominal amount of the share capital of our Company in issue or to be issued immediately following completion of the Global Offering and Capitalisation Issue (excluding any Shares which may be issued upon the exercise of the Over-allotment Option).

This mandate only relates to repurchases made on the Stock Exchange, or any other approved stock exchange(s) on which the Shares are listed (and which is recognised by the SFC and the Stock Exchange for this purpose), and which are made in accordance with all applicable laws and/or requirements of the Listing Rules. A summary of the relevant Listing Rules is set out in "Repurchase of our Shares" in Appendix VI to this prospectus.

This mandate will expire at the earliest of:

(i) the conclusion of our Company's next annual general meeting; or

(ii) the expiration of the period within which our Company is required by law or Articles of Association to hold its next annual general meeting; or

(iii) when varied, revoked or renewed by an ordinary resolution of our Company's Shareholders in a general meeting.

For further details of this repurchase mandate, please refer to "Statutory and General Information — Written Resolutions of Our Shareholders Passed on 30 April 2010" in Appendix VI to this prospectus.

Immediately following completion of the Global Offering and Capitalisation Issue (without taking into account any Shares which may be issued upon the exercise of the Over-allotment Option or options that may be granted under the Share Option Scheme), the following persons will have an interest or short position in Shares or underlying Shares which would be required to be disclosed to us and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO, or, directly or indirectly, be interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any other member of our Group:

| Name | Capacity/Nature of interest | Number of Shares interested | Approximate percentage of shareholding |
|---|---|---|---|
| Smart Port | Beneficial interest | 550,050,000 | 55.01% |
| Mr Ke | Interest in controlled corporation and interest of spouse[1] | 573,750,000 | 57.38% |
| Ms Cai Lishuang | Interest in controlled corporation and interest of spouse[2] | 573,750,000 | 57.38% |
| Cathay Special Paper | Beneficial interest | 88,350,000 | 8.84% |
| Mr Paul Steven Wolansky | Interest in controlled corporation[3] | 88,350,000 | 8.84% |

*Note 1:* The 573,750,000 Shares comprise:

(i) 550,050,000 Shares relating to the same block of shares held by Smart Port, which is wholly owned by Mr Ke; and

(ii) 23,700,000 Shares held by Denron, which in turn is wholly beneficially owned by Ms Cai Lishuang, and Mr Ke, being the spouse of Ms Cai Lishuang, is deemed to be interested in the said 23,700,000 Shares held by Denron.

*Note 2*: The 573,750,000 Shares comprise:

(i) 23,700,000 Shares relating to the same blocks of shares held by Denron, which is wholly owned by Ms Cai Lishuang; and

(ii) 550,050,000 Shares held by Smart Port, which in turn is wholly beneficially owned by Mr Ke, and Ms Cai Lishuang being the spouse of Mr Ke, is deemed to be interested in the said 550,050,000 Shares held by Smart Port.

*Note 3:* The 88,350,000 Shares refer to the same block of Shares held by Cathay Special Paper, which is wholly owned by Cathay Capital Holdings II, L.P., a limited liability partnership. Cathay Master GP, Ltd. is the general partner of Cathay Capital Holdings II, L.P., in which Mr Paul Steven Wolansky has an effective control of 45%, and pursuant to Part XV of the SFO, Cathay Master GP, Ltd. has *de facto* control and thus Mr Paul Steven Wolansky is deemed to be interested in the same Shares.

Save as disclosed herein, our Directors are not aware of any person who will, immediately following the Global Offering and Capitalisation Issue, have an interest or short position in Shares or underlying Shares which would be required to be disclosed to us and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO, or, directly or indirectly, be interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of our Company.

**Stock Borrowing Arrangement**

In order to facilitate the settlement of over-allocation in connection with the Global Offering, the Sole Sponsor or its authorised agents may borrow up to 37,500,000 Shares from Smart Port, equivalent to the maximum number of Shares that may be issued upon full exercise of the Over-allotment Option. Further details are set out in "Structure of the Global Offering" in this prospectus.

## Selected Financial Information

*You should read the selected financial information presented below in conjunction with our combined financial statements and the notes thereto included elsewhere in this prospectus. You should also read the section of this prospectus entitled "Share Capital".*

We have extracted our selected combined financial information presented in the tables below from our combined financial statements as of and for the years ended 31 December 2007, 2008 and 2009.

The consolidated financial statements of Xi Yuan BVI and its subsidiaries as of and for the years ended 31 December 2007, 2008 and 2009 have been audited by Deloitte Touche Tohmatsu, independent public accountants, which expressed an unqualified opinion on those statements.

### Selected Combined Statements of Comprehensive Income Data

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Revenue | 267.6 | 562.0 | 724.8 |
| Cost of sales | (187.1) | (373.9) | (484.1) |
| Gross profit | 80.5 | 188.1 | 240.7 |
| Selling and distribution expenses | (2.1) | (3.0) | (4.1) |
| Administrative expenses | (12.6) | (25.4) | (37.0) |
| Other income and other gains and losses | 5.3 | 5.9 | 2.4 |
| Finance costs | (13.6) | (20.0) | (18.2) |
| Profit before tax | 57.5 | 145.6 | 183.8 |
| Taxation | (15.2) | (13.0) | (13.1) |
| Profit and total comprehensive income for the year | 42.3 | 132.6 | 170.7 |
| Profit and total comprehensive income for the year attributable to: | | | |
| Owners of the Company | 40.3 | 126.4 | 166.0 |
| Minority interests | 2.0 | 6.2 | 4.7 |
| | 42.3 | 132.6 | 170.7 |
| Earnings per share - Basic (RMB)[1] | 0.05 | 0.17 | 0.22 |

*Note 1:* The calculation of the basic earnings per share for the Track Record Period is based on the profit attributable to the Shareholders of the Company and 750,000,000 Shares of the Company, taking into account the share swap pursuant to the Reorganisation and adjusted for the effect of the Capitalisation Issue.

### Selected Combined Statements of Financial Position Data

| | As of 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Non-current Assets | 626.8 | 700.5 | 945.0 |
| Currents Assets | 105.0 | 218.5 | 360.3 |
| Current Liabilities | 570.3 | 624.8 | 410.3 |
| Net Current Liabilities | (465.3) | (406.3) | (50.0) |
| Total Assets Less Current Liabilities | 161.5 | 294.2 | 895.0 |
| Non-current Liabilities | — | — | 340.2 |
| Share Capital/Paid-In Capital | 65.4 | 0.0 | 0.0 |
| Reserves | 83.0 | 274.8 | 554.8 |
| Equity Attributable to Owners of the Company | 148.4 | 274.8 | 554.8 |
| Minority Interests | 13.1 | 19.4 | — |

### Selected Combined Statements of Cash Flows Data

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Operating cash flows before movements in working capital | 82.9 | 184.9 | 228.8 |
| Cash generated from operations before income taxes paid | 47.9 | 219.9 | 76.3 |
| Net cash from operating activities | 34.9 | 204.7 | 63.6 |
| Net cash used in investing activities | (215.0) | (122.5) | (244.1) |
| Net cash from (used in) financing activities | 178.4 | (81.7) | 261.5 |
| Net (decrease) increase in cash and cash equivalents | (1.7) | 0.5 | 81.0 |

*The following discussion and analysis should be read in conjunction with our combined financial statements and accompanying notes as set forth in "Appendix I — Accountants' Report" and our selected financial information included elsewhere in this prospectus.*

**Basis of Presentation**

The Company was incorporated in the Cayman Islands on 12 October 2009 and pursuant to the Reorganisation, which is described more fully under the heading "History and Corporate Structure", the Company acquired a 100% equity interest in Xi Yuan BVI, a BVI company incorporated on 10 July 2009. Xi Yuan BVI is the holding company of Sunwell, a Hong Kong company incorporated on 13 September 2005, which is in turn the holding company of the Group's three operating subsidiaries, Youlanfa, a PRC company incorporated on 11 November 1994, Xiyuan, a PRC company incorporated on 18 January 2006, and Huaxiang, a PRC company incorporated on 9 March 2006.

The combined financial statements contained in this prospectus have been prepared as if the Group structure resulting from the Reorganisation had been in existence throughout the Track Record Period, or since the respective dates of incorporation/establishment of the relevant entities now comprising the Group where this is a shorter period. The combined financial statements, which are presented in Renminbi, have been prepared in accordance with IFRS issued by the International Accounting Standards Board.

**Overview**

We are a leading wrapping tissue paper manufacturer in the PRC. We were the largest among the major wrapping tissue paper manufacturers in the PRC by production output in 2008 according to the China Paper Association. We were also recognised by the China Paper Association as one of the Top 30 Pulp and Paper Making Enterprises in the PRC in 2008* (2008年度全國制漿造紙30強企業). Our principal products include double-sided MF tissue paper and singled-sided MF tissue paper, both of which are wrapping tissue paper with basis weight of less than 40g/m$^2$ and are commonly used to wrap clothing, footwear, fruit and other consumer products. We also manufacture copy paper. We market our MF tissue paper under the "Youlanfa" brand and our copy paper under the "Scholar* (大學士學)", "Young Scholar* (小秀才秀)" and "Prodigy* (小神童神)" brands.

We have achieved significant growth during the Track Record Period. For the three years ended 31 December 2007, 2008 and 2009, our revenue was RMB267.6 million, RMB562.0 million and RMB724.8 million, respectively, representing a CAGR of 64.6% from 2007 to 2009. Our profits for the same periods were RMB42.3 million, RMB132.6 million, and RMB170.7 million, respectively, representing a CAGR of 100.9% from 2007 to 2009.

**Recent Developments**

During January 2010 we launched our first production line dedicated to paper towels at our Youlanfa Factory, as well as two new single-sided MF tissue paper production lines at our Xiyuan Factory. During April 2010 we launched our first production line dedicated to ivory boards at our Youlanfa Factory. Please refer to "Business — Production — Production Facilities" in this prospectus for further details.

## Factors Affecting Results of Operations

The following are the primary factors that affect our results of operations.

### *Price, sales volume and product mix*

Our revenue is affected principally by the prices we are able to charge for our single-sided MF and double-sided MF tissue paper products, which in the year ended 31 December 2009 accounted for approximately 25.3% and 62.1% of our sales volume, respectively, and to a lesser extent the prices we charge for our copy paper products, which in the year ended 31 December 2009 accounted for approximately 12.6% of our sales volume. Our product prices are never fixed or guaranteed for customers on a long-term basis, instead they are adjusted on a monthly basis by our pricing committee after examining a variety of factors, including manufacturing costs, raw material costs and market prices. In particular, while demand for our products has been steadily increasing, we have in the past encountered and likely will encounter in the future pressure from distributors, which currently comprise our entire customer base, to lower our product prices from time-to-time in line with decreases in market prices of our key raw material inputs, namely wood pulp. This has in the past and likely will continue in the future to result in both upward and downward fluctuations in the prices of each of our products. Please refer to the first table under "Principal Components of Statements of Comprehensive Income — Revenue" in this section for a breakdown of how our product prices have fluctuated over the Track Record Period, and the disclosures under "Revenue" in the period on period discussions in this section for more detailed explanations regarding these product price fluctuations.

We categorise our customers into three groups: major, standard and small. We offer small price adjustments to our major and standard customers. While we do not enter into long-term contracts with our customers, we generally sign "framework letters" with all major and some standard customers, to whom we offer priority allocations in exchange for non-binding order forecasts. It is our policy to always give priority allocations to our major customers and, with respect to standard customers with whom we have entered into "framework letters", to assign and honour quotas when demand outweighs our production capacity. Our sales volume is primarily determined by customer demand and our production capacity. Product mix, which is determined by market demand, can also affect our profits as each of our products carries slightly different profit margins.

### *Economic Conditions*

The demand for our products is generally influenced by economic conditions in China, including consumer spending and the production output and sales volumes of companies that are the end users of our products. Continuously rising domestic consumption of consumer and manufactured goods, which has risen in line with the growth in Chinese GDP, as well as growth in Chinese exports, has resulted in increased demand for our wrapping tissue paper and copy paper products. Despite the global economic crisis that ensued in the second half of 2008, our product sales were not materially affected because domestic demand for wrapping tissue paper and copy paper in the PRC market remained strong. For the years ended 31 December 2008 and 2009, the Chinese economy experienced GDP growth of 9.6% and 8.7%, respectively, and we experienced 110.0% and 29.0% growth in our revenue, respectively.

### *Capacity Expansion*

Our results of operations have been and are expected to continue to be affected by our production capacity expansion. In recent years we have undertaken a significant expansion in production capacity, adding eight new double-sided MF tissue paper production lines between 2007 and 2009 and four new single-sided MF tissue paper production lines in 2007. Between 2007 and 2009 our annual sales volume of wrapping tissue paper and copy paper increased from 25,575.6 tonnes and 11,448.4 tonnes, respectively, to 92,693.5 tonnes and 13,373.9 tonnes, respectively. To capitalise on the expected increasing demand for wrapping tissue paper, paper towels, ivory boards and copy paper in the PRC, we have added four paper production lines in 2010 and plan to add another nine paper production lines by the end of 2012. Please refer to "Business — Production — Production facilities" in this prospectus for more details. Successfully implementing our planned capacity expansion will impact our future sales volumes, revenues and profits and also our market share. In addition to substantially increased raw material and energy requirements, the addition of new paper production lines will require a corresponding expansion of our supporting infrastructure, such as de-inking facilities, warehouses, water treatment facilities, coal boiler plants and staff dormitories. We expect to satisfy the capital expenditure needs for our planned expansion from the expected proceeds of the Global Offering, as well as from cash flow from operations and bank borrowings. For additional information on our planned future capital expenditures, please refer to "Capital Expenditures" in this section and "Future Plans and Use of Proceeds — Use of Proceeds" in this prospectus.

### *Cost of Wood Pulp, Reclaimed Pulp, De-inked Pulp and Recycled White Paper*

Our results of operations are affected by the cost of wood pulp, reclaimed pulp, recovered paper, which is the key component of the de-inked pulp we produce internally, and recycled white paper, all of which are supplied by third parties.

Wood pulp is our largest raw material component. Wood pulp prices are affected by its general short supply in China, as well as overall economic conditions, transportation costs and foreign exchange rates (a significant portion of wood pulp is imported). Wood pulp experienced significant price decreases beginning in the second half of 2008 and continuing through the first half of 2009 in line with decreased demand for this raw material attributable to depressed economic conditions resulting from the global economic crisis. However, during the second half of 2009 wood pulp prices generally recovered to their near pre-credit crisis levels. In 2008, we began importing wood pulp directly from foreign suppliers, which has resulted in modest cost savings. For example, while our average cost of wood pulp per tonne sourced from domestic and foreign suppliers was very similar, at RMB4,677.8 and RMB4,788.1, respectively, for the year ended 31 December 2008, we began receiving comparatively more favourable pricing from our foreign suppliers in 2009. This resulted in a shift in our average cost of wood pulp per tonne sourced from domestic and foreign suppliers to RMB3,941.4 and RMB3,362.3, respectively, for the year ended 31 December 2009. We believe the larger price decrease for 2009 for foreign-sourced wood pulp may be due to a greater sensitivity on the part of foreign wood pulp suppliers who reacted to decreased demand in the international market for wood pulp caused by the credit crisis. We plan to increase our use of foreign wood pulp suppliers to safeguard against supply disruptions and enhance our overall flexibility and bargaining position with wood pulp suppliers. The following table sets forth for the periods indicated our total cost of wood pulp, the percentage it represents of our total cost of sales and our average cost for wood pulp on a per tonne basis.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| Total cost (RMB in millions) | 71.1 | 119.6 | 180.2 |
| As percentage of total cost of sales | 38.0% | 32.0% | 37.2% |
| Average unit cost (RMB per tonne) | 4,806.0 | 4,762.1 | 3,799.6 |
| Average unit cost for wood pulp purchased from foreign suppliers (RMB per tonne) | — | 4,788.1 | 3,362.3 |
| Volume purchased from foreign suppliers (tonnes) | — | 3,191.0 | 7,400.6 |
| Average unit cost for wood pulp purchased from domestic suppliers (RMB per tonne) | 4,838.4 | 4,677.8 | 3,941.4 |
| Volume purchased from domestic suppliers (tonnes) | 15,266.1 | 23,701.0 | 55,547.4 |

As a result of the Chilean earthquake in February 2010 and an overall pickup in global economic activity, the market price for wood pulp rose substantially during the first quarter of 2010, significantly increasing our cost for wood pulp. For more information on the market prices for wood pulp through 31 March 2010, please refer to "Industry Overview — Overview of the PRC Paper and Paperboard Industry — Raw materials".

To ensure a steady and reliable supply of wood pulp, we maintain relationships with 15 independent suppliers. In addition, when we consider wood pulp prices to be low or about to rise we may undertake bulk purchases and then store the excess wood pulp in our warehouses. For example, during the fourth quarter of 2008 we began increasing the volume of our wood pulp purchases, which subsequently caused an increase in our inventory from approximately two to four weeks of production requirements to approximately two months of production requirements, as we considered wood pulp prices at the time to be particularly attractive.

Reclaimed pulp is our second largest raw material component. To ensure a steady and reliable supply of reclaimed pulp, we have entered into a purchase agreement with an independent reclaimed pulp supplier located in Xiamen, PRC. Under our purchase agreement this reclaimed pulp supplier has committed to give us priority with respect to its output of reclaimed pulp. We negotiate reclaimed pulp purchases with this reclaimed pulp supplier based on what we believe to be reasonable prices and we receive 60 day credit terms. The following table sets forth for the periods indicated our total cost of reclaimed pulp, the percentage it represents of our total cost of sales and our average cost for reclaimed pulp on a per tonne basis.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| Total cost (RMB in millions) | 49.0 | 80.5 | 60.1 |
| As percentage of total cost of sales | 26.2% | 21.5% | 12.4% |
| Average unit cost (RMB per tonne) | 2,927.2 | 2,796.7 | 2,509.8 |

De-inked pulp, which we produce by feeding recovered paper that we purchase from third party suppliers into our own de-inking facilities, has been our third largest raw material component since 2007, when we commenced operating our de-inking facilities. The availability and price of recovered paper, the key input in the production of de-inked pulp, are subject to overall economic conditions, such as the balance between supply and demand, transportation costs and exchange rates (a portion of our recovered paper is imported for us by local intermediaries). We maintain relationships with three independent recovered paper suppliers, all of whom are located in Fujian Province, PRC who source recovered paper for us from the PRC and, beginning in 2008, from Japan and Australia as well. The source of the recovered paper, which is comprised primarily of waste office paper, has a direct impact on its quality and, as a result, the price. For example, Japanese recovered paper is typically of a higher quality than PRC recovered paper, so as a result for the year ended 31 December 2009 we paid an average of RMB1,606.2 per tonne for Japanese recovered paper as opposed to an average per tonne price of RMB1,380.7 for domestically sourced recovered paper. We plan to begin directly sourcing a portion of our recovered paper from foreign sources rather than through local intermediaries in 2010, which we expect will result in some cost savings for us. The table below sets forth for the periods indicated our total cost of de-inked pulp, which includes our internal processing costs as well as the cost to procure recovered paper, the percentage that the cost of de-inked pulp represents of our total cost of sales and our average cost for de-inked pulp on a per tonne basis, including the related component costs for recovered paper and internal processing.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| Total cost (RMB in millions) | 8.7 | 55.9 | 56.6 |
| As percentage of total cost of sales | 4.6% | 15.0% | 11.7% |
| Average unit cost (RMB per tonne) | 2,836.1 | 3,051.7 | 2,495.2 |
| Recovered paper cost (RMB per tonne) | 2,210.1 | 2,463.3 | 1,951.4 |
| Internal processing cost (RMB per tonne) | 626.0 | 588.4 | 543.8 |

While we have been experimenting with it for some time, in 2009 we began purchasing more significant quantities of recycled white paper, which is shredded paper recycled during book and other white paper production. We use recycled white paper in the same manner as the other types of pulp, mixing it directly into the "slurry" that forms the base for our paper products. Our use of recycled white paper allows us to decrease the amount of wood pulp that would otherwise be required for the production of our products, thereby reducing our cost of sales and increasing the overall portion of recycled paper content contained in our products. We source recycled white paper from one supplier in Fujian, although recycled white paper is widely available from various recycling companies in the market. The following table sets forth for the periods indicated our total cost of recycled white paper, the percentage that the cost of recycled white paper represents of our total cost of sales and our average cost for recycled white paper on a per tonne basis.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| Total costs (RMB in millions) | 0.1 | 1.6 | 26.0 |
| As percentage of total cost of sales | 0.1% | 0.4% | 5.4% |
| Average unit cost (RMB per tonne) | 2,553.3 | 1,989.3 | 2,147.8 |

The following table sets forth for the periods indicated the number of tonnes of each type of raw material consumed to produce one tonne of product:

| | Year ended 31 December | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2007 | | | 2008 | | | 2009 | | |
| Raw Materials | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper | Double-sided MF tissue paper | Single-sided MF tissue paper | Copy paper |
| | (tonnes) | | | | | | | | |
| Wood pulp | 0.403 | 0.206 | 0.516 | 0.377 | 0.198 | 0.441 | 0.505 | 0.284 | 0.478 |
| Reclaimed pulp | 0.592 | 0.380 | 0.271 | 0.600 | 0.046 | 0.348 | 0.306 | — | 0.279 |
| De-inked pulp | — | 0.418 | — | 0.002 | 0.751 | — | 0.059 | 0.700 | — |
| Recycled white paper | — | — | 0.004 | 0.020 | — | 0.003 | 0.160 | 0.021 | 0.075 |
| Chemicals | 0.023 | 0.048 | 0.276 | 0.015 | 0.038 | 0.280 | 0.009 | 0.017 | 0.299 |
| Total | 1.018 | 1.052 | 1.067 | 1.014 | 1.033 | 1.072 | 1.039 | 1.022 | 1.131 |

The proportion of raw materials used in our products fluctuated during the Track Record Period primarily as a result of raw material price changes and enhanced production technologies that allow for the incorporation of a higher percentage of recycled pulp content into our products. In 2009, we increased the proportion of recycled white paper used in all of our paper products to reduce costs, while at the same time significantly reduced wood pulp prices allowed us to increase the proportion of wood pulp used in our products without increasing our cost of sales. Our ability to use more recycled white paper in 2009 resulted mainly from our improved technology, which enabled us to apply more recycled white paper in our production while at the same time maintaining our standards of quality. Going forward, our ability to continue to increase the use of less expensive recycled pulp content and to reduce the use of more expensive wood pulp will be an important source of future cost savings.

For the raw materials used in the production of double-sided MF tissue paper, we began using de-inked pulp and recycled white paper to partially replace wood pulp in 2008. Due to the commencement of production of semi-transparent paper, which consumes more wood pulp content than the other forms of double-sided MF tissue paper, the proportion of wood pulp used in the production of double-sided MF tissue paper increased in 2009.

With respect to single-sided MF tissue paper, in 2008 we increased the proportion of de-inked pulp and reduced the proportion of reclaimed pulp used in the production of single-sided MF tissue paper. De-inked pulp and reclaimed pulp can be used interchangeably and the proportions we use of each is adjusted based on our production plan.

As de-inked pulp is only produced and used at our Huaxiang Factory, it is not used in the production of copy paper, which is produced at our Youlanfa Factory. We also increased the proportion of reclaimed pulp and reduced the proportion of wood pulp and recycled white paper used in the production of copy paper in 2008 as compared to 2007.

***Coal and electricity***

After wood pulp, reclaimed pulp and de-inked pulp, coal and electricity are our next largest costs of sales. Coal accounted for RMB10.7 million, RMB22.9 million and RMB29.3 million, or 5.7%, 6.1% and 6.1% of our total cost of sales for the fiscal years ended 31 December 2007, 2008 and 2009, respectively, and electricity accounted for RMB11.3 million, RMB27.2 million and RMB44.6 million, or 6.0%, 7.3% and 9.2% of total cost of sales for the fiscal years ended 31 December 2007, 2008 and 2009, respectively.

Coal prices are affected by global economic conditions and transportation costs. To ensure a steady and reliable supply of coal, we maintain relationships with several independent suppliers located in Fujian Province. For the year ended 31 December 2009, our average price paid for coal was approximately RMB615 per tonne. The prices we paid for coal during the Track Record Period fluctuated modestly as a result of changes to the market price of coal.

We purchase electricity from state-owned utilities. For the year ended 31 December 2009, our average price paid for electricity was approximately RMB0.5 per kilowatt. Although recent government pronouncements indicate that our electricity costs may increase in the near term, we do not expect electricity prices to increase significantly. While the prices we paid for electricity during the Track Record period remained fairly stable, we did encounter modest fluctuations as a result of price changes effected by state-owned electricity providers.

The following table sets forth the cost of coal and electricity, as well as the coal and electricity costs and quantities necessary to produce one tonne of each of our products.

| | Year ended 31 December | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2007 | | | 2008 | | | 2009 | | |
| | Average consumption per tonne of product (kwh or tonne) | Average cost per kwh or tonne (RMB) | Cost per tonne of product (RMB) | Average consumption per tonne of product (kwh or tonne) | Average cost per kwh or tonne (RMB) | Cost per tonne of product (RMB) | Average consumption per tonne of product (kwh or tonne) | Average cost per kwh or tonne (RMB) | Cost per tonne of product (RMB) |
| Double-sided MF tissue paper | | | | | | | | | |
| electricity | 960.4 | 0.4 | 397 | 965.5 | 0.5 | 447 | 1,034.1 | 0.5 | 504 |
| coal | 0.6 | 538.1 | 341 | 0.6 | 651.4 | 377 | 0.5 | 615.2 | 317 |
| Single-sided MF tissue paper | | | | | | | | | |
| electricity | 701.0 | 0.4 | 292 | 700.4 | 0.5 | 322 | 676.0 | 0.5 | 333 |
| coal | 0.4 | 546.9 | 215 | 0.3 | 645.2 | 182 | 0.3 | 614.4 | 171 |
| Copy paper | | | | | | | | | |
| electricity | 388.4 | 0.4 | 162 | 386.5 | 0.4 | 169 | 410.5 | 0.5 | 187 |
| coal | 0.5 | 537.5 | 250 | 0.5 | 656.8 | 311 | 0.5 | 615.7 | 289 |

Throughout the Track Record Period the cost per tonne of product of electricity and coal were affected by a number of factors, including fluctuations in the average unit cost of coal per tonne and electricity per kilowatt or tonne, the amount of steam loss during the production process and the use of different production technologies for different products. The cost per tonne of product of electricity and coal will continue to be influenced by these factors going forward.

### *Taxation*

Our operations are subject to Hong Kong profits tax and PRC enterprise income tax. Our overall effective tax rates for each of the years ended 31 December 2007, 2008 and 2009 was 26.5%, 9.0% and 7.1%, respectively.

We had no Hong Kong tax obligations during the Track Record Period and do not expect to have any such obligations in the future as we have not generated and do not plan to generate taxable income in Hong Kong.

As all of our revenues come from our operations in China, all of our tax expenses are attributable to PRC enterprise income tax and local income tax. As of 31 December 2009, the PRC enterprise tax rate was 25%. We are able to take advantage of a variety of preferential tax treatments applicable to PRC enterprises, such as the two-year tax exemption and the three-year 50% tax reduction, which the PRC has granted to foreign-invested enterprises immediately following the year in which a profit is first reported. Each of our Huaxiang and Xiyuan subsidiaries have been granted a two-year tax exemption and the three-year 50% tax reduction treatment from 1 January 2008. For both Huaxiang and Xiyuan, as

2008 was their first profit-making year, their tax-exempt years are 2008 and 2009 and the years during which they are to receive a 50% tax reduction are 2010 through 2012. As Huaxiang and Xiyuan had profits before tax of RMB78.0 million and RMB10.9 million for the year ended 31 December 2008, respectively, and RMB84.3 million and RMB54.1 million for the year ended 31 December 2009, respectively, the effect of the two-year tax exemption was a tax savings of RMB22.2 million and RMB34.7 million and overall effective tax rates of 9.0% and 7.1% for the years ended 31 December 2008 and 2009, respectively.

Youlanfa has applied to the Fujian Provincial Department of Science and Technology* (福建省科學技術廳) for a High and New Technology Enterprise Certificate and has passed the public notice period ended 21 January 2010. We expect to obtain such certificate by August 2010. Upon issuance of the certificate, Youlanfa will be subject to a reduced PRC enterprise tax rate of 15% for the three-year period beginning 1 January 2010. Please refer to "Regulations — High and New Technology" in this prospectus for more details.

Beginning in 2013, Huaxiang, Xiyuan and Youlanfa may no longer benefit from reduced tax rates and the applicable enterprise income tax rate may revert to 25%, thereby raising the overall PRC enterprise tax rate applicable to our operations to 25%, assuming that tax rates and laws do not change. As our effective PRC enterprise tax rate from 2013 onwards is expected to be substantially more than the current effective tax rate, taxes are likely to have a more significant impact on our profits in the future.

***Production Volume***

With the exception of periodic repair and scheduled maintenance, which accounts for approximately 24 to 36 hours of downtime per month and one week annually, usually over the Chinese New Year holiday, we strive to keep our paper machines running continuously. Our ability to keep paper machines fully utilised has a direct impact on our production volumes, which in turn affects unit costs and profit margins. We currently have no back-up generators and are only in the planning stages of constructing cogeneration plants to make us energy independent, so any unexpected power outages for the near future would have a direct impact on our utilisation rates. Please refer to "Business — Production — Production Facilities" in this prospectus for detailed information on the utilisation rates of our paper machines.

In addition to the number of hours we operate our paper machines, the production volumes achieved by our paper machines are also affected by the speed, which is measured in terms of metres per minute, at which our paper machines are run. Please refer to "Business — Property, Plant and Equipment — Production equipment" in this prospectus for more details. We operated our wrapping tissue paper machines at speeds which we considered to be optimum during the Track Record Period and we do not believe we currently have the ability to increase such speeds significantly in the near future. With respect to our copy paper machine, we maintained significantly reduced operating speeds as compared to optimum operating rates immediately prior to the Track Record Period, which was in proportion to demand for our copy paper at that time. During the Track Record Period, in response to increased demand for our copy paper due to greater market awareness and acceptance of our copy paper, we increased the operating speed of our copy paper machine, which allowed us to moderately increase the production volume of copy paper.

### *Borrowing Costs*

We rely significantly on bank borrowings to fund our operations. Between 31 December 2007 and 31 December 2009 our aggregate bank borrowings increased by RMB229.0 million, or 77.9%, to RMB523.0 million from RMB294.0 million. Our borrowing costs amounted to RMB13.6 million, RMB20.0 million and RMB18.2 million for the years ended 31 December 2007, 2008 and 2009, respectively. Our borrowing costs are dependent on our level of debt and applicable interest rates. Our bank borrowings consist of both fixed and variable rate debt obligations linked to applicable bank rates, the latter of which may be adjusted by banks every year in accordance with prevailing interest rates. While our level of borrowings was comparable in each of 2007 and 2008, it increased significantly in 2009 as outlays related to our expansion plans increased, although our borrowing costs for 2009 were mitigated to an extent by lower average interest rates on our bank borrowings during this period. As of 31 December 2009, our total outstanding bank borrowings amounted to RMB523.0 million, of which RMB340.2 million consisted of long-term borrowings and RMB182.8 million of which consisted of short-term borrowings. As of 31 December 2007, 2008 and 2009, the weighted average interest rate of our total outstanding borrowings was 7.0% 6.8% and 4.8%, respectively. The approximate financial impact we would have suffered in terms of increased annual finance expenses from a 1% increase to the weighted average interest rate for our total variable-rate outstanding bank borrowings for the year ended 31 December 2009 is approximately RMB3.5 million. In order to improve our liquidity position and decrease our net current liabilities, which amounted to RMB406.3 million as of 31 December 2008, we have recently been repaying the majority of our short-term borrowings from the proceeds of long-term borrowings. Our liquidity position was also substantially improved by the waiver of RMB111.6 million in related party loans by our ultimate controlling shareholder during the fourth quarter of 2009. As a consequence, as of 31 December 2009 our net current liabilities were RMB50.0 million.

## Critical Accounting Judgements and Key Sources of Estimation Uncertainty

The preparation of financial statements in conformity with IFRS requires our management to make judgments and estimates and form assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent liabilities at the date of the financial statements, and the reported revenue and costs during the periods presented.

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next year.

### *Useful lives and impairment of property, plant and equipment*

Our management determines the estimated useful lives and related depreciation charges for our property, plant and equipment. This estimate is based on the historical experience of the actual useful lives of property, plant and equipment of a similar nature and function. Management will increase the depreciation charge where useful lives are expected to be shorter than estimated, or it will write off or write down obsolete or non-strategic assets that have been abandoned. Any change in these estimations may have a material impact on our results.

***Estimated impairment of trade receivables***

When there is objective evidence of impairment of trade receivables, our management takes into consideration the estimated future cash flows. The amount of the impairment loss is measured as the difference between the receivable's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). Where the actual future cash flows are less than expected, a material impairment loss may arise.

**Results of Operations**

The following table sets forth our results of operations for the periods indicated:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Revenue | 267.6 | 562.0 | 724.8 |
| Cost of sales | (187.1) | (373.9) | (484.1) |
| Gross profit | 80.5 | 188.1 | 240.7 |
| Selling and distribution expenses | (2.1) | (3.0) | (4.1) |
| Administrative expenses | (12.6) | (25.4) | (37.0) |
| Other income and other gains and losses | 5.3 | 5.9 | 2.4 |
| Finance costs | (13.6) | (20.0) | (18.2) |
| Profit before tax | 57.5 | 145.6 | 183.8 |
| Taxation | (15.2) | (13.0) | (13.1) |
| Profit and total comprehensive income for the year | 42.3 | 132.6 | 170.7 |
| Profit and total comprehensive income for the year attributable to: | | | |
| Owners of the Company | 40.3 | 126.4 | 166.0 |
| Minority interests | 2.0 | 6.2 | 4.7 |
| | 42.3 | 132.6 | 170.7 |

**Business Segments**

As of 31 December 2009, we maintained three operating segments: double-sided MF tissue paper, single-sided MF tissue paper and copy paper.

### *Double-Sided MF Tissue Paper Segment*

Our double-sided MF tissue paper segment consists of the manufacturing and marketing of double-sided MF tissue paper. The table below sets out our operating results with respect to our double-sided MF tissue paper segment.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Revenue | 147.9 | 299.4 | 470.4 |
| Gross profit | 47.2 | 99.4 | 154.1 |

### *Single-Sided MF Tissue Paper Segment*

Our single-sided MF tissue paper segment consists of the manufacturing and marketing of single-sided MF tissue paper. The table below sets out our operating results with respect to our single-sided MF tissue paper segment.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Revenue | 46.0 | 171.5 | 168.6 |
| Gross profit | 11.8 | 57.0 | 57.8 |

### *Copy Paper Segment*

Our copy paper segment consists of the manufacturing and marketing of copy paper. The table below sets out our operating results with respect to our copy paper segment.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Revenue | 73.7 | 91.1 | 85.8 |
| Gross profit | 21.5 | 31.7 | 28.8 |

The following table sets forth the gross profit margin by segment as well as our combined gross profit margin for the periods indicated.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| Double-sided MF tissue paper | 31.9% | 33.2% | 32.8% |
| Single-sided MF tissue paper | 25.7% | 33.2% | 34.3% |
| Copy paper | 29.2% | 34.8% | 33.6% |
| Overall | 30.1% | 33.5% | 33.2% |

**Principal Components of Statements of Comprehensive Income**

***Revenue***

We derive revenue from sales of double-sided MF tissue paper, single-sided MF tissue paper and copy paper. For a description of our revenues from each product please refer to "Business Segments" in this section. The following table sets forth our sales volumes and average selling prices for our products for the periods indicated.

| | Year ended 31 December | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | 2008 | | 2009 | |
| | Sales volume (tonnes) | Average sales price (RMB/tonne) | Sales volume (tonnes) | Average sales price (RMB/tonne) | Sales volume (tonnes) | Average sales price (RMB/tonne) |
| Double-sided MF tissue paper | 18,697.2 | 7,909.7 | 38,079.2 | 7,863.6 | 65,848.3 | 7,144.1 |
| Single-sided MF tissue paper | 6,878.4 | 6,693.3 | 24,754.4 | 6,926.0 | 26,845.2 | 6,280.8 |
| Copy paper | 11,448.4 | 6,433.8 | 12,867.5 | 7,082.3 | 13,373.9 | 6,412.3 |
| Total | 37,024.0 | | 75,701.1 | | 106,067.4 | |

The following table sets forth the revenue derived from each of our segments and the percentage such revenue represents of our total revenue for the periods indicated.

| | Year ended 31 December | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | 2008 | | 2009 | |
| | Revenue (RMB in MN) | % of Total Revenue | Revenue (RMB in MN) | % of Total Revenue | Revenue (RMB in MN) | % of Total Revenue |
| Double-sided MF tissue paper | 147.9 | 55.3 | 299.4 | 53.3 | 470.4 | 64.9 |
| Single-sided MF tissue paper | 46.0 | 17.2 | 171.5 | 30.5 | 168.6 | 23.3 |
| Copy paper | 73.7 | 27.5 | 91.1 | 16.2 | 85.8 | 11.8 |
| Total | 267.6 | 100.0 | 562.0 | 100.0 | 724.8 | 100.0 |

***Cost of Sales***

Cost of sales represents the direct costs of production which primarily include raw materials, coal, water, electricity, labour and other costs. Raw material costs consist of primary (e.g. wood pulp, reclaimed pulp, de-inked pulp and recycled white paper) and secondary (e.g. chemicals) raw material expenses; coal costs consist of the cost of coal for our boiler plants; water costs consist of the cost of water that we purchase from state-owned utilities for our production facilities; electricity costs consist of the cost of electricity purchased from state-owned utilities; labour costs consist mainly of wage expenses and government mandated social insurance contributions for employees who work in production; and other costs consist mainly of social security costs, materials consumption costs (which includes the cost of various consumables, including gasoline and spare parts), packaging material costs, sewage treatment costs, boiler maintenance costs, depreciation expenses and other miscellaneous costs.

The following table sets forth the components of our cost of sales and, with respect to raw materials, the total number of tonnes used in production for the periods indicated.

| | Year ended 31 December | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | 2008 | | 2009 | |
| | (RMB in MN) | (tonnes) | (RMB in MN) | (tonnes) | (RMB in MN) | (tonnes) |
| Raw materials | | | | | | |
| Wood pulp | 71.1 | 14,789 | 119.6 | 25,116 | 180.2 | 47,431 |
| Reclaimed pulp | 49.0 | 16,752 | 80.5 | 28,776 | 60.1 | 23,919 |
| De-inked pulp | 8.7 | 3,059 | 55.9 | 18,331 | 56.6 | 22,672 |
| Recycled white paper | 0.1 | 47 | 1.6 | 799 | 26.0 | 12,121 |
| Chemicals | 6.0 | | 9.4 | | 13.1 | |
| Sub-total | 134.9 | | 267.0 | | 336.0 | |
| Coal | 10.7 | | 22.9 | | 29.3 | |
| Water | 0.3 | | 1.3 | | 2.0 | |
| Electricity | 11.3 | | 27.2 | | 44.6 | |
| Labour | 4.3 | | 9.4 | | 12.5 | |
| Others | | | | | | |
| Social security costs | 1.0 | | 2.4 | | 2.1 | |
| Materials consumption | 4.5 | | 7.5 | | 9.8 | |
| Packing materials | 8.6 | | 18.5 | | 23.9 | |
| Depreciation | 8.6 | | 13.7 | | 18.1 | |
| Other miscellaneous costs | 2.9 | | 4.0 | | 5.8 | |
| Sub-total | 25.6 | | 46.1 | | 59.7 | |
| Total | 187.1 | | 373.9 | | 484.1 | |

### *Selling and Distribution Expenses*

Selling and distribution expenses primarily consist of sales and marketing staff salaries and benefits, billboard advertising, depreciation of the sales department's fixed assets and other costs, which include travel, business development and automobile expenses. The table below sets forth a breakdown of our selling and distribution expenses for the periods indicated.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Sales and marketing staff costs | 0.4 | 0.6 | 1.0 |
| Advertising | 0.8 | 1.0 | 1.4 |
| Depreciation | 0.3 | 0.5 | 0.8 |
| Others | 0.6 | 0.9 | 0.9 |
| Total | 2.1 | 3.0 | 4.1 |

***Administrative Expenses***

Administrative expenses primarily consist of administrative and management staff salaries and benefits, depreciation of non-production related fixed assets and amortisation of land use rights, property and land-use taxes, business development expenses, advisory fees and other expenses, which include property insurance, stamp duties and travel expenses. The table below sets forth a breakdown of our administrative expenses for the periods indicated.

| | Year ended 31 December | | |
|---|---|---|---|
| | **2007** | **2008** | **2009** |
| | **(RMB in MN)** | **(RMB in MN)** | **(RMB in MN)** |
| Administrative staff costs | 2.5 | 6.4 | 8.7 |
| Depreciation and amortisation | 2.3 | 5.0 | 7.8 |
| Property and land-use taxes | 1.8 | 2.3 | 3.8 |
| Business development | 0.5 | 0.9 | 0.9 |
| Advisory fees | 2.0 | 3.6 | 8.8 |
| Others | | | |
| Property insurance | 0.2 | 0.3 | 0.6 |
| Stamp duties | 0.1 | 0.3 | 0.6 |
| Travel expenses | 0.1 | 0.3 | 0.4 |
| Research and development expenses | 0.1 | 0.2 | 0.4 |
| Other miscellaneous expenses[1] | 3.0 | 6.1 | 5.0 |
| Sub-total | 3.5 | 7.2 | 7.0 |
| Total | 12.6 | 25.4 | 37.0 |

*Note 1:* Other miscellaneous costs include: employment security fund contributions for the disabled, labour union expenses, labour insurance costs, provisions for bad debts, electricity tariffs and sewage disposal fees, communication costs, maintenance costs, education expenses, environment and sanitation fees, water tariffs, environmental supervision fees, technical service charges, transportation and freight costs, agency fees, office supply costs, vehicle and vessel usage license plate taxes, organisation membership fees, recruitment costs, IT and internet service costs, security and fire prevention costs, laboratory equipment costs, labour protection fees, conference costs, vehicle operation and maintenance costs, environmental protection costs, embankment protection costs, board of directors' expenses and social insurance expenses.

In the ordinary course of our business we engage a number of professional advisors and consultants to provide us with a variety of services, including legal, patent and trademark prosecution, auditing, property surveying, examination and inspection, property valuation, market research, accreditation and maintenance. While we enter into various payment arrangements with these service providers, which include hourly rate and fixed fee agreements, all of them are entered into on an arm's length basis.

In 2007, the top five service providers that we used included, with respect to PRC and other legal services and management consultancy services, a PRC bank with respect to certain financial services and a Xiamen-based production safety consultancy firm with respect to certain production safety and examination services. Each of these service providers charged us according to standard fixed fee or hourly rate fee arrangements.

For 2008 and 2009 our most significant advisory expenses related to the Reorganisation and the Global Offering. Beginning in early 2008 we engaged Fortune China as an outside consultant to assist us in preparing for the Reorganisation and Global Offering. During 2008 we also engaged Deloitte Touche Tohmatsu with respect to the preparation of audited financial information for our Group, and King & Wood for certain PRC legal services, again all in relation to our planned Reorganisation and Global Offering. In 2009, to further assist us with various aspects of our planned Reorganisation and Global Offering, we engaged Jones Lang LaSalle Sallmanns Limited with respect to real property valuation services, Orrick, Herrington & Sutcliffe with respect to Hong Kong and US legal services and Conyers Dill & Pearman with respect to certain Cayman Islands legal services. The Global Offering fees we incurred in 2009 also included certain fees incurred by the Sole Sponsor for legal services, including those of Norton Rose Hong Kong with respect to Hong Kong and US legal services and Commerce and Finance Law Offices with respect to PRC legal services. Other than Fortune China, all of our aforementioned professional advisors charge us according to standard hourly rate fee arrangements. As consideration for the consulting services provided to us by Fortune China, Mr Ke, our Chairman, transferred a 1.25% equity interest in Smart Port to Best Believe (at the direction of Fortune China) in January 2010, which was subsequently repurchased by Smart Port by transferring our Shares to Best Believe in April 2010. For further information on our compensation arrangement with Fortune China, please refer to "History and Corporate Structure — Reorganisation — Establishment of our offshore shareholding structure — Smart Port" in this prospectus.

### *Other Income and Other Gains and Losses*

Other income and other gains and losses primarily consist of: bank interest income; interest income from a loan extended by us to a shareholder; gains or losses on the disposal of property, plant and equipment; net foreign exchange gains (related to a HKD denominated loan from our Chairman, Mr Ke); donations, such as donations to Jinjiang community charities; government grants, which represent incentives granted by local PRC authorities for developing innovative production technology and maintaining a good reputation in the business community; and net rental income from investment properties leased to a related party, such as rental income from leasing a production plant in Jinjiang.

The table below sets forth a breakdown of our other income and other gains and losses for the periods indicated.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB'000) | (RMB'000) | (RMB'000) |
| Bank interest income | 360 | 911 | 1,006 |
| Gain (loss) on disposal of property, plant and equipment | — | 31 | (123) |
| Net foreign exchange gains | 4,798 | 5,094 | 244 |
| Donation | (1,365) | (1,655) | (5) |
| Government grants[1] | 850 | 1,220 | 903 |
| Gross rental income from investment properties | 1,642 | 1,642 | 1,642 |
| Less: direct operating expenses from investment properties | (913) | (913) | (913) |
| Others | (31) | (368) | (333) |
| Total | 5,341 | 5,962 | 2,421 |

*Note 1:* Government grants represented incentives granted by the local authorities to the Group's subsidiaries located in the PRC for developing innovative production technology and maintaining a good reputation in the business community. There are no unfulfilled conditions or other contingencies attached to such grants.

The decrease in our other income and other gains and losses for the year ended 31 December 2009 as compared against earlier years is primarily attributable to a decrease in charitable donations made by the Group and a decrease in net foreign exchange gains related to a significant decrease in the Group's foreign currency denominated liabilities and decreased rate of appreciation of Renminbi against the US Dollar and the Hong Kong Dollar. Please refer to Note 7 to the Accountants' Report in Appendix I to this prospectus for further information with respect to the Group's exposure to foreign currency risk.

### *Finance Costs*

Finance costs primarily consist of interest on bank borrowings and amounts due to related parties.

Since 2007, we have been capitalising certain interest expenses that relate to borrowings for qualifying assets. These qualifying assets relate directly to production plants and equipment purchased for our Huaxiang Factory and Xiyuan Factory, and specifically include: double-sided MF tissue paper production machines; single-sided MF tissue paper production machines; buildings to house such tissue paper production equipment; a warehouse; coal-fired boilers for steam production; and other miscellaneous buildings and equipment. For the years ended 31 December 2007, 2008 and 2009, we had RMB1.0 million, RMB3.3 million and RMB4.5 million, respectively, of capitalised interest related to borrowings for qualified assets.

### *Taxation*

Income tax expense represents the Hong Kong profits tax and PRC enterprise income tax which is calculated at the prevailing tax rate on the taxable income of Sunwell, our Hong Kong entity, and Youlanfa, Xiyuan and Huaxiang, our PRC entities. For the years ended 31 December 2007, 2008 and 2009, the applicable PRC enterprise income tax rate was 27%, 25% and 25%, respectively. Historically we have not paid Hong Kong profits tax as the Group did not generate any taxable income in Hong Kong during the Track Record Period. Our subsidiaries in the PRC are subject to PRC enterprise income tax. Huaxiang and Xiyuan are entitled to an exemption from the PRC enterprise income tax for two years starting from 2008 followed by a 50% tax relief for the following three years.

Our overall effective tax rate for each of the three years ended 31 December 2007, 2008 and 2009 was 26.5%, 9.0% and 7.1%, respectively. Beginning in 2013, Huaxiang and Xiyuan will no longer benefit from reduced tax rates and the applicable enterprise income tax rate is expected to revert to 25%, thereby raising the overall PRC enterprise income tax rate applicable to our operations to 25%.

### *Year Ended 31 December 2009 compared to Year Ended 31 December 2008*

#### *Revenue*

Our total revenue increased by RMB162.8 million, or 29.0%, to RMB724.8 million in the year ended 31 December 2009 from RMB562.0 million in the year ended 31 December 2008, primarily due to increases in sales volumes, particularly sales volumes of our double-sided MF tissue paper, due to increased market demand from our existing customers and demand from our new customers, especially in the East China and South China regions, changes in customer mix, with a customer base composed almost exclusively of regional distributors who typically place much larger orders than end-user customers, our production capacity expansion, and the launch of our new semi-transparent paper product. Such increase in our revenue has been partially offset by decreases in the average sales prices of each of our products as a result of decreased raw material prices from the fourth quarter of 2008 attributable to the global economic recession.

With respect to double-sided MF tissue paper, our revenue increased by RMB171.0 million, or 57.1%, to RMB470.4 million in the year ended 31 December 2009 from RMB299.4 million in the year ended 31 December 2008. The increase in revenue from double-sided MF tissue paper is primarily attributable to the launch of two double-sided MF tissue paper production lines at our Huaxiang Factory and two double-sided MF tissue paper production lines at our Xiyuan Factory in 2009 which resulted in increased production volume, partially offset by decreased average sales prices as a result of lower market prices for key raw materials including wood pulp, reclaimed pulp, de-inked pulp and white recycled paper. As a percentage of total revenue, revenue from double-sided MF tissue paper increased to 64.9% in the year ended 31 December 2009 from 53.3% during the year ended 31 December 2008, which is attributable to an increase of our overall production capacity to produce double-sided MF tissue paper resulting from the four new double-sided MF tissue paper production lines launched in 2009.

With respect to single-sided MF tissue paper, our revenue decreased by RMB2.9 million, or 1.7%, to RMB168.6 million in the year ended 31 December 2009 from RMB171.5 million in the year ended 31 December 2008. The decrease in revenue from single-sided MF tissue paper is primarily attributable to a decrease in the average sales price for single-sided MF tissue paper as a result of lower market prices for key raw materials, partially offset by increased sales volumes as a result of increased market demand. As a percentage of total revenue, revenue from single-sided MF tissue paper decreased to 23.3% in the year ended 31 December 2009 from 30.5% during the year ended 31 December 2008, which is attributable to a greater proportion of our overall production capacity being devoted to double-sided MF tissue paper on account of the four new double-sided MF tissue paper production lines launched in 2009.

With respect to copy paper, our revenue decreased by RMB5.3 million, or 5.8%, to RMB85.8 million in the year ended 31 December 2009 from RMB91.1 million in the year ended 31 December 2008. The decrease in revenue from copy paper is primarily attributable to a decrease in the average sales price for copy paper as a result of lower market prices for key raw materials, partially offset by increased sales volumes as a result of increased market demand. As a percentage of total revenue, revenue from copy paper decreased to 11.8% in the year ended 31 December 2009 from 16.2% during the year ended 31 December 2008.

*Cost of sales*

Our cost of sales increased by RMB110.2 million, or 29.5%, to RMB484.1 million in the year ended 31 December 2009 from RMB373.9 million in the year ended 31 December 2008, primarily due to increased raw material, energy and water expenses in line with increases in the sales volumes of our products, as well as increased labour costs attributable to increases in staff head count (related to additional operators for two new double-sided MF tissue paper production lines at our Xiyuan Factory that commenced operation during the year ended 31 December 2009, as well as two new double-sided MF tissue paper production lines at our Huaxiang Factory) and increased depreciation expense (related to machine purchases for four new double-sided MF tissue paper production lines at our Huaxiang and Xiyuan Factories).

*Gross profit and gross profit margin*

Our gross profit increased by RMB52.6 million, or 28.0%, to RMB240.7 million in the year ended 31 December 2009 from RMB188.1 million in the year ended 31 December 2008. The gross profit margin for each of our three business segments remained stable, with the aggregate gross profit margin across all of our segments slightly decreasing to 33.2% from 33.5% during the same period.

*Selling and distribution expenses*

Our selling and distribution expenses increased by RMB1.1 million, or 36.7%, to RMB4.1 million in the year ended 31 December 2009 from RMB3.0 million in the year ended 31 December 2008, primarily due to increased salary costs attributable to increases in sales and marketing staff head count, increased depreciation expenses (related to newly purchased office equipment for our sales office), and increased advertising expenses (related to an increase in billboard advertisements).

*Administrative expenses*

Our administrative expenses increased by RMB11.6 million, or 45.7%, to RMB37.0 million in the year ended 31 December 2009 from RMB25.4 million in the year ended 31 December 2008, primarily due to increased salary costs attributable to increases in administrative staff head count (related to expansion of our office staff at our Huaxiang and Xiyuan Factories), increased depreciation and amortisation expenses (related to office equipment purchases and newly acquired land use rights), increased property and land-use taxes and an increase in fees payable to advisors of RMB5.2 million, or 144.4%, to RMB8.8 million in the year ended 31 December 2009 from RMB3.6 million in the year ended 31 December 2008 (primarily related to a substantial increase in advisory fees related to the Reorganisation and this Global Offering).

*Other income and other gains and losses*

Our other income and other gains and losses decreased by RMB3.5 million, or 59.3%, to RMB2.4 million in the year ended 31 December 2009 from RMB5.9 million in the year ended 31 December 2008, primarily due to a decrease in foreign exchange gains related to a HKD denominated loan from our chairman, Mr Ke, and charitable donations and, to a lesser extent, a RMB0.3 million decrease in government grants, partially offset by increased interest income from bank deposits and decreased charitable donations to Jinjiang Charity Association* (晉江市慈善總會).

*Finance costs*

Our finance costs decreased by RMB1.8 million, or 9.0%, to RMB18.2 million in the year ended 31 December 2009 from RMB20.0 million in the year ended 31 December 2008, primarily due to decreases in prevailing interest rates on our fixed-rate and variable-rate bank borrowings and increased capitalised interest expenses (related to borrowings for production equipment, which are characterised as qualifying assets).

*Profit before tax*

Our profit before tax increased by RMB38.2 million, or 26.2%, to RMB183.8 million in the year ended 31 December 2009 from RMB145.6 million in the year ended 31 December 2008.

*Taxation*

Our tax expenses increased by RMB0.1 million, or 0.8%, to RMB13.1 million in the year ended 31 December 2009 from RMB13.0 million in the year ended 31 December 2008, primarily due to a slight increase in taxable profits attributable to our Youlanfa subsidiary (the profits of which were subject to the 25% PRC enterprise income tax). As our Huaxiang and Xiyuan subsidiaries enjoyed a tax exemption for 2008 and 2009 with respect to all of their taxable profits, profits attributable to these two subsidiaries did not contribute to increases in our tax expenses.

*Profit and net profit margin for the period*

Our profit increased by RMB38.1 million, or 28.7%, to RMB170.7 million in the year ended 31 December 2009 from RMB132.6 million in the year ended 31 December 2008. Our net profit margin remained the same at 23.6% for the years ended 31 December 2009 and 2008.

***Year Ended 31 December 2008 Compared to Year Ended 31 December 2007***

*Revenue*

Our revenue increased by RMB294.4 million, or 110.0%, to RMB562.0 million in the year ended 31 December 2008 from RMB267.6 million in the year ended 31 December 2007, primarily due to increases in our sales volumes, particularly sales volumes of our double-sided MF tissue paper and single-sided MF tissue paper due to stronger market demand from our existing and new customers in the North China, East China and South China regions as well as our market expansion to the Northeast China and Southwest China regions, and our production capacity expansion following the launch of new production lines at our Huaxiang Factory and Xiyuan Factory.

With respect to double-sided MF tissue paper, our revenue increased by RMB151.5 million, or 102.4%, to RMB299.4 million in the year ended 31 December 2008 from RMB147.9 million in the year ended 31 December 2007. The increase in revenue from double-sided MF tissue paper is primarily attributable to strong market demand and the launch of two double-sided MF tissue paper production lines at Huaxiang during the second half of 2007 as well as two new double-sided MF tissue paper production lines at our Xiyuan Factory in 2008. The slight decrease in average sales prices of our double-sided MF tissue paper in 2008 was primarily attributable to a decrease in our average sales prices in the last quarter of 2008, following the global financial crisis, which resulted from a decrease in raw material prices. As a percentage of total revenue, revenue from double-sided MF tissue paper decreased slightly to 53.3% in the year ended 31 December 2008 from 55.3% during the year ended 31 December 2007, primarily due to increased revenue from increased sales of our singled-sided MF tissue paper attributable to four newly launched single-sided MF tissue paper production lines during the second half of 2007.

With respect to single-sided MF tissue paper, our revenue increased by RMB125.5 million, or 272.8%, to RMB171.5 million in the year ended 31 December 2008 from RMB46.0 million in the year ended 31 December 2007. The increase in revenue from single-sided MF tissue paper is primarily attributable to strong market demand and the launch of four single-sided MF tissue paper production lines at our Huaxiang Factory during the second half of 2007 and, to a lesser extent, a moderate increase in average sales prices. The average sales price increased because we no longer had to sell our single-sided MF tissue paper at lower than market prices on account of it gaining popularity within the market since its launch during the second half of 2007. As a percentage of total revenue, revenue from single-sided MF tissue paper increased to 30.5% in the year ended 31 December 2008 from 17.2% during the year ended 31 December 2007, due to the increase in production capacity from four single-sided MF tissue paper production lines having been launched in the second half of 2007 and the increased demand for single-sided MF tissue paper.

With respect to copy paper, our revenue increased by RMB17.4 million, or 23.6%, to RMB91.1 million in the year ended 31 December 2008 from RMB73.7 million in the year ended 31 December 2007. The increase in revenue from copy paper is primarily attributable to an upward adjustment of the operating speed of our copy paper production line as a result of increased market demand, which allowed us to increase sales volumes to 12,867.5 tonnes in 2008 from 11,448.4 tonnes in 2007 and a modest increase in average sales prices made possible by the increased popularity of our copy paper and overall PRC economic growth which had the effect of increasing the general market prices for copy paper. As a percentage of total revenue, revenue from copy paper decreased to 16.2% in the year ended 31 December 2008 from 27.5% during the year ended 31 December 2007 as a result of the significant increase of the revenues from double-sided and single-sided MF tissue paper.

*Cost of sales*

Our cost of sales increased by RMB186.8 million, or 99.8%, to RMB373.9 million in the year ended 31 December 2008 from RMB187.1 million in the year ended 31 December 2007, primarily due to an increase in the cost of wood pulp, reclaimed pulp, de-inked pulp and chemicals of RMB48.5 million, RMB31.5 million, RMB47.2 million and RMB3.4 million, respectively, all of which were related to increased product production, as well as an increase in production staff head count (related to additional operators for two new double-sided MF tissue paper production lines that commenced operation at our Xiyuan Factory during the period) and increased depreciation expenses (related to machine purchases for the aforementioned new production lines at our Xiyuan Factory).

*Gross profit and gross profit margin*

Our gross profit increased by RMB107.6 million, or 133.7%, to RMB188.1 million in the year ended 31 December 2008 from RMB80.5 million in the year ended 31 December 2007. Our aggregate gross profit margin for all of our products increased to 33.5% from 30.1% during the same period.

*Selling and distribution expenses*

Our selling and distribution expenses increased by RMB0.9 million, or 42.9%, to RMB3.0 million in the year ended 31 December 2008 from RMB2.1 million in the year ended 31 December 2007, primarily due to increased salary costs attributable to increases in sales and marketing staff head count, increased advertising expenses (related to an increase in billboard advertisements), increased depreciation expense (related to newly purchased office equipment for our sales office) and increased other expenses.

*Administrative expenses*

Our administrative expenses increased by RMB12.8 million, or 101.6%, to RMB25.4 million in the year ended 31 December 2008 from RMB12.6 million in the year ended 31 December 2007, primarily due to increased salary costs attributable to increases in administrative staff head count (related to expansion of our office staff at our Huaxiang and Xiyuan Factories), fees payable to advisors (primarily related to advisory fees for the Reorganisation and this Global Offering), depreciation and amortisation expense (relating primarily to newly acquired land use rights which are amortised over a 50 year period) and increased other expenses (primarily relating to stamp duties).

*Other income and other gains and losses*

Our other income and other gains and losses increased by RMB0.6 million, or 11.3%, to RMB5.9 million in the year ended 31 December 2008 from RMB5.3 million in the year ended 31 December 2007, primarily due to a RMB0.6 million increase in bank interest income related to an increase in bank deposits, a RMB0.3 million increase in net foreign exchange gains (related to a HKD denominated loan from our Chairman, Mr Ke), a RMB0.3 million increase in government grants and a RMB0.3 million increase in other expense, partially offset by an increase of RMB0.3 million in charitable donations.

*Finance costs*

Our finance costs increased by RMB6.4 million, or 47.1%, to RMB20.0 million in the year ended 31 December 2008 from RMB13.6 million in the year ended 31 December 2007, primarily due to a RMB7.3 million increase in interest payable on bank borrowings (primarily related to higher interest rates for both our fixed-rate and variable-rate borrowings) and a RMB1.5 million increase in amounts due to a related party, partially offset by an increase of RMB2.3 million of capitalised financed costs (related to increased borrowings for qualifying assets).

*Profit before tax*

Our profit before tax increased by RMB88.1 million, or 153.2%, to RMB145.6 million in the year ended 31 December 2008 from RMB57.5 million in the year ended 31 December 2007.

*Taxation*

In spite of our substantially increased profit before tax, our tax expenses decreased by RMB2.2 million, or 14.5%, to RMB13.0 million in the year ended 31 December 2008 from RMB15.2 million in the year ended 31 December 2007, primarily due to a lowering of the PRC enterprise income tax rate from 27% to 25% and the effect of PRC enterprise income tax exemptions for Huaxiang and Xiyuan in 2008 (two-year tax exemption and three-year 50% tax rate reduction attributable to PRC enterprises). As Huaxiang and Xiyuan had profit before tax of RMB78.0 million and RMB10.9 million, respectively, for the year ended 31 December 2008, the effect of these tax exemptions was a tax savings for us of RMB22.2 million for 2008.

*Profit and net profit margin for the year*

Our profit for the year increased by RMB90.3 million, or 213.5%, to RMB132.6 million in the year ended 31 December 2008 from RMB42.3 million in the year ended 31 December 2007. Our net profit margin increased to 23.6% from 15.8% during the same period primary due to our decreased effective tax rate.

**Liquidity and Capital Resources**

During the Track Record Period, we financed our working capital, capital expenditures and other capital requirements primarily through cash generated from operations and bank credit facilities, as well as equity contributed or loaned by shareholders. Going forward, we expect that cash generated from operations and bank credit facilities, together with the proceeds of the Global Offering, will be our primary sources of liquidity as well as funding for capital expenditures.

***Cash Flows***

The following table sets out a summary of our cash flows for the periods indicated:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Operating cash flows before movements in working capital | 82.9 | 184.9 | 228.8 |
| Cash generated from operations before income taxes paid | 47.9 | 219.9 | 76.3 |
| Net cash from operating activities | 34.9 | 204.7 | 63.6 |
| Net cash used in investing activities | (215.0) | (122.5) | (244.1) |
| Net cash from (used in) financing activities | 178.4 | (81.7) | 261.5 |
| Net (decrease) increase in cash and cash equivalents | (1.7) | 0.5 | 81.0 |

*Operating cash flows before movements in working capital*

Operating cash flows before movements in working capital amounted to RMB82.9 million, RMB184.9 million and RMB228.8 million for the years ended 31 December 2007, 2008 and 2009, respectively. The increase of RMB43.9 million in operating cash flows before movements in working capital in 2009 was primarily due to an increase in revenues of RMB162.8 million during the period. The increase in operating cash flows before movements in working capital in 2008 as compared to 2007 was primarily the result of an increase in revenues of RMB294.4 million during the period.

*Cash generated from operations before income taxes paid*

Cash generated from operations before income taxes paid were RMB47.9 million, RMB219.9 million and RMB76.3 million for the years ended 31 December 2007, 2008 and 2009, respectively. We experienced net working capital requirements of RMB152.5 million in 2009 mainly attributable to a decrease of RMB53.3 million in trade and other payables (related to a decreased use of promissory notes and letters of credit in 2009 as compared to the fourth quarter of 2008, in which we made extensive use of promissory notes and letters of credit in connection with the purchase of additional wood pulp inventory), an increase of RMB83.0 million in inventories (related to the Group's increased inventory requirements due to the launch of new production lines in 2009 as well as increased wood pulp purchases which began in the fourth quarter of 2008 and continued throughout 2009) and a RMB25.4 million increase in trade and other receivables and prepayments (primarily attributable to increased trade receivables in line with sales growth during the year), partially offset by a RMB8.6 million increase in amounts due to related parties.

We experienced a net working capital surplus of RMB35.0 million in 2008, compared to net working capital requirements of RMB35.0 million in 2007. The net working capital surplus in 2008 primarily resulted from a RMB109.4 million increase in trade and other payables (primarily related to the issuance of promissory notes and letters of credit for the procurement of raw materials), partially offset by a RMB67.1 million increase in trade and other receivables and prepayments and a RMB6.7 million increase in inventories. The net working capital requirements in 2007 resulted from a RMB42.5 million increase in trade and other receivables and prepayments and a RMB5.9 million increase in inventories, partially offset by a RMB13.4 million increase in trade and other payables.

*Net cash from operating activities*

We generated net cash from operating activities of RMB34.9 million, RMB204.7 million and RMB63.6 million for the years ended 31 December 2007, 2008 and 2009, respectively. The item which accounts for differences between cash generated from operations and net cash from operating activities is income taxes paid. In the years ended 31 December 2007, 2008 and 2009, we paid income taxes of RMB13.0 million, RMB15.2 million and RMB12.7 million, respectively.

*Net cash used in investing activities*

Net cash used in investing activities was RMB215.0 million, RMB122.5 million and RMB244.1 million for the years ended 31 December 2007, 2008 and 2009, respectively. The principal components of our investing activities in the year ended 31 December 2009 were RMB153.0 million for prepaid lease payments (related to land-use rights acquired from the government), RMB120.5 million of capital expenditures for the acquisition of property, plant and equipment, primarily related to the construction of new production facilities and the procurement of new equipment, and RMB21.6 million for the purchase of additional interest in subsidiaries (related to Youlanfa, Huaxiang and Xiyuan), which was partially offset by a RMB50.0 million decrease in pledged bank deposits and RMB1.0 million of interest income from bank deposits. The principal components of our investing activities in the year ended 31 December 2008 were RMB85.4 million of capital expenditures for the acquisition of property, plant and equipment, primarily related to machinery, equipment and plant construction at our Huaxiang and Xiyuan Factories, and a RMB50.2 million increase in pledged bank deposits related to letters of credit and bank notes issued for the purchase of machinery, equipment and plant construction. The principal components of our investing activities in the year ended 31 December 2007 were RMB257.8 million of capital expenditures for the acquisition of property, plant and equipment (primarily related to expansion of our production capacity at our Huaxiang and Xiyuan Factories) and RMB61.4 million for prepaid lease payments (related to land use rights acquired from the government), partially offset by a repayment of RMB93.1 million from an ultimate controlling shareholder and a RMB3.6 million decrease in pledged bank deposits (related to a decreased use of letters of credit and bank notes) and RMB7.1 million for repayments from related parties.

*Net cash from (used in) financing activities*

Net cash from (used in) financing activities was RMB178.4 million, RMB(81.7) million and RMB261.5 million for the years ended 31 December 2007, 2008 and 2009, respectively. The principal components of our financing activities for the year ended 31 December 2009 were RMB680.5 million in new bank loans, RMB95.6 million in advances from our immediate holding company, and a RMB21.4 million advance from Mr Ke, our chairman, partially offset by RMB468.5 million in bank borrowing repayments, RMB44.7 million in repayments to related parties and RMB22.8 million in interest payments. The principal components of our cash flow used in financing activities for the year ended 31 December 2008 were RMB91.9 million in repayments to related parties, RMB366.5 million in repayments of bank borrowings and RMB21.8 million in interest payments, partially offset by RMB383.5 million of new bank borrowings raised and a RMB15.0 million advance from a shareholder. The principal components of our cash flow from financing activities for the year ended 31 December 2007 were RMB354.0 million of new bank borrowings raised, a RMB49.3 million advance from a shareholder, and RMB2.2 million in contributions from minority interests, partially offset by RMB212.8 million in repayments of bank borrowings and RMB14.3 million in interest payments.

### *Net Current Liabilities*

As of 31 March 2010, the date being the latest practicable date for the purpose of our indebtedness statement, we had net current liabilities of RMB60.9 million. The following table sets forth our current assets, current liabilities and net current liabilities as of 31 December 2009 and 31 March 2010.

| | At 31 December 2009 | At 31 March 2010 |
|---|---|---|
| | (RMB in MN) | (RMB in MN) (unaudited) |
| CURRENT ASSETS | | |
| Inventories | 110.3 | 143.5 |
| Trade and other receivables and prepayments | 154.6 | 181.2 |
| Prepaid lease payments | 5.8 | 5.8 |
| Pledged bank deposits | 2.8 | 1.8 |
| Bank balances and cash | 86.8 | 123.5 |
| | 360.3 | 455.8 |
| CURRENT LIABILITIES | | |
| Trade and other payables | 118.4 | 161.4 |
| Amounts due to related parties | 8.6 | 4.4 |
| Amount due to ultimate controlling shareholder | 1.6 | — |
| Amount due to immediate holding company | 95.6 | 140.0 |
| Income tax payables | 3.3 | 10.0 |
| Bank borrowings | 182.8 | 200.9 |
| | 410.3 | 516.7 |
| NET CURRENT LIABILITIES | (50.0) | (60.9) |

We had net current liabilities of RMB465.3 million, RMB406.3 million and RMB50.0 million as of 31 December 2007, 2008 and 2009, respectively. Following completion of the Global Offering, we expect to move from a net current liabilities position to a net current assets position. The significant reduction in our net current liability position as of 31 December 2009 as compared to 31 December 2008 is primarily attributable to our paying off a portion of our short-term borrowings and replacing such liabilities with long-term borrowings, the waiver of RMB111.6 million in related party loans by our ultimate controlling shareholder, our increased inventories, trade and other receivables and prepayments, a decrease in amounts due to related parties as well as a decrease in trade and other payables, partially offset by an increase in amount due to our immediate holding company. The moderate decrease in our net current liability position as of 31 December 2008 as compared to 31 December 2007 was primarily due to increases in pledged bank deposits, trade receivables and prepayments to suppliers, as well as a decrease in amounts due to related parties, which was substantially offset by an increase in trade and other payables.

Our current assets as of 31 December 2009 mainly comprised RMB110.3 million of inventories, RMB154.6 million of trade and other receivables and other prepayments, and RMB86.8 million of bank balances and cash. Our current liabilities as of 31 December 2009 mainly comprised RMB118.4 million of trade and other payables, RMB8.6 million of amounts due to related parties, RMB95.6 million of amounts due to our immediate holding company and RMB182.8 million of bank borrowings. The amounts due to our immediate holding company, which was RMB95.6 million as of 31 December 2009 and RMB140.0 million as of 31 March 2010, relates to shareholder loans made following payments by Cathay to Smart Port pursuant to the Cathay Subscription Agreement as well as a loan extended to Smart Port by Cathay pursuant to the Smart Port Loan Agreement. The RMB140.0 million was fully converted to equity in May 2010 and thus is no longer recognised as a current liability. Please refer to "History and Corporate Structure — Investment by Cathay Special Paper" in this prospectus for further details on the Cathay Subscription Agreement, the Smart Port Loan Agreement and the transactions contemplated thereby.

For the two years ended 31 December 2008, we substantially relied on short-term bank borrowings to finance our operations and production capacity expansion, including construction of new production facilities, purchasing production equipment and funding our general working capital requirements. We used short-term borrowings in the past primarily due to their lower interest rates, as compared to long-term borrowings.[1] In addition, the level of our capital expenditures was less significant and our purpose for borrowing was more driven by financing short-term working capital needs, so short-term borrowings better suited our needs. Despite our net current liability position during the Track Record Period, we did not default on the payment of any of our borrowings, or experience any difficulty in raising longer term borrowings with our principal banks or rolling over any of our short-term borrowings. In an effort to improve our capital structure by using long-term financing to fund our investments in long-term assets, as of 31 December 2009 we had long-term bank borrowings of RMB340.2 million, allowing us to partially pay off our short-term bank borrowings. As of 31 December 2009, the weighted average interest rate of our short-term and long-term bank borrowings was 4.8% and 4.9%, respectively. Going forward, we intend to finance a higher proportion of our operations and expansion with long-term borrowings.

We intend to continue to fund our future development and debt servicing costs from existing financial resources and cash generated from operations. We may also raise additional funds through debt or equity offerings or sales or other dispositions of assets in the future to finance all or a portion of our future development, for debt servicing or for other purposes. Our ability to obtain adequate financing to satisfy our debt service requirements may be limited by our financial condition and results of operations and the liquidity of international and domestic financial markets. If our cash flow from operating activities becomes insufficient to service our debt, we could be forced to take certain actions which had not previously formed part of our strategy, including delaying or reducing capital and other expenditures and the restructuring or refinancing of our debt, selling our assets or operations, or raising capital through the sale of additional equity.

*Note 1:* The benchmark interest rates since 1991 set by the PBOC demonstrate that interest rates for short-term loans have always been lower than interest rates for long-term loans. For example, during 2007, the benchmark interest rates for loans between six months and one year ranged from 5.6% to 6.3%, while the benchmark interest rates for loans between one and three years ranged from 6.6% to 7.6%. During 2008, the benchmark interest rates for loans between six months and one year ranged from 4.9% to 6.6%, while the benchmark interest rates for loans between one to three years ranged from 5.4% to 7.6%.

### *Indebtedness*

As of 31 March 2010, the date being the latest practicable date for the purpose of this indebtedness statement, we had total borrowings of RMB712.4 million, which comprised RMB568.0 million of bank borrowings, RMB4.4 million of amounts due to related parties and RMB140.0 million of amounts due to our immediate holding company. The following table sets forth our bank borrowings as of the dates indicated.

| | As of 31 December | | | As at 31 March |
|---|---|---|---|---|
| | 2007 | 2008 | 2009 | 2010 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) | (RMB in MN) (unaudited) |
| Secured bank borrowings | 128.0 | 286.5 | 403.0 | 448.0 |
| Unsecured bank borrowings | 166.0 | 24.5 | 120.0 | 120.0 |
| Total | 294.0 | 311.0 | 523.0 | 568.0 |
| The amount is repayable as follows: | | | | |
| Within one year | 294.0 | 311.0 | 182.8 | 200.9 |
| More than one year, but not exceeding two years | — | — | 71.3 | 98.4 |
| More than two years, but not exceeding five years | — | — | 268.9 | 268.7 |
| Total | 294.0 | 311.0 | 523.0 | 568.0 |

As of 31 March 2010, we had secured and unsecured bank borrowings amounting to RMB568.0 million, which were comprised of short-, medium- and long-term loan agreements and revolving credit facilities, all of which were denominated in RMB. As of 31 March 2010, we had RMB35.0 million available under undrawn bank credit facilities, with the expiry dates for such facilities ranging from 9 July 2010 to 29 October 2010. With respect to all bank borrowings that are scheduled to fall due during 2010, we have received written confirmations from our banks that such obligations will, subject to the expiry of the relevant bank credit facilities, be rolled-over on similar terms upon our request. With respect to all outstanding bank borrowings that are scheduled to fall due beyond 2010, we expect to be able to either refinance using bank facilities or repay using cash flow from operations.

Our secured bank borrowings are secured by a certain portion of our assets as well as guarantees by certain related parties of the Group that have been released on or before Listing. As of 31 March, 2010, 78.9% of our bank borrowings consisted of secured debt.

As of 31 March 2010, we had balances due to related parties in the amount of RMB144.4 million, including amount due to our immediate holding company of RMB140.0 million and amount due to other related parties of RMB4.4 million. These obligations to our immediate holding company and other related parties were subsequently settled before the Latest Practicable Date.

Our Directors confirm that there has been no material change in the Company's indebtedness and contingent liabilities since 31 March 2010.

Except as disclosed above, as of 31 March 2010 we did not have any outstanding debt securities issued and outstanding or authorised or otherwise created but unissued, term loans, other borrowings or indebtedness in the nature of borrowing including bank overdrafts, liabilities under acceptances (other than normal trade bills), acceptance credits, hire purchase commitments, mortgages and charges, material contingent liabilities or guarantees.

***Certain Financial Ratios***

| | 2007 | 2008 | 2009 |
|---|---|---|---|
| Gearing ratio [1] | 40% | 34% | 40% |
| Return on equity [2] | 31% | 60% | 40% |
| Return on total assets [3] | 7% | 15% | 15% |
| Current ratio [4] | 0.18 | 0.35 | 0.88 |
| Quick ratio [5] | 0.14 | 0.30 | 0.60 |

*Notes:*

1 The gearing ratio is calculated by dividing bank borrowings with total assets as at the end of the respective period, and then multiplying by 100%.

2 Return on equity equals the profit attributable to owners of the Company divided by the average balance of equity attributable to owners of the Company for the respective years, and then multiplying by 100%.

3 Return on total assets equals the profit attributable to owners of the Company divided by the average balance of total assets of the Company for the respective years, and then multiplying by 100%.

4 The current ratio is calculated by dividing current assets with current liabilities as at the end of the respective period.

5 The quick ratio is calculated by dividing the balance of current assets less inventories and prepaid lease payments, with current liabilities as at the end of the respective period.

*Gearing ratio*

The Group's gearing ratio increased from 34% as of 31 December 2008 to 40% as of 31 December 2009. This is mainly due to the Group securing a substantial amount of long-term bank borrowings during 2009 in order to support the Group's current and future capital expenditures.

The Group's gearing ratio decreased modestly from 40% as of 31 December 2007 to 34% as of 31 December 2008. This was mainly due to the Group's strong cash flow from operating activities in 2008, which as a consequence allowed greater use of operational cash flow to finance capital expenditures during 2008. Consequently, the rate of increase with respect to our bank borrowings is relatively lower than the increase in our total assets during the period.

*Return on equity*

Our return on equity decreased from 60% as of 31 December 2008 to 40% as of 31 December 2009, as a result of the higher growth in the equity attributable to owners of the Group than that in net profit attributable to owners of the Group, which was primarily caused by Mr Ke, the ultimate controlling shareholder of the Group, waiving an amount due to him of RMB111.6 million which was then recorded in capital reserve for 2009.

Our return on equity increased from 31% as of 31 December 2007 to 60% as of 31 December 2008, primarily due to the substantial increase in net profit attributable to owners of the Group as a result of increased revenue and increased profitability, and relatively slower growth of the equity attributable to owners of the Group during the same period.

*Return on total assets*

As the percentage in terms of average equity attributable to owners of the Group divided by average total assets which increased from 26% as of 31 December 2008 to 37% as of 31 December 2009 was offset by a decrease in return on equity during the same period, our return on total assets remained the same as of 31 December 2008 and 2009 at 15%.

As the Group maintained a relatively stable percentage in terms of average equity attributable to owners of the Group divided by average total assets, our return on total assets also increased from 7% as of 31 December 2007 to 15% as of 31 December 2008 as a result of an increase in return on equity during the same period.

*Current ratio*

Our current ratio increased from 0.35 as of 31 December 2008 to 0.88 as of 31 December 2009, primarily due to an increase in inventories as a result of business growth and increased purchases of wood pulp beginning in the fourth quarter of 2008, the waiver of loans extended to the Group by the ultimate controlling shareholder and a decrease in short-term bank borrowings as a result of the Group's efforts to replace significant portions of its short-term bank borrowings with long-term bank borrowings. As at 31 December 2008 and 2009 the balance of our short-term bank borrowings was RMB311.0 million and RMB182.8 million, respectively.

Our current ratios as of 31 December 2007 and 2008 were 0.18 and 0.35, respectively, which were relatively low on account of the Group's use of significant short-term borrowings and loans extended by the Group's ultimate controlling shareholder, most of which was used to finance the rapid growth of the Group's operations and capital expenditures. The increase between 2007 and 2008 was primarily due to increases in trade and other receivables and prepayments, pledged bank deposits in relation to banking facilities as our business expanded, and a decrease in amounts due to related parties.

*Quick ratio*

Our quick ratio increased from 0.30 as of 31 December 2008 to 0.60 as of 31 December 2009, primarily due to the waiver of loans extended to the Group by the ultimate controlling shareholder and a decrease in short-term bank borrowings as a result of the Group's efforts to replace significant portions of its short-term bank borrowings with long-term bank borrowings. Our quick ratio increased less than our current ratio between 2008 and 2009 as inventories are deducted from the determination of current assets for the purposes of the quick ratio calculation and we experienced significant inventory growth between 31 December 2008 and 2009.

The increase in our quick ratio from 0.14 as of 31 December 2007 to 0.30 as of 31 December 2008 was primarily due to increases in trade and other receivables and prepayments, pledged bank deposits in relation to banking facilities as our business expanded, and a decrease in amounts due to related parties.

**Capital Commitments**

The following table sets forth information regarding our capital commitments as of 31 December 2007, 2008 and 2009.

| | As at 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Capital expenditure contracted for but not provided in the Financial Information in respect of: | | | |
| Acquisition of property, plant and equipment | 48.7 | 7.1 | 83.4 |
| Acquisition of additional interest in subsidiaries from minority interests | — | 2.1 | — |
| Total | 48.7 | 9.2 | 83.4 |

**Capital Expenditures**

The Youlanfa, Xiyuan and Huaxiang investment plans are expected to require total capital expenditures of approximately RMB1.57 billion to be made between 2010 and 2012. Of this amount, we intend to dedicate approximately RMB34.0 million towards expansion of the Youlanfa Factory, which will be applied towards investments in production lines, approximately RMB723.7 million towards expansion of the Xiyuan Factory, which will be applied towards expansion of production lines, waste water treatment equipment and ancillary facilities, including de-inking facilities and a cogeneration plant, and approximately RMB807.6 million towards expansion of the Huaxiang Factory, which will be applied towards expansion of production lines, waste water treatment equipment and ancillary facilities, including de-inking facilities.

Our current capital expenditure plans for the periods indicated are summarised in the following table:

| | Expected Capital Expenditures | | |
|---|---|---|---|
| | 2010 | 2011 | 2012 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Production Facilities | | | |
| Double-sided MF tissue paper production capacity expansion [1] | 129.2 | 165.0 | 14.3 |
| Single-sided MF tissue paper production capacity expansion [2] | 15.9 | 206.5 | 227.9 |
| Copy paper production capacity expansion | 35.3 | 3.4 | 99.0 |
| Ivory board production capacity | 8.0 | — | — |
| Paper towel production capacity | 13.1 | 0.8 | — |
| Acquisition of land use rights | 27.7 | — | — |
| Other property, plant and equipment expenditures | 324.5 | 173.3 | 124.5 |
| Total | 553.7 | 549.0 | 465.7 |

*Notes:*

1 Includes planned capital expenditures for food wrapping paper production capacity.

2 Includes planned capital expenditures for coloured single-sided MF tissue paper production capacity.

The above described expected capital expenditures constitute forward-looking statements. Please refer to "Forward-Looking Statements" in this prospectus for more details.

Our expansion plans are further described in the "Summary" and "Business" sections of this prospectus.

We anticipate that our capital expenditures from 2010 through 2012 will be financed primarily by the proceeds from the Global Offering, as well as cash from operations and bank borrowings. We may also rely on additional equity or debt financing. Our actual capital expenditures may be significantly higher or lower than these planned amounts due to various factors, including but not limited to unplanned cost overruns, our ability to generate sufficient cash flows from operations and our ability to obtain adequate external financing for these planned capital expenditures. In addition, we cannot assure you whether, or at what cost, our planned or other possible capital projects will be completed or that these projects will be successful if completed. Please refer to "Risk Factors — Risks Relating to Our Business and Our Group — We may be unable to implement our expansion plans in full, within budget or on schedule or sustain the considerable business growth that we have experienced during the Track Record Period" in this prospectus for more details.

### Inventory Management

We seek to maintain a low level of inventory of raw materials and finished products. We generally keep an inventory level of two to four weeks supply for most raw materials, although we follow a "just in time" policy for reclaimed pulp which we source locally and do not need to inventory in significant quantities. From time to time we may increase our purchases of raw materials when we believe that the cost of raw materials and our estimates of production and sales make it prudent to do so. For example, during the fourth quarter of 2008 we began increasing our purchases of wood pulp, which caused an increase in our inventory starting in mid-2009 (when we began taking delivery of the larger wood pulp orders) up from approximately two to four weeks of production requirements to approximately two months of production requirements, as we considered wood pulp prices at the time to be particularly attractive. Our inventory of work in progress is comprised of the volume of paper products under production at the time of determination. Our inventory of finished goods is comprised of products awaiting delivery to customers, products produced in anticipation of existing customers' demand and products produced and stored to meet unexpected demand. We do not normally make provisions for inventory obsolescence as wood pulp, reclaimed pulp and recovered paper, our primary raw materials, as well as finished products are generally not susceptible to obsolescence by passage of time.

The following table sets forth our inventory of raw materials, work in progress and finished goods as at the end of the periods indicated and average inventory turnover days for the periods indicated:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Raw materials | 13.4 | 15.9 | 99.5 |
| Work in progress | 0.8 | 0.0 | 0.1 |
| Finished goods | 6.6 | 11.6 | 10.7 |
| Total | 20.8 | 27.5 | 110.3 |
| Average inventory turnover days | 34.7 | 23.6 | 51.9 |

The following table sets forth as of 31 March 2010 the yet to be used/sold portion of our inventory of raw materials, work in progress and finished goods as of 31 December 2009 and indicated in the table above:

| | As of 31 March 2010 |
|---|---|
| | (RMB in MN)<br>(unaudited figures) |
| Raw materials | 32.5 |
| Work in progress | — |
| Finished goods | 2.4 |
| Less: allowance for obsolete inventory | (0.1) |
| Total | 34.8 |

As of 31 December 2007, 2008 and 2009, our average inventory turnover days, which equals average inventory values divided by cost of sales and then multiplied by 365, was 34.7 days, 23.6 days and 51.9 days, respectively. The decrease in our inventory turnover days between 2007 and 2008 is primarily attributable to coincidentally low inventory levels as at 1 January 2008 and 31 December 2008. The increase in inventory turnover days for the year ended 31 December 2009 is attributable to our decision to begin increasing our purchases of wood pulp starting from the fourth quarter of 2008, which subsequently increased our inventory from approximately two to four weeks of production requirements to approximately two months of production requirements.

**Trade and Other Receivables and Prepayments**

The following table sets forth the value of our trade and other receivables and prepayments as at the end of the periods indicated and average trade receivables turnover days for the periods indicated:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Trade receivables | 58.6 | 92.5 | 134.0 |
| Prepayments to suppliers | 3.2 | 35.6 | 13.7 |
| Other prepayments | 0.2 | 1.1 | 5.4 |
| Other tax recoverable | — | — | 1.2 |
| Others | 0.1 | — | 0.3 |
| Total | 62.1 | 129.2 | 154.6 |
| Average trade receivables turnover days | 53.1 | 49.1 | 57.0 |

The following table sets forth as of 31 March 2010 the unsettled/unrecognised balance of our trade receivables and prepayments to suppliers outstanding as of 31 December 2009 and indicated in the table above:

| | As of 31 March 2010 |
|---|---|
| | (RMB in MN)<br>(unaudited figures) |
| Trade receivables | — |
| Prepayments to suppliers | 1.3 |
| Total | 1.3 |

During the year ended 31 December 2009, our use of prepayments, which consist of letters of credit and notes issued on our behalf by banks, significantly decreased due to our election to use notes payables in the fourth quarter of 2008 as consideration for certain large orders of wood pulp, which we placed so as to take advantage of attractive wood pulp prices. For larger raw material orders we will often use notes payables as their increased arrangement fees can be more than offset by slightly lower interest expense as compared to letters of credit (i.e. unlike letters of credit, notes payables allow the Company to continue to earn interest on a portion of the funds covered by the note, which partially offsets the interest charged for the note), and notes payables provide additional flexibility as they are typically effective for six months as opposed to three months of effectiveness for letters of credit. As raw material prices stabilised in 2009 we returned to settling orders with our suppliers using more conventional trade payables, which in turn reduced the principal amount of the letters of credit and notes we requested to consummate orders placed in 2009. The significant use of notes payable in the fourth quarter of 2008 to place larger orders for wood pulp also accounts for the significant increase in our balance of prepayments to suppliers as of 31 December 2008 as compared to 31 December 2007.

As of 31 December 2007, 2008 and 2009, our average turnover days for trade receivables (or debtor's turnover days), which equals average trade receivables values divided by sales and then multiplied by 365, was 53.1 days, 49.1 days and 57.0 days, respectively. Our trade receivables turnover days has remained fairly steady throughout the Track Record Period.

As our production capacity and revenue have increased, our working capital requirements have also increased. We actively manage the level of our trade and other receivables and prepayments. Trade and other receivables and prepayments have steadily increased during the Track Record Period which is in line with our increased sales revenue. Prepayments to suppliers generally represent letters of credit, which are generally issued to foreign suppliers, and bank notes, which are generally issued to domestic suppliers. Other taxes recoverable generally represent value added tax recoverable, while others include government grants provided by the Jinjiang Finance Bureau to encourage scientific and technological innovations.

It is our policy to grant all our customers a credit period of 60 days. At the end of each fiscal year we consider whether full provision for overdue debts should be made. In making this judgement, we review the carrying amounts of our assets to determine whether there is any indication that those assets have suffered an impairment loss. In determining whether an impairment loss may be required, we take into consideration the ageing status and the likelihood of payment default. We have not had any substantial bad debt or doubtful accounts during the Track Record Period. We periodically review the payment status of our accounts receivables and take appropriate measures to collect overdue accounts. As a policy, we will make full provisions for bad debt if it remains overdue for more than two years.

The following table sets forth an ageing analysis with respect to our trade receivables at the end of the periods indicated:

| | At 31 December | | |
|---|---|---|---|
| | **2007** | **2008** | **2009** |
| | **(RMB in MN)** | **(RMB in MN)** | **(RMB in MN)** |
| 0 to 30 days | 34.9 | 60.0 | 90.4 |
| 31 to 60 days | 18.9 | 28.5 | 43.6 |
| 61 to 90 days | 3.6 | 2.7 | — |
| 91 to 180 days | 1.2 | 1.3 | — |
| Total | 58.6 | 92.5 | 134.0 |

### Trade and Other Payables

The following table sets forth our trade and other payables as at the end of the periods indicated and average trade and notes payable turnover days for the periods indicated:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Trade payables | 32.8 | 20.6 | 67.5 |
| Notes payables | 8.6 | 119.7 | 13.2 |
| | 41.4 | 140.3 | 80.7 |
| Other payables for acquisition of plant and equipment | 4.0 | 9.5 | 6.9 |
| Other tax payables | 6.5 | 9.0 | 7.1 |
| Accrued staff costs | 1.4 | 2.3 | 2.8 |
| Accrued employee social insurance | 2.7 | 6.5 | 9.8 |
| Accrued electricity expenses | 1.9 | 3.4 | 4.9 |
| Other accrued expenses | 1.4 | 3.2 | 6.1 |
| Total | 59.3 | 174.2 | 118.3 |
| Average trade and notes payables turnover days | 75.6 | 88.7 | 83.3 |

The following table sets forth as of 31 March 2010 the unsettled balance of our trade payables and notes payables outstanding as of 31 December 2009 and indicated in the table above:

| | As of 31 March 2010 |
|---|---|
| | (RMB in MN) (unaudited figures) |
| Trade payables | 0.2 |
| Notes payables | 1.5 |
| Total | 1.7 |

The significant increase in our use of notes payables during 2008 is attributable to our election to use notes payables (as opposed to letters of credit) in the fourth quarter of 2008 as consideration for certain large orders of wood pulp, which we placed so as to take advantage of attractive wood pulp prices. For larger raw material orders we will often use notes payables as their increased arrangement fees can be more than offset by a slightly lower interest expense as compared to letters of credit (i.e. unlike letters of credit, notes payables allow the Company to continue to earn interest on a portion of the funds covered by the note, which partially offsets the interest charged for the note), and notes payables provide additional flexibility as they are typically effective for six months as opposed to three months of effectiveness for letters of credit. The decrease in notes payables as of 31 December 2009 was due to the fact that raw material prices became more stable in 2009, which caused us to return to settling orders with our suppliers using more conventional trade payables. The increase in accrued employee social insurance expenses during 2008 is primarily related to a proportionate increase in our overall average staff head count, which increased by 569 to 1,138 in 2008 from 569 for 2007.

As of 31 December 2007, 2008 and 2009, our average turnover days for trade and notes payables (or creditor's turnover days), which equals average trade and notes payable values divided by cost of sales and then multiplied by 365, was 75.6 days, 88.7 days and 83.3 days, respectively. Our trade and notes payable turnover days has remained fairly steady throughout the Track Record Period.

As our production capacity and revenue have increased, our working capital requirements have also increased. Most of our trade and other payables are expected to be settled within one year.

The following table sets forth an ageing analysis of our trade payables at the end of the periods indicated:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| Within 30 days | 21.8 | 11.6 | 42.2 |
| 31 to 90 days | 10.9 | 8.9 | 25.3 |
| 91 to 120 days | 0.1 | 0.1 | 0.0 |
| 121 to 180 days | 0.0 | — | — |
| Total | 32.8 | 20.6 | 67.5 |

The following table sets forth an ageing analysis of our notes payables at the end of the periods indicated:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | (RMB in MN) | (RMB in MN) | (RMB in MN) |
| 31 to 90 days | 2.1 | 41.5 | — |
| 91 to 120 days | — | 45.7 | 8.6 |
| 121 to 180 days | 6.5 | 32.5 | 4.6 |
| Total | 8.6 | 119.7 | 13.2 |

Trade payables and notes payables are principally comprised of amounts outstanding for the purchase of raw materials. Our suppliers typically extend to us credit periods of 60 to 180 days for the purchase of raw materials and equipment. We have established financial risk management policies to ensure that all payables are settled within the credit periods.

### Working Capital

Taking into account our cash inflows from operating and financing activities, cash received from bank borrowings, and the estimated net proceeds from the Global Offering, our Directors believe that we have sufficient working capital for our present requirements and for at least the next 12 months from the date of this prospectus.

### Off-Balance Sheet Arrangements and Contingent Liabilities

As of 31 December 2009, we did not have any off-balance sheet arrangements or contingent liabilities.

### Quantitative and Qualitative Disclosure about Market Risk

Our major financial instruments include trade and other receivables, amounts due from or to related parties, pledged bank deposits, bank balances and cash, trade and other payables, amounts due from or to a shareholder, amount due to an immediate holding company and bank borrowings. The risks associated with these financial instruments include currency risk, interest rate risk, credit risk and liquidity risk. We do not enter into any hedging transactions and therefore do not use hedge accounting.

The risks associated with our financial instruments are set out below.

#### *Currency Risk*

We are exposed to foreign currency risk on the portion of our bank deposits that we maintain in US dollars and HKD, as well as with respect to a loan from our Chairman, Mr Ke, that is denominated in HKD. The carrying amount of our HKD denominated loans as of 31 December 2009, 2008 and 2007 was RMB1.6 million, RMB91.9 million and RMB88.6 million, respectively, or 0.4%, 14.7% and 15.5% of our total current liabilities, respectively. As of 31 December 2009 and 31 December 2008, the carrying amount of our US dollar denominated liabilities was RMB108.8 million and RMB7.2 million, respectively. The increase in our US dollar liabilities for 2009 relates to an amount due to our immediate holding company with a carrying value of RMB95.6 million as of 31 December 2009. As of the Latest Practicable Date, we did not have any US dollar denominated loans.

#### *Interest Rate Risk*

Interest rate risk is the risk that the value of our financial instruments and variable-rate debt will fluctuate due to changes in market interest rates. We rely on financing part of our working capital and certain long-term assets with credit facilities, short-term bank loans, borrowings from related parties and other borrowings. As of the 31 December 2009, RMB350.0 million or 66.9% of our total bank borrowings consisted of floating rate borrowings.

***Credit Risk***

Credit risk is the risk that our customers will not discharge their obligations at the respective due dates. We believe that our exposure to credit risk is limited as historically we have incurred negligible bad debts.

***Liquidity Risk***

Liquidity risk is the risk that we will not be able to liquidate our assets for value sufficient to cover our financial liabilities. We believe that our exposure to liquidity risk is limited by maintaining sufficient cash and marketable securities and adequate committed credit facilities.

For additional information on our exposure to currency, interest rate, credit and liquidity risks please refer to Note 7b to the Accountants' Report included in Appendix I to this prospectus.

**Dividend Policy**

During the Track Record Period, we did not declare any dividends. In the future, we may distribute dividends by way of cash or by other means that we consider appropriate. Dividends may be declared and paid out of profits of the Company, realised or unrealised, or from any reserve set aside from profits which the Board determines is no longer needed, or not in the same amount. Dividends may also be declared and paid out of the share premium account or any other fund or account which can be authorised under the Companies Law for this purpose. No unpaid dividend shall bear interest as against the Company. A decision to declare and pay any dividends would require the approval of our Board and will be at its discretion. In addition, any final dividend for a financial year will be subject to our Shareholders' approval. The payment and the amount of any dividends declared will be subject to our Articles of Association and the Companies Law. No dividends are payable if doing so would render our Company unable to pay our liabilities as they become due or if the realisable assets would be less than the aggregate of our liabilities and our issued share capital.

The timing, amount and form of future dividends, if any, will depend on, inter alia:

- our results of operations and cash flows;
- our future prospects;
- general business conditions;
- our capital requirements and surplus;
- contractual restrictions on the payment of dividends by us to our Shareholders or by our subsidiaries to our Company;
- taxation considerations;
- possible effects on our Company's creditworthiness;

- statutory and regulatory restrictions; and
- any other factors our Board may deem relevant.

Our Company's ability to pay cash dividends will also depend upon the amount of distributions, if any, received by the Company from our PRC operating subsidiaries. Under PRC laws, dividends may be paid only out of distributable profits calculated according to the PRC GAAP, which differs from generally accepted accounting principles in other jurisdictions. Any distributable profits that are not distributed in a given year are retained and available for distribution in subsequent years.

There can be no assurance that any dividends will be paid. Investors should consider the risk factors affecting our Group as set forth in the section titled "Risk Factors" and the cautionary notice regarding forward-looking statements contained in the section titled "Forward-Looking Statements".

**Unaudited Pro Forma Statement of Adjusted Net Tangible Assets**

The following is an illustrative and unaudited pro forma statement of adjusted combined net tangible assets of our Company, which has been prepared on the basis of the notes set out below for the purpose of illustrating the effect of the Global Offering as if it had taken place on 31 December 2009. This unaudited pro forma statement of adjusted combined net tangible assets has been prepared for illustrative purposes only and because of its hypothetical nature, it may not give a true picture of our financial position had the Global Offering been completed as at 31 December 2009 or at any future date.

| | Audited combined net tangible assets of the Group attributable to owners of the Company as of 31 December 2009 | Estimated net proceeds from the Global Offering[1] | Unaudited pro forma adjusted combined net tangible assets of the Group attributable to owners of our Company | Unaudited pro forma adjusted combined net tangible assets attributable to owners of the Company per Share[2 3] | |
|---|---|---|---|---|---|
| | RMB'000 | RMB'000 | RMB'000 | RMB[2] | HK$[3] |
| Based on an Offer Price of HK$2.58 per Offer Share . . . | 554,847 | 524,360 | 1,079,207 | 1.08 | 1.23 |
| Based on an Offer Price of HK$3.38 per Offer Share . . . | 554,847 | 692,684 | 1,247,531 | 1.25 | 1.42 |

*Notes:*

1 The estimated net proceeds from the Global Offering are based on 250,000,000 new Shares at the indicative Offer Price of HK$2.58 and HK$3.38 per Offer Share, respectively, after deduction of the underwriting fees and other related expenses payable by the Company (excluding other related expenses of approximately RMB12.6 million which have been paid or accrued as of 31 December 2009). No account has been taken of the Shares that may be issued pursuant to any exercise of Over-allotment Option.

2 The unaudited pro forma adjusted combined net tangible assets attributable to owners of the Company as of 31 December 2009 per Share is based on 1,000,000,000 Shares expected to be in issue immediately following completion of the Global Offering. No account has been taken of the Shares that may be issued pursuant to any exercise of Over-allotment Option.

3 The unaudited pro forma adjusted combined net tangible asset attributable to owners of the Company per Share is translated into Hong Kong dollar at an exchange rate of RMB0.87898 to HK$1.00, the rate of The People's Bank of China prevailing on 6 May 2010. No representation is made that the Renminbi amounts have been, could have been or may be converted to Hong Kong dollars, or vice versa, at that rate.

4 By comparing the valuation of the Group's property interests of RMB539.3 million as set out in Appendix IV to this prospectus and the unaudited net book value of these properties including buildings held for own use, investment properties and prepaid lease payments of RMB539.8 million as of 28 February 2010, there is net valuation deficit of approximately RMB0.5 million. Accordingly, there is no additional annual depreciation expense would be charged against profit or loss.

**Profit Forecast for the Six Months Ending 30 June 2010**

The Directors have prepared the forecast of our Group's combined profit attributable to Shareholders of our Company for the six months ending 30 June 2010 based on the unaudited management accounts of our Group for the two months ended 28 February 2010 and a forecast of the combined results of our Group for the remaining four months ending 30 June 2010. The forecast for the six months ending 30 June 2010 has been prepared on bases consistent in all material respects with the accounting policies adopted by our Group and its associates as set out in the Accountants' Report in Appendix I to this prospectus.

| | |
|---|---|
| Forecast of combined net profit attributable to the Shareholders of our Company[1] | Not less than RMB82 million |
| Unaudited pro forma forecast earnings per Share[2] | Not less than RMB0.08 (HK$0.09) |

*Notes:*

1 The above profit forecast has been prepared on the bases and assumptions set out in Appendix III to this prospectus.

2 Solely for your convenience, forecast earnings per Share are converted into Hong Kong dollars at the exchange rate of RMB0.87898 to HK$1.00, the rate of the People's Bank of China prevailing on 6 May 2010. You should not construe such conversion as a representation that the Renminbi amounts could actually be converted into HK dollar amounts at the rate indicated or at all. The calculation of the forecast earnings per Share on a pro forma fully diluted basis is based on the forecast combined profit attributable to Shareholders for the six months ending 30 June 2010, assuming that we had been listed since 1 January 2010 and a total of 1,000,000,000 Shares were in issue during the period. This calculation assumes that the Over-allotment Option will not be exercised.

The Company undertakes that the interim report for the six months ending 30 June 2010 will be audited pursuant to Rule 11.18 of the Listing Rules.

**Related Party Transactions**

During the Track Record Period, we entered into various transactions with related parties for the acquisition of land use rights. The consideration for each such acquisition was determined by reference to the valuation of the land use rights as contained in the relevant property valuation report, except for an acquisition of land use rights by Youlanfa from YLF Industry for approximately RMB2.48 million in 2007, which was determined through negotiation between the parties.

During the two years ended 31 December 2009, in order to ensure supply for our increased demand in raw materials, in particular wood pulp and recovered paper, we purchased some of our wood pulp and recovered paper from Zhangzhou Shunxiong Trading Co., Ltd. (漳州順雄貿易有限公司) on normal commercial terms. The total purchase from Zhangzhou Shunxiong Trading Co., Ltd. (漳州順雄貿易有限公司) amounted to approximately RMB35.6 million and RMB87.6 million for each of the two years ended 31 December 2009, respectively. We do not intend to continue to acquire raw materials from Zhangzhou Shunxiong Trading Co., Ltd. (漳州順雄貿易有限公司) after the Listing and instead expect to procure such raw materials from independent wood pulp and recovered paper suppliers.

During the Track Record Period, certain related parties provided guarantees for our bank borrowings and we pledged certain assets of our Group in respect of banking facilities for YLF Leathercover and YLF Industry. Our Directors confirm that all guarantees by related parties of the Group to secure banking facilities granted to our Group were cancelled as of the Latest Practicable Date. Our Directors further confirm that all pledges relating to Group assets offered to secure banking facilities granted to our related parties were cancelled as of the Latest Practicable Date.

As of 31 December 2007, 2008 and 2009, we had RMB12.1 million, RMB0.6 million and nil due from related parties, and RMB211.9 million, RMB136.6 million and RMB105.8 million due to our related parties, respectively .

Regarding the amounts due to our related parties, the balances due to Mr Ke, our Controlling Shareholder, as of 31 December 2007, 2008 and 2009, were in the amount of RMB88.6 million, RMB91.9 million and RMB1.6 million, respectively. Mr Ke obtained the funding for such loans to us through personal loans from Mr Ke Qingkai, a cousin of Mr Ke who resides in the Philippines. On 20 April 2006, Mr Ke as borrower and Mr Ke Qingkai as lender entered into a loan agreement, pursuant to which Mr Ke Qingkai provided a 10-year interest-free loan facility of up to HK$150 million to Mr Ke, with a 5% default interest rate applicable on any amounts due following the 10-year interest free period. On 1 July 2009, Mr Ke and Mr Ke Qingkai entered into a supplemental agreement, pursuant to which the parties acknowledged that Mr Ke Qingkai never intended to acquire an equity interest in the Group by providing such a loan facility and that Mr Ke could repay amounts due under the loan facility through future dividends to be distributed to Mr Ke by the Company after Listing. The balance due from us to Mr Ke was fully settled prior to 31 March 2010. In addition, as of 31 December 2009 we owed RMB95.6 million to our immediate holding company. This amount relates to shareholder loans made to us following payments made by Cathay to Smart Port pursuant to the Cathay Subscription Agreement as well as a loan extended to Smart Port by Cathay pursuant to the Smart Port Loan Agreement. This RMB95.6 million due to our immediate holding company was fully converted to equity prior to the completion of the Global Offering. As of 31 December 2007, 2008 and 2009, the amounts due to our other related parties were RMB123.3 million, RMB44.7 million and RMB8.6 million. Our Directors confirm that the RMB8.6 million due to our other related parties as of 31 December 2009 was fully settled prior to the Latest Practicable Date. Our Directors further confirm that all interest-bearing indebtedness owed to related parties was fully settled as of 31 December 2009. In the opinion of the Group's PRC lawyer, King & Wood, unless the related parties initiate legal proceedings against one another, the Group will not suffer adverse consequences under PRC law for having previously entered into interest-bearing loans with related parties.

Details of the related party transactions are set out in note 26 of the Accountants' Report in Appendix I to this prospectus.

### Distributable Reserves

As of 31 December 2009, our Group had an aggregate of RMB336.5 million in accumulated profits available for distribution to our Shareholders.

### No Material Adverse Change

Our Directors confirm that there has been no material adverse change in our financial or trading position since 31 December 2009 (being the date of our latest audited consolidated statements of financial results, as set out in the Accountants' Report in Appendix I to this prospectus).

### Disclosure Required under the Listing Rules

Our Directors confirm that, as of the Latest Practicable Date, there were no circumstances which would give rise to a disclosure requirement under Listing Rules 13.13 to 13.19, had they been required to comply with Listing Rules 13.13. to 13.19.

## FUTURE PLANS

We aim to maintain our position as a leading manufacturer of MF tissue paper products in the PRC. To achieve this, amongst other strategies, the Group plans to significantly expand its production capacity in the next few years.

As of the Latest Practicable Date, we have added four paper production lines in 2010 and plan to add another nine paper production lines by the end of 2012. These 13 new production lines include nine MF tissue paper production lines (of which two will be used for the manufacture of food wrapping paper), one copy paper production line, two paper towel production lines and one ivory board production line. We expect these 13 new paper production lines will increase our maximum annual production capacity by 209,250 tonnes, including 145,000 tonnes of MF tissue paper, 30,000 tonnes of copy paper, 20,000 tonnes of ivory boards and 14,250 tonnes of paper towels. Our new MF tissue paper production capacity is expected to be utilised to maintain our position as a leading manufacturer of wrapping tissue paper products in the PRC and to further expand our market share by strengthening our position in Eastern and Southern China as well as expand our footprint within Western China, where demand for packing materials has increased owing to the local economic development. Our new copy paper production capacity will be utilised to meet the market demand given that our existing copy paper production line has been fully utilised as of the Latest Practicable Date. Our new ivory board capacity is to meet the demand from existing customers who produce price tags. We expect demand for our paper towels to come from both our existing and new customers.

Our Directors' belief that our additional production capacity will be taken up by increased market demand is premised on industry growth forecasts issued by the China Paper Association. In 2008, the PRC produced approximately 450,000 tonnes of MF tissue paper and the growth of wrapping tissue paper consumption in the PRC is expected to continue at a rate of approximately 8% per annum, according to a report prepared by the China Paper Association. Assuming MF tissue paper production output in the PRC grows at the same rate, it would reach approximately 486,000 tonnes in 2009. Based on our production output of approximately 92,274 tonnes of MF tissue paper in 2009, we had achieved approximately 19.0% market share by production output, which is approximately 5% higher than that in 2008. Considering that a single-sided MF tissue paper production line is expected to commence operation in August 2012 and given its utilisation rate will be low during the trial period, our Directors expect our production output of MF tissue paper for the year ending 31 December 2012 to be approximately 207,000 tonnes. Assuming MF tissue paper production output in the PRC keeps growing at 8% per annum, it will reach approximately 612,000 tonnes in 2012. With this industry capacity as a backdrop and assuming our 2009 growth rate remains steady, we expect to achieve an approximately 33.8% market share for MF tissue paper by production output within the PRC in 2012.

We also intend to increase advertising and promotion activities of our products under the "Youlanfa" trademark. In particular, we plan to expand our sales team to enhance our marketing in Western and Central China, increase the number of our outdoor billboards and begin advertising campaigns on television.

For each of the three years ended 31 December 2010, 2011 and 2012, our planned investment on paper machines amounts to RMB201.5 million, RMB375.7 million and RMB341.2 million, respectively. The following table sets forth details of our 13 new paper production lines, including planned annual production capacity as estimated by our Directors.

| No. | Location | Products | Planned annual production capacity | Planned/Actual* commencement of operation |
|---|---|---|---|---|
| | | | (tonnes) | |
| 1 | Youlanfa Factory | paper towels | 6,000 | January 2010* |
| 2 | Youlanfa Factory | ivory boards | 20,000 | April 2010* |
| 3 | Youlanfa Factory | coloured single-sided MF tissue paper | 4,000 | October 2010 |
| 4 | Youlanfa Factory | coloured single-sided MF tissue paper | 4,000 | November 2010 |
| 5 | Huaxiang Factory | paper towels | 8,250 | June 2010 |
| 6 | Huaxiang Factory | double-sided MF tissue paper | 25,000 | October 2011 |
| 7 | Huaxiang Factory | double-sided MF tissue paper | 30,000 | December 2011 |
| 8 | Huaxiang Factory | single-sided MF tissue paper | 50,000 | August 2012 |
| 9 | Xiyuan Factory | single-sided MF tissue paper | 9,000 | January 2010* |
| 10 | Xiyuan Factory | single-sided MF tissue paper | 9,000 | January 2010* |
| 11 | Xiyuan Factory | food wrapping paper | 7,000 | September 2010 |
| 12 | Xiyuan Factory | food wrapping paper | 7,000 | September 2010 |
| 13 | Xiyuan Factory | copy paper | 30,000 | September 2010 |
| | | Total | 209,250 | |

Of the above 13 new paper production lines, our Youlanfa Factory has purchased and installed one production line for the production of paper towels which has a design capacity of 25 tonnes per day and has a maximum design speed of 220 metres per minute. It has the capacity to produce paper towels with a maximum paper width of 2.8 metres. Our Youlanfa Factory also purchased and installed one production line for the production of ivory boards which has a design capacity of 70 tonnes per day and a maximum design speed of 380 metres per minute. It has the capacity to produce ivory boards with a maximum paper width of 2.75 metres. Our Xiyuan Factory has purchased and installed two production lines for the production of single-sided MF tissue paper, each of which has a design capacity of 30 tonnes per day and a maximum design speed of 450 metres per minute. These single-sided MF tissue paper machines can produce tissue paper with a maximum paper width of 2.9 metres. Each of these paper towels, ivory, boards and single-sided MF tissue paper production lines commenced production before the Latest Practicable Date.

We also intend to upgrade our supporting facilities. We plan to construct a cogeneration plant at our Xiyuan Factory which will upon completion significantly reduce our Xiyuan Factory's reliance on local utilities for the supply of electricity. We also plan to add two de-inking facilities with an annual capacity of 160,000 tonnes of de-inked pulp by the end of 2012. We intend to utilise this added capacity to meet our increasing demand for de-inked pulp which, through further research and development, is expected to gradually replace reclaimed pulp and reduce the percentage of wood pulp we use in our production, thereby further lowering our production costs.

For each of the three years ended 31 December 2010, 2011 and 2012, our planned investment on other property, plant and equipment amounts to RMB352.2 million, RMB173.3 million and RMB124.5 million, respectively. The following table sets forth details of the major new plants and supporting facilities.

| No. | Location | New plants and supporting facilities | Expected capacity | Site area | Expected completion time |
|---|---|---|---|---|---|
| | | | (tonnes/year except otherwise specified) | (sq.m.) | |
| 1 | Youlanfa Factory | blue top linerboard production line | 8,400 | — | July 2010 |
| 2 | Huaxiang Factory | de-inking facility | 60,000[1] | — | July 2010 |
| 3 | Huaxiang Factory | water treatment and recycling system | — | — | July 2010 |
| 4 | Huaxiang Factory | warehouses | — | 33,894 | November 2010 |
| 5 | Huaxiang Factory | dormitories | — | — | July 2010 |
| 6 | Xiyuan Factory | production plants | — | — | September 2010 |
| 7 | Xiyuan Factory | cogeneration plant | 35t/h | — | September 2010 |
| 8 | Xiyuan Factory | water treatment and recycling system | — | — | September 2010 |
| 9 | Xiyuan Factory | warehouses | — | 23,000 | October 2010 |
| 10 | Huaxiang Factory | production plants | — | — | October 2011 |
| 11 | Huaxiang Factory | coal yard | — | 5,000 | October 2011 |
| 12 | Huaxiang Factory | boiler plant | 20t/h | — | October 2011 |
| 13 | Huaxiang Factory | warehouses | — | 30,000 | December 2011 |
| 14 | Xiyuan Factory | de-inking facility | 60,000 | — | February 2011 |
| 15 | Xiyuan Factory | dormitory | — | — | July 2011 |
| 16 | Huaxiang Factory | production plant | — | — | August 2012 |
| 17 | Huaxiang Factory | boiler plant | 20t/h | — | August 2012 |
| 18 | Huaxiang Factory | warehouses | — | 4,000 | June 2012 |
| 19 | Xiyuan Factory | warehouses | — | 5,000 | May 2012 |

*Note 1:* To be upgraded to 100,000 tonnes in July 2011.

Our planned investment on paper machines, plants and supporting facilities is expected to be financed primarily by the proceeds from the Global Offering, operating cashflow and bank loans.

Apart from paper production lines that are not comparable with our existing production facilities as they will produce new products such as paper towels and ivory boards, most of the planned new production lines and supporting facilities are expected to have higher capacities than our existing production facilities. We plan to procure the double-sided MF tissue paper and the single-sided MF tissue paper production lines for our Huaxiang Factory from overseas manufacturers, and the specifications for such machines are expected to include higher speeds and wider paper widths as compared to paper machines produced domestically.

For a detailed description of our future plans, please refer to "Business — Business Strategies" in this prospectus.

## USE OF PROCEEDS

We estimate that the net proceeds of the Global Offering (after deducting underwriting commissions and estimated expenses payable by us in connection with the Global Offering and assuming the Over-allotment Option is not exercised), assuming an Offer Price of HK$2.98 per share, being the mid-point of the indicative Offer Price range, will be approximately HK$677.9 million. We intend to apply such net proceeds in the following manner:

- approximately HK$305.1 million or approximately 45% of the aggregate net proceeds is expected to be used for the purchase of machinery and equipment relating to new production facilities, of which approximately HK$164.7 million or 54% is expected to be spent on the new production lines at Huaxiang Factory, approximately HK$131.2 million or 43% is expected to be spent on the new production lines at Xiyuan Factory, and approximately HK$9.2 million or 3% is expected to be spent on the new production lines at Youlanfa Factory;

- approximately HK$271.2 million or approximately 40% of the aggregate net proceeds is expected to be used for the construction of new plant and supporting facilities to support production of new products and increases to production capacity, of which approximately HK$130.2 million or 48% is expected to be spent on the new plant and supporting facilities of Huaxiang Factory, approximately HK$135.6 million or 50% is expected to be spent on the new plant and supporting facilities of Xiyuan Factory, and approximately HK$5.4 million or 2% is expected to be spent on the new plant and supporting facilities of Youlanfa Factory;

- approximately HK$67.7 million or approximately 10% of the aggregate net proceeds is expected to be used for working capital and other general corporate purposes; and

- approximately HK$33.9 million or approximately 5% of the aggregate net proceeds is expected to be used for marketing expenses for growing our existing business in the PRC.

If the Offer Price is set at the high-end of the indicative Offer Price range, being HK$3.38 per Share, the net proceeds of the Global Offering (assuming the Over-allotment Option is not exercised), will increase by approximately HK$95.7 million. We intend to apply the additional net proceeds for the above purposes on a pro-rata basis.

If the Offer Price is set at the low-end of the indicative Offer Price range, being HK$2.58 per Share, the net proceeds of the Global Offering (assuming the Over-allotment Option is not exercised), will decrease by approximately HK$95.7 million. In such case, we intend to reduce the allocation of such net proceeds for the above purposes on a pro-rata basis.

If the Over-allotment Option is exercised in full, the net proceeds from the Global Offering will be approximately HK$784.9 million, assuming the Offer Price is set at the mid-point of the indicative Offer Price range. If the Offer Price is set at the high-end of the indicative Offer Price range, the net proceeds from the Global Offering (including the proceeds from the exercise of the Over-allotment Option) will be approximately HK$895.0 million. If the Offer Price is set at the low-end of the indicative Offer Price range, the net proceeds from the Global Offering (including the proceeds from the exercise of the Over-allotment Option) will be approximately HK$674.8 million. We intend to apply any additional net proceeds to the above purposes on a pro-rata basis.

To the extent that the net proceeds are not immediately required for or applied to the above purposes, we may hold such funds in short-term deposits with licensed banks and authorised financial institutions in Hong Kong for so long as it is in our best interests.

As advised by our PRC legal advisers, subject to the relevant PRC governmental approval, registrations and/or filings, the net proceeds from the Global Offering can be applied in the PRC according to the above intended use of the net proceeds under the relevant existing laws and regulations in the PRC by: (i) increasing the registered capital of the Company's PRC subsidiary; (ii) establishing a new PRC subsidiary; (iii) acquiring equity interests in the other companies in the PRC; and/or (iv) providing shareholder loans to the Company's subsidiary in the PRC in an amount not exceeding the difference between the investment amount and the registered capital of such subsidiary. As advised by our PRC legal advisers, there are no material legal obstacles to obtaining the relevant PRC governmental approvals to apply the net proceeds from the Global Offering in the PRC, if all requirements of the relevant PRC government authorities are satisfied.

We will make an appropriate announcement and comply with the requirements of the Listing Rules if there is any change to the above proposed use of proceeds.

## SOLE GLOBAL COORDINATOR

The Hongkong and Shanghai Banking Corporation Limited

## HONG KONG UNDERWRITERS

### Sole Lead Manager

The Hongkong and Shanghai Banking Corporation Limited

### Co-Manager

GF Securities (Hong Kong) Brokerage Limited

## UNDERWRITING ARRANGEMENTS AND EXPENSES

### Hong Kong Public Offering

*Hong Kong Underwriting Agreement*

Pursuant to the Hong Kong Public Offering, our Company is offering the Hong Kong Offer Shares for subscription by the public in Hong Kong on and subject to the terms and conditions of this prospectus and the Application Forms. Subject to the Listing Committee granting listing of, and permission to deal in, the Shares to be offered as mentioned herein (including the additional Shares to be issued pursuant to the exercise of the Over-allotment Option and under the Share Option Scheme) and to certain other conditions set out in the Hong Kong Underwriting Agreement and the International Underwriting Agreement having been duly executed and delivered and having become unconditional in accordance with its terms, the Hong Kong Underwriters have agreed severally to subscribe or procure subscribers for, their respective applicable proportions of the Hong Kong Offer Shares which are being offered but are not taken up under the Hong Kong Public Offering on the terms and subject to the conditions of this prospectus, the Application Forms and the Hong Kong Underwriting Agreement.

*Grounds for termination*

The respective obligations of the Hong Kong Underwriters to subscribe for, or procure subscribers for, the Hong Kong Offer Shares are subject to termination. The Sole Global Coordinator (for itself and on behalf of the Hong Kong Underwriters) shall be entitled by giving notice in writing to our Company to terminate the Hong Kong Underwriting Agreement with immediate effect if at any time prior to 8:00 a.m. on the Listing Date:

(A) there shall develop, occur, exist or come into effect:

(a) any event, or series of events, in the nature of force majeure (including, without limitation, any acts of government, declaration of a national or international emergency or war, calamity, crisis, epidemic, pandemic, outbreak of disease, economic sanctions, strikes, lock-outs, fire, explosion, flooding, earthquake, civil commotion, riots, public disorder, acts of war, outbreak or escalation of hostilities (whether or not war is declared), acts of God or acts of terrorism); or

(b) any change or development involving a prospective change, or any event or series of events likely to result in any change or development involving a prospective change, in local, national, regional or international financial, economic, political, military, industrial, fiscal, regulatory, currency, credit or market conditions (including, without limitation, conditions in the stock and bond markets, money and foreign exchange markets, the interbank markets and credit markets), in or affecting Hong Kong, the PRC, the United States, the United Kingdom, the European Union (or any member thereof), Japan or any other jurisdiction relevant to any member of our Group (each a "Relevant Jurisdiction"); or

(c) any moratorium, suspension or restriction in or on trading in securities generally on the Stock Exchange, the Shanghai Stock Exchange, the Shenzhen Stock Exchange, the New York Stock Exchange, the NASDAQ Global Market, the London Stock Exchange or the Tokyo Stock Exchange; or

(d) any general moratorium on commercial banking activities in Hong Kong (imposed by the Financial Secretary or the Hong Kong Monetary Authority or other competent Authority), New York (imposed at Federal or New York State level or other competent Authority), London, the PRC, the European Union (or any member thereof), Japan or any other Relevant Jurisdiction, or any disruption in commercial banking or foreign exchange trading or securities settlement or clearance services, procedures or matters in any Relevant Jurisdiction; or

(e) any new law or regulation or any change or development involving a prospective change in existing laws or regulations or any change or development involving a prospective change in the interpretation or application thereof by any court or other competent Authority (as defined in the Hong Kong Underwriting Agreement) in or affecting any Relevant Jurisdiction; or

(f) the imposition of economic sanctions, in whatever form, directly or indirectly, by, or for, any Relevant Jurisdiction; or

(g) a change or development involving a prospective change in Taxation (as defined in the Hong Kong Underwriting Agreement) or exchange control, currency exchange rates or foreign investment regulations (including without limitation a change in the system under which the value of the Hong Kong dollar is linked to that of the United States dollar, or a material devaluation of the Hong Kong dollar or the Renminbi or the Euro against any foreign currencies), or the implementation of any exchange control, in any Relevant Jurisdiction; or

(h) any breach of any of the obligations imposed upon any party to Hong Kong Underwriting Agreement or the International Underwriting Agreement (other than upon any of the Hong Kong Underwriters or the International Underwriters); or

(i) any event, act or omission which gives or is likely to give rise to any liability of any of the indemnifying parties under the Hong Kong Underwriting Agreement; or

(j) any adverse change or development involving a prospective adverse change in the assets, liabilities, business, general affairs, management, prospects, shareholders' equity, profits, losses, results of operations, position or condition, financial or otherwise, or performance of any member of our Group; or

(k) any breach of, or any event rendering untrue or incorrect in any respect, any of the warranties contained in the Hong Kong Underwriting Agreement; or

(l) any litigation or claim of any third party being threatened or instigated against any member of our Group,

which, individually or in the aggregate, in the sole opinion of the Sole Global Coordinator (1) has or will or may have a material adverse effect on the assets, liabilities, business, general affairs, management, prospects, shareholders' equity, profits, losses, results of operations, position or condition, financial or otherwise, or performance of our Group as a whole; or (2) has or will have or may have a material adverse effect on the success of the Global Offering or the level of applications under the Hong Kong Public Offering or the level of interest under the International Offering; or (3) makes or will make or may make it inadvisable or inexpedient or impracticable for the Global Offering to proceed or to market the Global Offering; or (4) has or will or may have the effect of making any part of Hong Kong Underwriting Agreement (including underwriting) incapable of performance in accordance with its terms or preventing the processing of applications and/or payments pursuant to the Global Offering or pursuant to the underwriting thereof; or

(B) there has come to the notice of the Sole Global Coordinator:

(a) an Authority (as defined in the Hong Kong Underwriting Agreement) or organisation in any relevant jurisdiction commencing any investigation or other action, or announcing an intention to investigate or take other action, against any Director; or

(b) a contravention by any member of our Group of the applicable laws; or

(c) non-compliance of this prospectus (or any other documents used in connection with the contemplated subscription and sale of the Shares) or any aspect of the Global Offering with the Listing Rules or any other applicable law or regulation; or

(d) an order or petition for the winding up of any member of our Group or any composition or arrangement made by any member of our Group with its creditors or a scheme of arrangement entered into by any member of our Group or any resolution for the winding-up of any member of our Group or the appointment of a provisional liquidator, receiver or manager over all or part of the material assets or undertaking of any member of our Group or anything analogous thereto occurring in respect of any member of our Group; or

(e) that any statement contained in any of this prospectus, the Application Forms and/or in any notices, announcements or other documents issued by, or authorised to be issued by, our Company in connection with the Global Offering (including any supplement or amendment thereto) was, when it was issued, or has become, in the sole opinion of the Global Coordinator, untrue, incorrect or misleading in any material respect, or that any forecast, expression of opinion, intention or expectation contained in any of this prospectus, the Application Forms and/or any notices, announcements or other documents issued by, or authorised to be issued by, our Company in connection with the Hong Kong Public Offering (including any supplement or amendment thereto) is not fair and honest and based on reasonable assumptions; or

(f) that any matter has arisen or has been discovered which would, had it arisen or been discovered immediately before the date of this prospectus, constitute an omission from any of this prospectus, the Application Forms and/or in any notices, announcements or other documents issued by, or authorised to be issued by, our Company in connection with the Hong Kong Public Offering (including any supplement or amendment thereto); or

(g) our Company withdraws this prospectus (and/or any other documents issued or used in connection with the Global Offering) or the Global Offering.

**International Offering**

In connection with the International Offering, it is expected that our Company, our Controlling Shareholders, Mr Ke Jixiong and Everproud will enter into the International Underwriting Agreement with the International Underwriters on or about 20 May 2010, shortly after determination of the Offer Price.

Under the International Underwriting Agreement, subject to the conditions set forth therein, the International Underwriters are expected to severally agree to subscribe or procure purchasers for, or failing which to purchase, the International Offer Shares initially being offered pursuant to the International Offering. It is expected that the International Underwriting Agreement may be terminated on similar grounds as the Hong Kong Underwriting Agreement. Potential investors shall be reminded that in the event that the International Underwriting Agreement is not entered into, the Global Offering will not proceed.

Our Company is expected to grant to the Sole Global Coordinator, on behalf of the International Underwriters, the Over-allotment Option exercisable at any time from the date of the International Underwriting Agreement until the 30th day after 19 May 2010, being the last date for lodging of applications under the Hong Kong Public Offering, to require our Company to allot and issue up to an aggregate of 37,500,000 additional Shares, representing 15% of the initial Offer Shares, at the same price per Offer Share under the International Offering, solely to cover over-allocations, if any, in the International Offering.

**Commissions and expenses**

The Underwriters will receive an underwriting commission of 3.25% of the aggregate Offer Price payable for the Offer Shares (including any Shares to be issued pursuant to the Over-allotment Option), excluding the incentive fees, out of which they will pay any sub-underwriting commission.

The aggregate commissions and the maximum amount of incentive fees in connection with the Global Offering, together with listing fees, legal and other professional fees and printing and other expenses relating to the Global Offering and the SFC transaction levy and Stock Exchange trading fee, which are estimated to be approximately HK$67.1 million in aggregate (based on the Offer Price of HK$2.98, being the mid-point of the indicative Offer Price range between HK$2.58 and HK$3.38, and the assumption that the Over-allotment Option is not exercised), will be payable by our Company.

**Undertakings by the Controlling Shareholders to the Stock Exchange pursuant to the Listing Rules**

Pursuant to Rule 10.07(1) of the Listing Rules, the Controlling Shareholders (namely, Mr Ke and Smart Port) have undertaken to the Stock Exchange and to our Company that except pursuant to the Global Offering or the Capitalisation Issue or the Over-allotment Option or the Stock Borrowing Agreement,

(a) in the period commencing on the date by reference to which disclosure of their shareholdings in our Company is made in this prospectus and ending on the date which is 6 months from the Listing Date, they shall not dispose of, nor enter into any agreement to dispose of or otherwise create any options, rights, interests or encumbrances in respect of, any of the Shares in respect of which each of them is shown in this prospectus to be the beneficial owner; and

(b) in the period of 6 months commencing on the date on which the period referred to in paragraph (a) above expires, they shall not dispose of, nor enter into any agreement to dispose of or otherwise create any options, rights, interests or encumbrances in respect of, any of the Shares in respect of which each of them is shown in this prospectus to be the beneficial owner if, immediately following such disposal or upon the exercise or enforcement of such options, rights, interests or encumbrances, they would cease to be a controlling shareholder (as defined in the Listing Rules) of our Company.

Pursuant to Note 3 to Rule 10.07(2) of the Listing Rules, the Controlling Shareholders (namely, Mr Ke and Smart Port) have undertaken to the Stock Exchange and to our Company that within the period commencing on the date by reference to which disclosure of their shareholdings in our Company is made in this prospectus and ending on the date which is 12 months from the Listing Date, they shall:

(a) when any of them pledges or charges any securities beneficially owned by any of them in favour of an authorised institution (as defined in the Banking Ordinance) for a bona fide commercial loan pursuant to Note (2) to Rule 10.07(2) of the Listing Rules, immediately inform our Company in writing of such pledge or charge together with the number of Shares so pledged or charged; and

(b) when any of them receive indications, whether verbal or written, from the pledgee or chargee that any of the pledged or charged securities will be disposed of, immediately inform our Company in writing of such indications.

**Other Undertakings**

Our Company has undertaken to each of the Sole Global Coordinator, the Hong Kong Underwriters and the Sole Sponsor that except for the offer and sale of the Offer Shares pursuant to the Global Offering (including pursuant to the Over-allotment Option) or any options which may be granted under the Share Option Scheme of our Company, during the period commencing on the date of the Hong Kong Underwriting Agreement and ending on, and including, the date that is six months after the Listing Date (the "First Six-month Period"), our Company shall not, and shall procure each other member of our Group shall not, without the prior written consent of the Sole Sponsor and the Sole Global Coordinator (on behalf of the Hong Kong Underwriters) and unless in compliance with the requirements of the Listing Rules:

(a) allot, issue, sell, accept subscription for, offer to allot, issue or sell, contract or agree to allot, issue or sell, mortgage, charge, pledge, hypothecate, lend, grant or sell any option, warrant, contract or right to subscribe for or purchase, grant or purchase any option, warrant, contract or right to allot, issue or sell, or otherwise transfer or dispose of or create an encumbrance over, or agree to transfer or dispose of or create an encumbrance over, either directly or indirectly, conditionally or unconditionally, any Shares or any other securities of our Company or any shares or other securities of such other member of our Group, as applicable, or any interest in any of the foregoing (including, without limitation, any securities convertible into or exchangeable or exercisable for or that represent the right to receive, or any warrants or other rights to purchase, any Shares or any shares of such other member of our Group, as applicable), save and except for such actions referred to above as taken by any member of our Group other than our Company which will not have any dilutive effect on the effective interest of our Company in any other member of our Group; or

(b) enter into any swap or other arrangement that transfers to another, in whole or in part, any of the economic consequences of ownership of Shares or any other securities of our Company or any shares or other securities of such other member of our Group, as applicable, or any interest in any of the foregoing (including, without limitation, any securities convertible into or exchangeable or exercisable for or that represent the right to receive, or any warrants or other rights to purchase, any Shares or any shares of such other member of our Group, as applicable), save and except for such actions referred to above as taken by any member of our Group other than our Company which will not have any dilutive effect on the effective interest of our Company in any other member of our Group; or

(c) enter into any transaction with the same economic effect as any transaction specified in paragraphs (a) or (b) above; or

(d) offer to or agree to or announce any intention to effect any transaction specified in paragraphs (a), (b) or (c) above,

in each case, whether any of the transactions specified in paragraphs (a), (b) or (c) above is to be settled by delivery of Shares or such other securities of our Company or shares or other securities of such other member of our Group, as applicable, or in cash or otherwise (whether or not the issue of Shares or such other securities will be completed within the aforesaid period). In the event that, during the period of six months commencing on the date on which the First Six-month Period expires (the “Second Six-month Period”), our Company enters into any of the transactions specified in paragraphs (a), (b) or (c) above or offers to or agrees to or announces any intention to effect any such transaction, our Company shall take all reasonable steps to ensure that it will not create a disorderly or false market in the securities of our Company. Each of Mr Ke, Smart Port and Mr Ke Jixiong has undertaken to each of the Sole Global Coordinator, the Hong Kong Underwriters and the Sole Sponsor to procure our Company to comply with the above undertakings.

Each of Mr Ke, Smart Port, Mr Ke Jixiong, Everproud, Ms Cai Lishuang, Denron, Ms Ke Jinzhen, Giantwish, Ms Ke Jinzhi, Grand Earning and Cathay Special Paper (and its shareholder, namely Cathay Capital Holdings II, L.P.) has undertaken to each of our Company, the Sole Global Coordinator, the Hong Kong Underwriters and the Sole Sponsor that, without the prior written consent of the Sole Sponsor and the Sole Global Coordinator (on behalf of the Hong Kong Underwriters) and unless in compliance with the requirements of the Listing Rules that, he or she or it will not, at any time during the First Six-month Period, (i) sell, offer to sell, contract or agree to sell, mortgage, charge, pledge, hypothecate, lend, grant or sell any option, warrant, contract or right to purchase, grant or purchase any option, warrant, contract or right to sell, or otherwise transfer or dispose of or create an encumbrance over, or agree to transfer or dispose of or create an encumbrance over, either directly or indirectly, conditionally or unconditionally, any Shares or any other securities of our Company or any interest therein or voting right or any other right attaching thereto (including, without limitation, any securities convertible into or exchangeable or exercisable for or that represent the right to receive, or any warrants or other rights to purchase, any Shares, as applicable), or (ii) enter into any swap or other arrangement that transfers to another, in whole or in part, any of the economic consequences of ownership of Shares or any other securities of our Company or any interest therein (including, without limitation, any securities convertible into or exchangeable or exercisable for or that represent the right to receive, or any warrants or other rights to purchase, any Shares), or (iii) enter into any transaction with the same economic effect as any transaction specified in (i) or (ii) above, or (iv) offer to or agree to or announce any intention to effect any transaction specified in (i), (ii) or (iii) above, in each case, whether any of the transactions specified in (i), (ii) or (iii) above is to be settled by delivery of Shares or such other securities of our Company or shares or other securities of such other member of our Group, as applicable, or in cash or otherwise (whether or not the issue of Shares or such other securities will be completed within the aforesaid period).

Each of Mr Ke and Smart Port has further undertaken to each of our Company, the Sole Global Coordinator, the Hong Kong Underwriters and the Sole Sponsor, without the prior written consent of the Sole Sponsor and the Sole Global Coordinator (on behalf of the Hong Kong Underwriters) and unless in compliance with the requirements of the Listing Rules, that:

(a) he or it will not, during the Second Six-month Period, (i) sell, offer to sell, contract or agree to sell, mortgage, charge, pledge, hypothecate, lend, grant or sell any option, warrant, contract or right to purchase, grant or purchase any option, warrant, contract or right to sell, or otherwise transfer or dispose of or create an encumbrance over, or agree to transfer or dispose of or create an encumbrance over, either directly or indirectly, conditionally or unconditionally, any Shares or any other securities of our Company or any interest therein or voting right or any other right attaching thereto (including, without limitation, any securities convertible into or exchangeable or exercisable for or that represent the right to receive, or any warrants or other rights to purchase, any Shares, as applicable), or (ii) enter into any swap or other arrangement that transfers to another, in whole or in part, any of the economic consequences of ownership of Shares or any other securities of our Company or any interest therein (including, without limitation, any securities convertible into or exchangeable or exercisable for or that represent the right to receive, or any warrants or other rights to purchase, any Shares), or (iii) enter into any transaction with the same economic effect as any transaction specified in (i) or (ii) above, or offer to or agree to or announce any intention to effect any such transaction if, immediately following any sale, transfer or disposal or upon the exercise or enforcement of any option, right, interest or encumbrance pursuant to such transaction, he or it will cease to be a "controlling shareholder" (as the term is defined in the Listing Rules) of our Company; and

(b) until the expiry of the Second Six-month Period, in the event that it enters into any of the transactions specified in paragraph (a)(i), (ii) or (iii) above or offer to or agrees to or announce any intention to effect any such transaction, he or it will take all reasonable steps to ensure that he or it will not create a disorderly or false market in the securities of our Company.

Each of Mr Ke and Smart Port has further undertaken to our Company, the Sole Global Coordinator, the Sole Sponsor and the Hong Kong Underwriters that he or it will, at any time within the period commencing on the date of the Hong Kong Underwriting Agreement and ending on the date which is 12 months after the Listing Date:

(a) upon any pledge or charge in favour of an authorized institution (as defined in the Banking Ordinance (Chapter 155 of the Laws of Hong Kong)) of any Shares or securities or interests in the Shares or other securities of our Company beneficially owned by he or it for a bona fide commercial loan, immediately inform our Company and the Sole Global Coordinator in writing of such pledge or charge together with the number of Shares or securities so pledged or charged; and

(b) upon any indication received by it or him, either verbal or written, from any pledgee or chargee that any of the pledged or charged Shares or securities or interests in the Shares or securities of our Company will be disposed of, immediately inform our Company and the Sole Global Coordinator in writing of such indications.

## SOLE SPONSOR'S AND UNDERWRITERS' INTEREST IN OUR COMPANY

The Sole Lead Manager and the other Underwriters will receive an underwriting commission. Particulars of these underwriting commission and expenses are set forth under the paragraph headed "Commission and expenses" above.

Save as disclosed above, including the Underwriters' obligations under the Underwriting Agreements, none of the Sole Sponsor, the Sole Lead Manager and the other Underwriters is interested legally or beneficially in shares of any members of our Group or has any right or option (whether legally enforceable or not) to subscribe for or purchase or to nominate persons to subscribe for or purchase securities in any of our members nor any interest in the Global Offering.

## MINIMUM PUBLIC FLOAT

Our Directors and the Sole Global Coordinator will ensure that there will be a minimum 25% of the total issued Shares held in public hands in accordance with Rule 8.08 of the Listing Rules after completion of the Global Offering.

## OFFER PRICE AND PRICE PAYABLE ON APPLICATION

The Offer Price will not be more than HK$3.38 and is not expected to be less than HK$2.58 per Offer Share. Based on the maximum Offer Price of HK$3.38 per Offer Share, plus 1% brokerage fee, 0.004% SFC transaction levy, and 0.005% Stock Exchange trading fee, one board lot of 1,000 Shares will amount to a total of HK$3,414.11.

The Offer Price is expected to be determined by our Company and the Sole Global Coordinator (on behalf of the Underwriters) on the Price Determination Date. The Price Determination Date is expected to be on or before Thursday, 20 May 2010 and in any event, not later than Wednesday, 26 May 2010.

If, based on the level of interests expressed by prospective professional, institutional and/or other investors during the book-building process, the Sole Global Coordinator (on behalf of the Underwriters, and with the consent of our Company) thinks it appropriate (for instance, if the level of interests is below the indicative Offer Price range), the indicative Offer Price range may be reduced below that stated in this prospectus at any time prior to the morning of the last day for lodging applications. In such case, our Company will, as soon as practicable following the decision to make such reduction, and in any event not later than the morning of the last day for lodging applications under the Hong Kong Public Offering cause there to be published in the South China Morning Post (in English) and the Hong Kong Economic Times (in Chinese) and on the website of the Stock Exchange at www.hkexnews.hk and our Company's website at www.youyuan.com.hk notice of the reduction of the indicative Offer Price range. Such notice will also include any financial information which may change as a result of any such reduction. **If applications for Hong Kong Offer Shares have been submitted prior to the day which is the last day for lodging applications under the Hong Kong Public Offering, then even if the indicative Offer Price range is so reduced, such applications cannot be subsequently withdrawn.**

**If, for any reason, the Offer Price is not agreed between our Company and the Sole Global Coordinator (on behalf of the Underwriters) on or before Wednesday, 26 May 2010, the Global Offering will not become unconditional and will lapse.**

## CONDITIONS

Acceptance of all applications for the Global Offering will be conditional upon:

(i) the Listing Committee of the Stock Exchange granting a listing of, and permission to deal in the Shares (including any Shares which may fall to be issued upon the exercise of the Over-allotment Option or any Shares which may fall to be issued upon the exercise of the option that may be granted under the Share Option Scheme), and such listing and permission not subsequently having been revoked prior to the commencement of dealings in the Shares on the Stock Exchange;

(ii) the Offer Price having been duly determined and the execution and delivery of the Price Determination Agreement on or about the Price Determination Date; and

(iii) the obligations of the Underwriters under the Underwriting Agreement becoming unconditional (including the waiver of any condition(s) by the Sole Global Coordinator on behalf of the Underwriters) and not being terminated in accordance with the terms of either agreement or otherwise,

in each case on or before the dates and times specified in the Underwriting Agreement. If these conditions are not fulfilled, all application monies will be returned, without interest, on the terms set out in "How to Apply for Hong Kong Offer Shares" in this prospectus. In the meantime, such monies will be held in separate bank accounts with the receiving banker or other licensed bank(s) in Hong Kong.

## OFFER MECHANISM — BASIS OF ALLOCATION OF SHARES

### The Global Offering

The Global Offering consists of the International Offering and the Hong Kong Public Offering. The 250,000,000 Shares initially offered will comprise 225,000,000 Shares being offered under the International Offering (being 225,000,000 new Shares offered for subscription by our Company) and 25,000,000 Shares being offered under the Hong Kong Public Offering. The 250,000,000 Shares being offered under the Global Offering will represent approximately 25% of our Company's share capital immediately after completion of the Global Offering and the Capitalisation Issue but without taking into account any Shares which may fall to be issued upon the exercise of the Over-allotment Option or any Shares which may fall to be issued upon the exercise of the option that may be granted under the Share Option Scheme. The Over-allotment Option is expected to be made available to the International Offering Underwriters and will not be part of the Hong Kong Public Offering.

Subject to possible reallocation on the basis set forth below, 25,000,000 Shares, representing 10% of the total number of Shares initially being offered under the Global Offering, will be offered to the public in Hong Kong under the Hong Kong Public Offering. The Hong Kong Public Offering is open to all members of the public in Hong Kong as well as to institutional and professional investors.

Out of the total 250,000,000 Shares offered pursuant to the Global Offering, 225,000,000 Shares, representing 90% of the total number of Shares initially being offered under the Global Offering, will be placed with professional, institutional investors and/or other investors in Hong Kong, the United States, Europe and elsewhere under the International Offering. The International Offer Shares will be offered in Hong Kong, Europe and other jurisdictions outside the United States in offshore transactions, as defined in, and in reliance on, Regulation S of the US Securities Act, and in the United States to QIBs, as defined in and in reliance on, Rule 144A of the US Securities Act.

In connection with the Global Offering, we have granted to the Sole Global Coordinator the Over-allotment Option which is exercisable by the Sole Global Coordinator (on behalf of the International Offering Underwriters) no later than 18 June 2010, being the 30th day after the last day for lodging applications under the Hong Kong Public Offering. Pursuant to the Over-allotment Option, we may be required to allot and issue up to an aggregate of 37,500,000 additional Shares (representing 15% of the number of Shares initially being offered under the Global Offering) to cover over-allocations in the International Offering. The Sole Global Coordinator may also cover over-allocations in the International Offering by purchasing Shares in the secondary market or by a combination of purchases in the secondary market and the exercise, in part or in full, of the Over-allotment Option. The number of Shares that may be over-allocated will not exceed the maximum number of Shares that may be issued under the Over-allotment Option. Any such secondary market purchases will be made in compliance with all applicable laws, rules and regulations. If the Over-allotment Option is exercised in full, on completion of the Global Offering and the Capitalisation Issue but without taking into account any Shares which may fall to be issued upon the exercise of the option that may be granted under the Share Option Scheme, the Offer Shares will represent approximately 27.7% of our Company's enlarged issued share capital.

If the Sole Global Coordinator decides to exercise the Over-allotment Option, it will be exercised solely to cover over-allocations in the International Offering. The International Offer Shares (including any over-allocations) will be allocated prior to the commencement of trading of the Shares on the Stock Exchange.

**The Hong Kong Public Offering**

Our Company is initially offering 25,000,000 Hong Kong Offer Shares, representing 10% of the total number of Shares initially being offered in the Global Offering, for subscription by way of a public offer in Hong Kong. The Hong Kong Offer Shares are being offered at the Offer Price. Pursuant to the Hong Kong Underwriting Agreement, the Hong Kong Public Offering is fully underwritten by the Hong Kong Underwriters, subject to the agreement on the Offer Price between the Sole Global Coordinator (on behalf of the Underwriters) and us on the Price Determination Date.

The total number of Shares available for subscription under the Hong Kong Public Offering (after taking into account any reallocation referred to below) is to be divided equally into two pools for allocation purposes: pool A and pool B. The Shares in pool A will be allocated on an equitable basis to applicants who have applied for Shares with an aggregate subscription amount of HK$5 million (excluding the brokerage fee, the SFC transaction levy and the Stock Exchange trading fee payable) or less. The Shares in pool B will be allocated on an equitable basis to applicants who have applied for Shares with an aggregate subscription amount of more than HK$5 million (excluding the brokerage fee, the SFC transaction levy, and the Stock Exchange trading fee payable) and up to the value of pool B. Investors should be aware that applications in pool A and applications in pool B may receive different allocation ratios. If Shares in one (but not both) of the pools are undersubscribed, the surplus Shares will be transferred to the other pool to satisfy demand in the pool and be allocated accordingly.

Applicants can only receive an allocation of Shares from either pool A or pool B but not from both pools. Multiple or suspected multiple applications within either pool or between pools and any application for more than the total number of Shares originally allocated to each pool (i.e., 12,500,000 Shares) are liable to be rejected. Each applicant under the Hong Kong Public Offering will also be required to give an undertaking and confirmation in the Application Form submitted by him that he and any person(s) for whose benefit he is making the application have not received any Shares under the International Offering and such applicant's application is liable to be rejected if the said undertaking and/or confirmation is breached and/or untrue (as the case may be).

The allocation of the Shares between the International Offering and the Hong Kong Public Offering is subject to adjustment.

If the number of Shares validly applied for under the Hong Kong Public Offering represents 15 times or more but less than 50 times the number of Shares initially available for subscription under the Hong Kong Public Offering, then Shares will be reallocated to the Hong Kong Public Offering from the International Offering, so that the total number of Shares available for subscription under the Hong Kong Public Offering will increase to 75,000,000 Shares, representing 30% of the Shares initially available for subscription under the Global Offering.

If the number of Shares validly applied for under the Hong Kong Public Offering represents 50 times or more but less than 100 times the number of Shares initially available for subscription under the Hong Kong Public Offering, then the number of Shares to be reallocated to the Hong Kong Public Offering from the International Offering will be increased so that the total number of Shares available for subscription under the Hong Kong Public Offering will be 100,000,000 Shares, representing 40% of the Shares initially available for subscription under the Global Offering.

If the number of Shares validly applied for under the Hong Kong Public Offering represents 100 times or more the number of Shares initially available for subscription under the Hong Kong Public Offering, then the number of Shares to be reallocated to the Hong Kong Public Offering from the International Offering will be increased, so that the total number of Shares available for subscription under the Hong Kong Public Offering will increase to 125,000,000 Shares, representing 50% of the Shares initially available for subscription under the Global Offering. In each such case, the additional Shares reallocated to the Hong Kong Public Offering will be allocated equally between pool A and pool B and the number of Shares allocated to the International Offering will be correspondingly reduced.

If the Hong Kong Public Offering is not fully subscribed, the Sole Global Coordinator, in its discretion, may reallocate all or any unsubscribed Shares originally included in the Hong Kong Public Offering to the International Offering, in such proportion as it considers appropriate provided that there is sufficient demand under the International Offering to take up such re-allocated Offer Shares. If the International Offering is not fully subscribed, the Sole Global Coordinator, in its discretion, may reallocate all or any unsubscribed Shares originally included in the International Offering to the Hong Kong Public Offering, in such proportion as it considers appropriate provided that there is sufficient demand under the Hong Kong Public Offering to take up such re-allocated Offer Shares.

The Hongkong and Shanghai Banking Corporation Limited is the Sole Global Coordinator and the Sole Bookrunner of the Hong Kong Public Offering which is underwritten at the Offer Price by the Hong Kong Underwriters, on and subject to the terms and conditions of the Hong Kong Underwriting Agreement.

Allocation of Hong Kong Offer Shares to investors under the Hong Kong Public Offering will be based solely on the level of valid applications received under the Hong Kong Public Offering. The basis of allocation may vary, depending on the number of Hong Kong Offer Shares validly applied for by applicants although this could, where appropriate, consist of balloting. Balloting would mean that some applicants may receive a higher allocation than others who have applied for the same number of Hong Kong Offer Shares and those applicants who are not successful in the ballot may not receive any Hong Kong Offer Shares.

**The International Offering**

Our Company is initially offering 225,000,000 Shares as International Offer Shares, representing 90% of the total number of Shares initially being offered in the Global Offering (subject to the Over-allotment Option), for subscription or purchase by way of the International Offering subject to the reallocation of Offer Shares between the International Offering and the Hong Kong Public Offering. Pursuant to the International Underwriting Agreement, the International Offering is fully underwritten by the International Underwriters, subject to the agreement on the Offer Price between the Sole Global Coordinator (on behalf of the Underwriters) and us on the Price Determination Date.

The International Underwriters are soliciting from prospective professional, institutional investors and/or other investors' indications of interest in acquiring International Offer Shares in the International Offering. Prospective professional, institutional investors and/or other investors will be required to specify the number of International Offer Shares they would be prepared to acquire either at different prices or at a particular price. This process is known as "book building". In Hong Kong, individual retail investors should apply for Shares in the Hong Kong Public Offering, as individual retail investors applying for International Offer Shares, including individual retail investors applying through banks and other institutions, will not be allocated any International Offer Shares.

Allocation of the International Offer Shares pursuant to the International Offering is based on a number of factors, including the level and timing of demand and whether or not it is expected that the relevant investor is likely to buy further and/or hold or sell its Shares after the Listing. Such allocation is generally intended to result in a distribution of the International Offer Shares on a basis which would lead to the establishment of a broad shareholder base to the benefit of our Company and our Shareholders as a whole.

The International Underwriters or selling agents nominated by the International Underwriters shall, on behalf of our Company, conditionally place the International Offer Shares with professional, institutional and/or other investors in Hong Kong, the United States (pursuant to Rule 144A and Regulation S of the US Securities Act), Europe and other regions. The International Offering shall be subject to the Global Offering restrictions set out in "Information about this Prospectus and the Global Offering" in this prospectus.

The International Offering is conditional on the same conditions as set out in "Conditions" in this section. The total number of International Offer Shares to be sold and transferred or allotted and issued pursuant to the International Offering may change as a result of the clawback arrangement referred to in the section "The Hong Kong Public Offering" above, the exercise of the Over-allotment Option and any reallocation of unsubscribed Shares originally included in the Hong Kong Public Offering.

## OVER-ALLOTMENT AND STABILISATION

### The Over-allotment Option

In connection with the Global Offering, we intend to grant to the Sole Global Coordinator the Over-allotment Option, which will be exercisable by the Sole Global Coordinator (on behalf of the International Underwriters) no later than 18 June 2010, being the 30th day after the last day for lodging applications under the Hong Kong Public Offering. Pursuant to the Over-allotment Option, our Company may be required to allot and issue at the Offer Price up to an aggregate of 37,500,000 additional Shares, representing 15% of the total number of Shares initially available under the Global Offering, in connection with overallocations in the International Offering, if any, to be issued and all issued on the same terms and conditions as the Shares subject to the Global Offering. If the Over-allotment Option is exercised in full, the additional Offer Shares will represent approximately 3.61% of our Company's enlarged issued share capital following the completion of the Global Offering and the exercise of the Over-allotment Option but without taking into account any Shares which may fall to be issued upon the exercise of any options that may be granted under the Share Option Scheme. In the event that the Over-allotment Option is exercised, a press announcement will be made.

### Stabilisation action

In connection with the Global Offering, the Sole Global Coordinator, or any person acting for them, may over-allocate or effect transactions with a view to supporting the market price of the Shares at a level higher than that which might otherwise prevail for a limited period. Such transactions, if commenced, may be discontinued at any time. The Sole Global Coordinator has been or will be appointed as stabilising manager (the "Stabilising Manager") for purposes of the Global Offering in accordance with the Securities and Futures (Price Stabilising) Rules made under the SFO and, should stabilising transactions be effected in connection with the Global Offering, this will be at the absolute discretion of the Stabilising Manager and will be effected in accordance with the laws, rules and regulations in place in Hong Kong on stabilisation. An announcement will be made to the public within seven days after the end of the stabilising period as required under the Securities and Futures (Price Stabilising) Rules made under the SFO.

Following any over-allocation of Shares in connection with the Global Offering, the Stabilising Manager or any person acting for them may cover such over-allocation by (among other methods) making purchases in the secondary market or exercising the Over-allotment Option in full or in part, or by any combination of purchases and exercise of the Over-allotment Option. Any such purchases will be made in compliance with all applicable laws and regulatory requirements including the Securities and Futures (Price Stabilising) Rules made under the SFO. The number of Shares which can be over-allocated will not exceed the number of Shares which may be issued upon exercise of the Over-allotment Option, being 37,500,000 Shares representing 15% of the Shares initially available under the Global Offering.

In order to facilitate the settlement of over-allocations in connection with the Global Offering, the Stabilising Manager (or their affiliate(s)) may choose to borrow Shares from Smart Port under stock borrowing arrangements, or acquire Shares from other sources, including exercise of the Over-allotment Option. Such stock borrowing arrangements include the Stock Borrowing Agreement.

The stabilising manager or its authorised agents may borrow up to 37,500,000 Shares from Smart Port, equivalent to the maximum number of additional Shares to be offered upon full exercise of the Over-allotment Option, under the Stock Borrowing Agreement. The stock borrowing arrangement under the Stock Borrowing Agreement will comply with the requirements set out in Rule 10.07(3) of the Listing Rules such that it will not be subject to the restrictions of Rule 10.07(1) of the Listing Rules. Rule 10.07(3) of the Listing Rules requires that:

- the Stock Borrowing Agreement will be for the sole purpose of covering any short position prior to the exercise of the Over-allotment Option in connection with the International Offering;

- the maximum number of Shares to be borrowed from Smart Port will be limited to the maximum number of Shares which may be issued or sold upon exercise of the Over-allotment Option;

- the same number of Shares so borrowed must be returned to Smart Port within three business days after the last day on which the Over-allotment Option may be exercised or, if earlier, the date on which the Over-allotment Option is exercised in full;

- borrowing of shares pursuant to the Stock Borrowing Agreement will be effected in compliance with all applicable Listing Rules, laws and other regulatory requirements; and

- no payments will be made to Smart Port by the stabilising manager in relation to the Stock Borrowing Agreement.

The possible stabilising action which may be taken by the Stabilising Manager in connection with the Global Offering may involve (among other things): (i) over-allocation of Shares, (ii) purchases of, or agreement to purchase, Shares, (iii) establishing, hedging and liquidating positions in Shares, (iv) exercising the Over-allotment Option in whole or in part and/or (v) offering or attempting to do any of the foregoing.

Specifically, prospective applicants for and investors in Offer Shares should note that:

- the Stabilising Manager may, in connection with any stabilising action, maintain a long position in the Shares;

- there is no certainty regarding the extent to which and the time period for which the Stabilising Manager will maintain such a position;

- liquidation of any such long position by the Stabilising Manager may have an adverse impact on the market price of the Shares;

- no stabilising action can be taken to support the price of the Shares for longer than the stabilising period which is expected to expire on 18 June 2010, being the 30th day after the date expected to be the latest date for lodging applications under the Hong Kong Public Offering. After this date, when no further action may be taken to support the price of the Shares, demand for the Shares, and therefore the price of the Shares, could fall;

- the price of any security (including the Shares) cannot be assured to stay at or above its offer price by the taking of any stabilising action; and

- stabilising bids may be made or transactions effected in the course of the stabilising action at any price at or below the Offer Price, which means that stabilising bids may be made or transactions effected at a price below the price paid by applicants for, or investors in, the Shares.

## LISTING ON ANY OTHER STOCK EXCHANGE

Our Directors are not considering any listing of our Company on any other overseas stock exchange. We have not submitted any application nor obtained any approval for the listing of the Shares on any other overseas stock exchange.

## 1 CHANNELS OF APPLYING FOR THE HONG KONG OFFER SHARES

You may apply for the Hong Kong Offer Shares by using one of the following channels:

- using a **WHITE** or **YELLOW** Application Form; or
- applying through the **White Form eIPO** service by submitting an electronic application to the White Form eIPO Service Provider through the designated website at **www.eipo.com.hk**; or
- **electronically instructing** HKSCC to cause HKSCC Nominees to apply for Hong Kong Offer Shares on your behalf.

**You may not both apply on a WHITE or YELLOW Application Form and give electronic application instructions to HKSCC.**

## 2 WHO CAN APPLY FOR THE HONG KONG OFFER SHARES

You can apply for the Hong Kong Offer Shares available for subscription by the public on a **WHITE** or **YELLOW** Application Form if you or any person(s) for whose benefit you are applying, are an individual, and:

- are 18 years of age or older;
- have a Hong Kong address;
- are not a US person (as defined in Regulation S);
- are outside the United States; and
- are not a legal or natural person of the PRC (except qualified domestic institutional investors).

If you wish to apply for Hong Kong Offer Shares online through the **White Form eIPO** service (**www.eipo.com.hk**), in addition to the above, you must also:

- have a valid Hong Kong identity card number; and
- be willing to provide a valid e-mail address and a contact telephone number.

You may only apply by means of the **White Form eIPO** service if you are an individual applicant. Corporations or joint applicants may not apply by means of the **White Form eIPO** service.

If the applicant is a firm, the application must be in the names of the individual members, not the firm's name. If the applicant is a body corporate, the Application Form must be signed by a duly authorised officer, who must state his or her representative capacity.

If an application is made by a person duly authorised under a valid power of attorney, our Company and the Sole Global Coordinator (as our agent and on behalf of the Hong Kong Underwriters) may accept it at our discretion, subject to any conditions we think fit, including production of evidence of the authority of the attorney.

The number of joint applicants may not exceed four.

## 3 WHICH APPLICATION CHANNELS YOU SHOULD USE

### (a) WHITE Application Forms

Use a **WHITE** Application Form if you want the Hong Kong Offer Shares to be registered in your own name.

### (b) White Form eIPO

Instead of using a **WHITE** Application Form, you may apply for the Hong Kong Offer Shares by means of the **White Form eIPO** service by submitting an application online through the designated website at **www.eipo.com.hk**. Use the **White Form eIPO** service if you want the Shares to be registered in your own name.

### (c) YELLOW Application Forms

Use a **YELLOW** Application Form if you want the Hong Kong Offer Shares to be registered in the name of HKSCC Nominees and deposited directly into CCASS for credit to your CCASS Investor Participant stock account or your designated CCASS Participant's stock account.

### (d) Instruct HKSCC to make an electronic application on your behalf

Instead of using a **YELLOW** Application Form, you may **electronically instruct** HKSCC to cause HKSCC Nominees to apply for the Hong Kong Offer Shares on your behalf via CCASS. Any Hong Kong Offer Shares allocated to you will be registered in the name of HKSCC Nominees and deposited directly into CCASS for credit to your CCASS Investor Participant stock account or your designated CCASS Participant's stock account.

## 4 WHERE TO COLLECT THE APPLICATION FORMS

(a) You can collect a **WHITE** Application Form and a prospectus during normal business hours from 9:00 a.m. on Friday, 14 May 2010 until 12:00 noon on Wednesday, 19 May 2010 from:

| | |
|---|---|
| The Hongkong and Shanghai Banking Corporation Limited | HSBC Main Building, 1 Queen's Road Central, Hong Kong |

- or any of the following branches of the Hongkong and Shanghai Banking Corporation Limited:

| | Branch Name | Branch Address |
|---|---|---|
| Hong Kong Island | Hong Kong Office | Level 3, 1 Queen's Road Central, HK |
| | North Point Branch | G/F, Winner House, 306-316 King's Road, North Point, HK |
| | Des Voeux Road West Branch | Western Centre, 40-50 Des Voeux Road West, HK |
| | Hopewell Centre Branch | Shops 2A, 2/F, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong |
| Kowloon | Kwun Tong Branch | No. 1, Yue Man Square, Kwun Tong, KLN |
| | Kowloon City Branch | 1/F, 18 Fuk Lo Tsun Road, Kowloon City, KLN |
| | Mong Kok Branch | L/G & U/G, 673 Nathan Road, Mong Kok, KLN |
| | 238 Nathan Road Branch | Shop No. 1 ,1/F, 238 Nathan Rd, KLN |
| | Tsim Sha Tsui Branch | Basement, UG/F & 1/F, 82-84 Nathan Road, Tsim Sha Tsui, KLN |
| New Territories | Yuen Long Branch | G/F, HSBC Building Yuen Long, 150-160 Castle Peak Rd, Yuen Long, NT |

(b) You can collect a **YELLOW** Application Form and a prospectus during normal business hours from 9:00 a.m. on Friday, 14 May 2010 until 12:00 noon on Wednesday, 19 May 2010 from:

the Depository Counter of HKSCC at 2nd Floor, Vicwood Plaza, 199 Des Voeux Road Central, Hong Kong; or

(c) Your broker may have **YELLOW** Application Forms and this prospectus available.

## 5 WHEN TO APPLY FOR THE HONG KONG OFFER SHARES

### (a) WHITE or YELLOW Application Forms

Completed **WHITE** or **YELLOW** Application Forms, with a cheque or banker's cashier order attached, must be lodged by 12:00 noon on Wednesday, 19 May 2010, or, if the application lists are not open on that day, then by 12:00 noon on the next day the lists are open.

Your completed **WHITE** or **YELLOW** Application Form, with full payment in HK dollars attached, should be deposited in the special collection boxes provided at any of the branches of The Hongkong and Shanghai Banking Corporation Limited listed under the section headed "How to Apply for Hong Kong Offer Shares — Where to Collect the Application Forms" in this prospectus at the following times:

**Friday, 14 May 2010 — 9:00 a.m. to 4:30 p.m.**
**Saturday, 15 May 2010 — 9:00 a.m. to 1:00 p.m.**
**Monday, 17 May 2010 — 9:00 a.m. to 4:30 p.m.**
**Tuesday, 18 May 2010 — 9:00 a.m. to 4:30 p.m.**
**Wednesday, 19 May 2010 — 9:00 a.m. to 12:00 noon**

(b) **White Form eIPO**

You may submit your application to the designated White Form eIPO Service Provider through the designated website at **www.eipo.com.hk** from 9:00 a.m. on Friday, 14 May 2010 until 11:30 a.m. on Wednesday, 19 May 2010 or such later time as described under the paragraph headed "How to Apply for Hong Kong Offer Shares — How to Apply through the White Form eIPO Service — Effect of bad weather conditions on the last application day" (24 hours daily, except on the last application day). The latest time for completing full payment of application monies in respect of such applications will be 12:00 noon on Wednesday, 19 May 2010, the last application day, or, if the application lists are not open on that day, then by the time and date stated in the paragraph headed "How to Apply for Hong Kong Offer Shares — How to Apply through the White Form eIPO Service — Effect of bad weather conditions on the last application day". You will not be permitted to submit your application to the designated White Form eIPO Service Provider through the designated website at **www.eipo.com.hk** after 11:30 a.m. on the last day for submitting applications. If you have already submitted your application and obtained an application reference number from the website prior to 11:30 a.m., you will be permitted to continue the application process (by completing payment of application monies) until 12:00 noon on the last day for submitting applications, when the application lists close.

(c) **Electronic application instructions to HKSCC via CCASS**

CCASS Clearing/Custodian Participants should input **electronic application instructions** via CCASS at the following times on the following dates:

**Friday, 14 May 2010 — 9:00 a.m. to 8:30 p.m.[1]**
**Saturday, 15 May 2010 — 8:00 a.m. to 1:00 p.m.[1]**
**Monday, 17 May 2010 — 8:00 a.m. to 8:30 p.m.[1]**
**Tuesday, 18 May 2010 — 8:00 a.m. to 8:30 p.m.[1]**
**Wednesday, 19 May 2010 — 8:00 a.m.[1] to 12:00 noon**

*Note 1: These times are subject to such changes as HKSCC may determine from time to time with prior notification to CCASS Participants.*

CCASS Investor Participants can input **electronic application instructions** from 9:00 a.m. on Friday, 14 May 2010 until 12:00 noon on Wednesday, 19 May 2010 (24 hours daily, except the last application day).

The latest time for inputting your **electronic application instructions** via CCASS is 12:00 noon on Wednesday, 19 May 2010, the last application day, or if the application lists are not open on that day, by the time and date stated in the paragraph headed "How to Apply for Hong Kong Offer Shares — When to Apply for the Hong Kong Offer Shares — Effect of bad weather conditions on the opening of the application lists" in this prospectus.

(d) **Application lists**

The application lists will be open from 11:45 a.m. to 12:00 noon on Wednesday, 19 May 2010, except as provided in the paragraph headed "How to Apply for Hong Kong Offer Shares — When to Apply for the Hong Kong Offer Shares — Effect of bad weather conditions on the opening of the application lists" in this prospectus. No proceedings will be taken on applications for the Hong Kong Offer Shares and no allotment of any of such Hong Kong Offer Shares will be made until after the closing of the application lists.

(e) **Effect of bad weather conditions on the opening of the application lists**

The application lists will be opened between 11:45 a.m. and 12:00 noon on Wednesday, 19 May 2010, subject to weather conditions. The application lists will not be open in relation to the Hong Kong Public Offering if there is:

- a tropical cyclone warning signal number 8 or above; or
- a "black" rainstorm warning signal,

in force in Hong Kong at any time between 9:00 a.m. and 12:00 noon on Wednesday, 19 May 2010, or if there are similar extraneous factors as are acceptable to the Stock Exchange. Instead, they will be open between 11:45 a.m. and 12:00 noon on the next Business Day which does not fall within the above circumstances at any time between 9:00 a.m. and 12:00 noon in Hong Kong.

If the application lists of the Hong Kong Public Offering do not open and close on Wednesday, 19 May 2010 or if there is a tropical cyclone warning signal number 8 or above or a "black" rainstorm warning signal in force in Hong Kong on the other dates mentioned in the section headed "Expected Timetable" in this prospectus, such dates mentioned in the section headed "Expected Timetable" in this prospectus may be affected. A press announcement will be made in such event.

## 6 HOW TO APPLY USING A WHITE OR YELLOW APPLICATION FORM

(a) Obtain a **WHITE** or **YELLOW** Application Form.

(b) There are detailed instructions on each Application Form. You should read the instructions in this prospectus and the relevant Application Form carefully. If you do not follow the instructions, your application may be rejected and returned by ordinary post together with the accompanying cheque or banker's cashier order to you (or the first-named applicant in the case of joint applicants) at your own risk to the address stated on your Application Form.

(c) Decide how many Hong Kong Offer Shares you want to purchase. The table in the Application Forms sets out the total amount payable for the specified number of the Hong Kong Offer Shares.

(d) Complete the Application Form in English (save as otherwise indicated) and sign it. Only written signatures will be accepted. Applications made by corporations, whether on their own behalf, or on behalf of other persons, must be stamped with a company chop (bearing our company name) and signed by a duly authorised officer, whose representative capacity must be stated. If you are applying for the benefit of someone else, you, rather than that person, must sign the Application Form. If it is a joint application, all applicants must sign it. If your application is made through a duly authorised attorney, our Company and the Sole Sponsor (or their respective agents or nominees) may accept it at their discretion, and subject to any conditions they think fit, including production of evidence of the authority of your attorney.

(e) Each Application Form must be accompanied by either one cheque or one banker's cashier order, which must be stapled to the top left-hand corner of the Application Form.

If you pay by cheque, the cheque must:

- be in Hong Kong dollars;
- not be post-dated;
- be drawn on your Hong Kong dollar bank account in Hong Kong;
- show your account name, which must either be pre-printed on the cheque, or be endorsed on the back by a person authorised by the bank. This account name must be the same as the name on the Application Form. If it is a joint application, the account name must be the same as the name of the first-named joint applicant;
- be made payable to "HSBC Nominees (Hong Kong) Limited — Youyuan Public Offer"; and
- be crossed "Account Payee Only".

Your application may be rejected if your cheque does not meet all of these requirements or is dishonoured on its first presentation.

If you pay by banker's cashier order, the banker's cashier order must:

- be issued by a licensed bank in Hong Kong and have your name certified on the back by a person authorised by the bank. The name on the back of the banker's cashier order and the name on the Application Form must be the same. If it is a joint application, the name on the back of the banker's cashier order must be the same as the name of the first-named joint applicant;

- be in Hong Kong dollars;
- not be post-dated;
- be made payable to "HSBC Nominees (Hong Kong) Limited — Youyuan Public Offer"; and
- be crossed "Account Payee Only".

Your application is liable to be rejected if your banker's cashier order does not meet all of these requirements.

(f) If you are applying for Shares using a **WHITE** or **YELLOW** Application Form, you should lodge your Application Form in the special collection boxes provided at any of the branches of The Hongkong and Shanghai Banking Corporation Limited listed under the section headed "How to Apply for Hong Kong Offer Shares — Where to Collect the Application Forms" in this prospectus and by the time referred to in the section headed "How to Apply for Hong Kong Offer Shares — When to Apply for the Hong Kong Offer Shares — WHITE or YELLOW Application Forms" in this prospectus.

(g) Multiple or suspected multiple applications are liable to be rejected. Please refer to "How Many Applications You May Make" in this section.

(h) In order for the **YELLOW** Application Forms to be valid:

- If you are applying through a designated CCASS Participant (other than a CCASS Investor Participant):
  - — the designated CCASS Participant must endorse the form with its company chop (bearing its company name) and insert its CCASS Participant I.D. in the appropriate box.
- If you are applying as an individual CCASS Investor Participant:
  - — you must fill in your full name and your Hong Kong Identity Card number; and
  - — you must insert your CCASS Participant I.D. in the appropriate box.
- If you are applying as a joint individual CCASS Investor Participant:
  - — you must insert all joint CCASS Investor Participants' names and the Hong Kong Identity Card numbers of all joint CCASS Investor Participants; and
  - — you must insert your CCASS Participant I.D. in the appropriate box.

- If you are applying as a corporate CCASS Investor Participant:
  - — you must insert your company name and your company's Hong Kong business registration number; and
  - — you must fill in your CCASS Participant I.D. and stamp your company chop (bearing your company's name) in the appropriate box.

Incorrect or omission details of the CCASS Participant (including CCASS Participant I.D. and/or company chop bearing its company name) or other similar matters may render the application invalid.

(i) Nominees who wish to submit separate applications in their names on behalf of different beneficial owners are requested to designate on each Application Form in the box marked "For nominees" an identification number for each beneficial owner.

(j) If an application is made by a person duly authorised under a valid power of attorney, our Company and the Sole Global Coordinator (as our agent and on behalf of the Hong Kong Underwriters) may accept it at our discretion, subject to any conditions we think fit, including production of evidence of the authority of the attorney. Our Company and the Sole Global Coordinator (as our agent and on behalf of the Hong Kong Underwriters), will have full discretion to reject or accept any application, in full or in part, without assigning any reason.

**7 HOW TO COMPLETE THE APPLICATION FORM**

There are detailed instructions on each Application Form. You should read these instructions carefully. If you do not strictly follow the instructions your application may be rejected.

If the Offer Price as finally determined is less than HK$3.38 per Share, appropriate refund payments (including the brokerage fee, the SFC transaction levy and the Stock Exchange trading fee attributable to the surplus application monies) will be made to successful or partially successful applications, without interest. Details of the procedure for refunds are set out in "How to Apply for Hong Kong Offer Shares — Despatch/Collection of Share Certificates/e-Refund Payment Instructions/Refund Cheques" in this section.

You should note that by signing on the Application Form:

(a) you agree with our Company and each Shareholder of our Company that the Shares in our Company are freely transferable by the holders thereof;

(b) you confirm that you have only relied on the information and representations in this prospectus in making your application and will not rely on any other information and representations concerning our Company save as set out in any supplement to this prospectus;

(c) you agree that our Company, the Sole Sponsor, the Underwriters and any of their respective directors, officers, employees, partners, agents or advisers are liable only for the information and representations contained in this prospectus and any supplement thereto;

(d) you undertake and confirm that, you (if the application is made for your benefit) or the person(s) for whose benefit you have made the application, have not indicated an interest for, applied for or taken up any Offer Shares under the International Offering; and

(e) you agree to disclose to our Company and/or our Hong Kong Share Registrar, the receiving banker, the Sole Global Coordinator and their respective advisers and agents personal data and any information which they require about you or the person(s) for whose benefit you have made the application.

**8 HOW TO APPLY THROUGH THE WHITE FORM eIPO SERVICE**

(a) If you are an individual and meet the criteria set out above in relation to applying for Hong Kong Offer Shares through the **White Form eIPO** service in "How to Apply for Hong Kong Offer Shares — Who Can Apply for the Hong Kong Offer Shares" in this section, you may apply through the **White Form eIPO** service by submitting an application through the designated website at **www.eipo.com.hk**. If you apply through the **White Form eIPO** service the Shares will be issued in your own name.

(b) Detailed instructions for application through the **White Form eIPO** service are set out on the designated website at **www.eipo.com.hk**. You should read these instructions carefully. If you do not follow the instructions, your application may be rejected by the designated White Form eIPO Service Provider and may not be submitted to our Company.

(c) In addition to the terms and conditions set out in this prospectus, the designated White Form eIPO Service Provider may impose additional terms and conditions upon you for the use of the **White Form eIPO** service. Such terms and conditions are set out on the designated website at **www.eipo.com.hk**. You will be required to read, understand and agree to such terms and conditions in full prior to making any application.

(d) By submitting an application to the designated White Form eIPO Service Provider through the **White Form eIPO** service (**www.eipo.com.hk**), you are deemed to have authorised the designated White Form eIPO Service Provider to transfer the details of your application to our Company and our Hong Kong Share Registrar.

(e) You may submit an application through the **White Form eIPO** service in respect of a minimum of 1,000 Hong Kong Offer Shares. Each **electronic application instruction** in respect of more than 1,000 Hong Kong Offer Shares must be in one of the numbers set out in the table in the Application Forms, or as otherwise specified on the designated website at **www.eipo.com.hk**.

(f) You may submit your application to the designated White Form eIPO Service Provider through the designated website at **www.eipo.com.hk** from 9:00 a.m. on Friday, 14 May

2010 until 11:30 a.m. on Wednesday, 19 May 2010 or such later time as described under the paragraph headed "How to Apply for Hong Kong Offer Shares — How to Apply through the White Form eIPO Service — Effect of bad weather conditions on the last application day" (24 hours daily, except on the last application day). The latest time for completing full payment of application monies in respect of such applications will be 12:00 noon on Wednesday, 19 May 2010, the last application day, or, if the application lists are not open on that day, then by the time and date stated in the paragraph headed "How to Apply for Hong Kong Offer Shares — How to Apply through the White Form eIPO Service — Effect of bad weather conditions on the last application day".

(g) You will not be permitted to submit your application to the designated White Form eIPO Service Provider through the designated website at **www.eipo.com.hk** after 11:30 a.m. on the last day for submitting applications. If you have already submitted your application and obtained an application reference number from the website prior to 11:30 a.m., you will be permitted to continue the application process (by completing payment of application monies) until 12:00 noon on the last day for submitting applications, when the application lists close. You should make payment for your application made through the **White Form eIPO** service in accordance with the methods and instructions set out in the designated website at **www.eipo.com.hk**. If you do not make complete payment of the application monies (including any related fees) on or before 12:00 noon on Wednesday, 19 May 2010, or such later time as described under the paragraph headed "How to Apply for Hong Kong Offer Shares — How to Apply through the White Form eIPO Service — Effects of bad weather conditions on the last application day" in this prospectus, the designated White Form eIPO Service Provider will reject your application and your application monies will be returned to you in the manner described in the designated website at **www.eipo.com.hk**.

*Effect of bad weather conditions on the last application day*

The latest time for submitting an application to the designated White Form eIPO Service Provider through the **White Form eIPO** service will be 11:30 a.m., and the latest time for completing full payment of application monies in respect of such applications will be 12:00 noon on Wednesday, 19 May 2010, the last application day. If there is:

- a tropical cyclone warning signal number 8 or above; or
- a "black" rainstorm warning

in force in Hong Kong at any time between 9:00 a.m. and 12:00 noon on Wednesday, 19 May 2010, the last application day will be postponed to the next business day which does not have either of those waning signals in force in Hong Kong at any time between 9:00 a.m. and 12:00 noon on such day.

*Conditions of the White Form eIPO service*

In using the **White Form eIPO** service to apply for the Hong Kong Offer Shares, the applicant shall be deemed to have accepted the following conditions:

That the applicant:

- **Applies** for the desired number of Hong Kong Offer Shares on the terms and conditions of this prospectus and White Form eIPO Application Form subject to the Articles of Association;

- **Undertakes** and agrees to accept the Hong Kong Offer Shares applied for, or any lesser number allotted to the applicant on such application;

- **Declares** that such application is the only application made and the only application intended by the applicant to be made whether on a **WHITE** or **YELLOW** Application Form or by giving **electronic application instructions** to HKSCC or to the White Form eIPO Service Provider under the **White Form eIPO** service, to benefit the applicant or the person for whose benefit the applicant is applying;

- **Undertakes** and **confirms** that the applicant or the person for whose benefit the applicant is applying has not applied for or taken up, or indicated an interest for, or received or been placed or allocated (including conditionally and/or provisionally) and will not apply for or take up, or indicate an interest for, any International Offer Shares, nor otherwise participate in the International Offering;

- **Understands** that this declaration and representation will be relied upon by our Company in deciding whether or not to make any allotment of Hong Kong Offer Shares in response to such application;

- **Authorises** our Company to place the applicant's name on the register of members of our Company as the holder of any Hong Kong Offer Shares to be allotted to the applicant, and (subject to the terms and conditions set out in this prospectus) to send any Share certificates by ordinary post at the applicant's own risk to the address given on the White Form eIPO Application Form except where the applicant has applied for 1,000,000 or more Hong Kong Offer Shares and that applicant collects any Share certificate(s) in person in accordance with the procedures prescribed in the White Form eIPO application and this prospectus;

- **Authorises** the Company to despatch any e-Refund payment instructions to the applicant's application payment bank account if the applicant has completed payment of the **White Form eIPO** application monies from a single bank account; or **authorises** the Company to issue and despatch any refund cheque to the address given on the **White Form eIPO** application if the applicant has completed payment of the application monies from multi-bank accounts, and

- **Requests** that any refund cheque(s) be made payable to the applicant, and (subject to the terms and conditions set out in this prospectus) authorises our Company to send any refund cheques by ordinary post and at the applicant's own risk to the address given on the White Form eIPO application (except where the applicant has applied for 1,000,000 or more Hong Kong Offer Shares and collects any refund cheque(s) in person in accordance with the procedures prescribed in the designated White Form eIPO website at **www.eipo.com.hk** and this prospectus);

- **Has read** the terms and conditions and application procedures set out on in the White Form eIPO Application Form, this prospectus and the White Form eIPO website (**www.eipo.com.hk**) and **agrees** to be bound by them.

- **Represents, warrants** and **undertakes** that (i) the applicant or any persons for whose benefit the applicant is applying is outside the United States when completing and submitting the White Form eIPO Application Form and is not a US person (as defined in Regulation S under the US Securities Act, as amended), or is a person described in paragraph (h)(3) of Rule 902 of Regulation S under the US Securities Act as amended, and (ii) the allotment of or application for the Hong Kong Offer Shares to or by the applicant or the persons for whose benefit this application is made would not require our Company, the Sole Global Coordinator or the Underwriters to comply with any requirements under any law or regulation (whether or not having the force of law) of any territory outside Hong Kong; and

- **Agrees** that such application, any acceptance of it and the resulting contract, will be governed by and construed in accordance with the Laws of Hong Kong.

*Supplemental Information*

If any supplement to this prospectus is issued, applicant(s) who have already submitted an **electronic application instruction** through the **White Form eIPO** service may or may not (depending on the information contained in the supplement) be notified that they can withdraw their applications. If applicant(s) have not been so notified, or if applicant(s) have been notified but have not withdrawn their applications in accordance with the procedure to be notified, all applications through the **White Form eIPO** service that have been submitted remain valid and may be accepted. Subject to the above and below, an application once made through the **White Form eIPO** service is irrevocable and applicants shall be deemed to have applied on the basis of this prospectus as supplemented.

*Effect of completing and submitting an application through the White Form eIPO service*

By completing and submitting an application through the **White Form eIPO** service, you for yourself or as agent or nominee for and on behalf of any person for whom you act as agent or nominee shall be deemed to:

- instruct and authorise our Company, the Sole Global Coordinator (or their respective agents or nominees) as agent for our Company to do on your behalf all things necessary to register any Hong Kong Offer Shares allotted to you in your name as required by the Articles of Association and otherwise to give effect to the arrangements described in this prospectus and the White Form eIPO Application Form;

- confirm that you have only relied on the information and representations in this prospectus in making your application and will not rely on any other information and representations save as set out in any supplement to this prospectus;

- agree that our Company and the Directors are liable only for the information and representations contained in this prospectus and any supplement thereto;

- agree (without prejudice to any other rights which you may have) that once your application has been accepted, you may not rescind it because of an innocent misrepresentation;

- (if the application is made for your own benefit) warrant that such application is the only application which will be made for your benefit on a **WHITE** or **YELLOW** Application Form or by giving **electronic application instructions** to HKSCC or to the White Form eIPO Service Provider via the **White Form eIPO** service;

- (if you are an agent or nominee for another person) warrant that reasonable enquiries have been made of that other person that such application is the only application which will be made for the benefit of that other person on a **WHITE** or **YELLOW** Application Form or by giving **electronic application instructions** to HKSCC or to the White Form eIPO Service Provider via the **White Form eIPO** service, and that you are duly authorised to submit such application as that other person's agent or nominee;

- undertake and confirm that, you (if the application is made for your benefit) or the person(s) for whose benefit you have made this application have not applied for or taken up, or indicated an interest for, and will not apply for, take up or indicate an interest for, any International Offer Shares;

- agree that your application, any acceptance of it and the resulting contract will be governed by and construed in accordance with the Laws of Hong Kong;

- agree to disclose to our Company, and/or its Hong Kong Share Registrar, receiving bankers, the Sole Sponsor, the Sole Global Coordinator and their respective advisers and agents personal data and any information which they require about you or the person(s) for whose benefit you have made this application;

- agree with our Company and each Shareholder of our Company, and our Company agrees with each of its Shareholders, to observe and comply with the Companies Ordinance, the Memorandum of Association and the Articles of Association;

- agree with our Company and each Shareholder of our Company that the Shares in our Company are freely transferable by the holders thereof;

- authorise our Company to enter into a contract on your behalf with each Director and officer of our Company whereby each such Director and officer undertakes to observe and comply with his or her obligations to Shareholders as stipulated in the Memorandum of Association and the Articles of Association;

- represent, warrant and undertake that you are not, and none of the other person(s) (if any) for whose benefit you are applying, are a US person (as defined in Regulation S);

- represent and warrant that you understand that the Shares have not been and will not be registered under the US Securities Act and you are outside the United States (as defined in Regulation S) when completing the Application Form or are a person described in paragraph (h)(3) of Rule 902 of Regulation S;

- confirm that you have read the terms and conditions and application procedures set out in this prospectus, the White Form eIPO Application Form and the White Form eIPO website (**www.eipo.com.hk**) and agree to be bound by them;

- undertake and agree to accept the Shares applied for, or any lesser number allocated to you under your application; and

- if the laws of any place outside Hong Kong are applicable to your application, agree and warrant that you have complied with all such laws and none of our Company, the Sole Global Coordinator and the Underwriters nor any of their respective officers or advisers will infringe any laws outside Hong Kong as a result of the acceptance of your offer to purchase, or any actions arising from your rights and obligations under the terms and conditions contained in this prospectus, the White Form eIPO Application Form and the White Form eIPO website (**www.eipo.com.hk**).

Our Company, the Sole Sponsor, the Hong Kong Underwriters and their respective directors, officers, employees, partners, agents, advisers, and any other parties involved in the Global Offering are entitled to rely on any warranty, representation or declaration made by you in such application.

*Additional information*

For the purposes of allocating Hong Kong Offer Shares, each applicant giving **electronic application instructions** through the **White Form eIPO** service to the White Form eIPO Service Provider through the designated website at **www.eipo.com.hk** will be treated as an applicant.

If your payment of application monies is insufficient, or in excess of the required amount, having regard to the number of Hong Kong Offer Shares for which you have applied, or if your application is otherwise rejected by the designated White Form eIPO Service Provider, the designated White Form eIPO Service Provider may adopt alternative arrangements for the refund of monies to you. Please refer to the additional information provided by the designated White Form eIPO Service Provider on the designated website at **www.eipo.com.hk**.

Please note that internet services may have capacity limitations and/or be subject to service interruptions from time to time. To ensure that you can submit your applications through the **White Form eIPO** service (**www.eipo.com.hk**), you are advised not to wait until the last day for submitting applications in the Hong Kong Public Offering to submit your **electronic application instructions**. In the event that you have problems connecting to the designated website for the **White Form eIPO** service (**www.eipo.com.hk**), you should submit a **WHITE** Application Form. However, once you have submitted

**electronic application instructions** and completed payment in full using the application reference number provided to you on the designated website, you will be deemed to have made an actual application and should not submit a **WHITE** Application Form. Please refer to "How Many Applications You May Make" in this section.

**Environmental Protection**

The obvious advantage of **White Form eIPO** is to save the use of papers via the self-serviced and electronic application process. Computershare Hong Kong Investor Services Limited, being the designated White Form eIPO Service Provider, will contribute HK$2 for each "Youyuan International Holdings Limited" **White Form eIPO** application submitted via **www.eipo.com.hk** to support the funding of the "Source of DongJiang - Hong Kong Forest" project initiated by Friends of the Earth (HK).

**Personal Data**

The section of the Application Form captioned "Personal Data" applies to any personal data held by our Company, the Hong Kong Share Registrar, our receiving bankers, the Sole Sponsor, the Underwriters and any of their respective advisers and agents about you in the same way as it applies to personal data about applicants other than HKSCC Nominees.

**Warning**

**The application for Hong Kong Offer Shares through the White Form eIPO service (www.eipo.com.hk) is only a facility provided by the designated White Form eIPO Service Provider to public investors. Our Company, our Directors, the Sole Global Coordinator, the Underwriters and the White Form eIPO Service Provider take no responsibility for such applications, and provide no assurance that applications through the White Form eIPO service (www.eipo.com.hk) will be submitted to our Company or that you will be allotted any Hong Kong Offer Shares.**

**9 HOW TO APPLY BY GIVING ELECTRONIC APPLICATION INSTRUCTIONS TO HKSCC**

(a) CCASS Participants may give **electronic application instructions** via CCASS to HKSCC to apply for Hong Kong Offer Shares and to arrange payment of the monies due on application and payment of refunds. This will be in accordance with their participant agreements with HKSCC and the General Rules of CCASS and the CCASS Operational Procedures.

(b) If you are a CCASS Investor Participant, you may give **electronic application instructions** through the CCASS Phone System by calling 2979 7888 or CCASS Internet System at *https://ip.ccass.com* (according to the procedures contained in HKSCC's "An Operating Guide for Investor Participants" in effect from time to time). HKSCC can also input **electronic application instructions** for you if you go to:

Hong Kong Securities Clearing Company Limited Customer Service Centre
2/F Vicwood Plaza, 199 Des Voeux Road Central, Hong Kong

and complete an input request form.

Prospectuses are available for collection from the above address.

(c) If you are not a CCASS Investor Participant, you may instruct your broker or custodian who is a CCASS Clearing Participant or a CCASS Custodian Participant to give **electronic application instructions** via CCASS terminals to apply for Hong Kong Offer Shares on your behalf.

(d) You are deemed to have authorised HKSCC and/or HKSCC Nominees to transfer the details of your application, whether submitted by you or through your CCASS Clearing/Custodian Participant, to our Company and the Hong Kong Share Registrar.

(e) You may give or cause your CCASS Clearing/Custodian Participant to give **electronic application instructions** in respect of a minimum of 1,000 Hong Kong Offer Shares. Each **electronic application instruction** in respect of more than 1,000 Hong Kong Offer Shares must be in one of the numbers set out in the table in the Application Form. No application for any other number of Hong Kong Offer Shares will be considered and any such application is liable to be rejected.

(f) Where a **WHITE** Application Form is signed by HKSCC Nominees on behalf of persons who have given **electronic application instructions** to apply for the Hong Kong Offer Shares:

(i) HKSCC Nominees is only acting as nominee for those persons and shall not be liable for any breach of the terms and conditions of the **WHITE** Application Form or this prospectus; and

(ii) HKSCC Nominees shall do the following things on behalf of each of such persons:

- agree that the Hong Kong Offer Shares to be allotted shall be issued in the name of HKSCC Nominees and deposited directly into CCASS for the credit of the stock account of the CCASS Participant who has inputted **electronic application instructions** on that person's behalf or that person's CCASS Investor Participant stock account;

- undertake and agree to accept the Hong Kong Offer Shares in respect of which that person has given **electronic application instructions** or any lesser number;

- undertake and confirm that that person has not indicated an interest for, applied for or taken up any International Offer Shares;

- (if the **electronic application instructions** are given for that person's own benefit) declare that only one set of **electronic application instructions** has been given for that person's benefit;

- (if that person is an agent for another person) declare that that person has only given one set of **electronic application instructions** for the benefit of that other person and that that person is duly authorised to give those instructions as that other person's agent;

- understand that the above declaration will be relied upon by our Company and the Sole Global Coordinator in deciding whether or not to make any allotment of Hong Kong Offer Shares in respect of the **electronic application instructions** given by that person and that that person may be prosecuted if he makes a false declaration;

- authorise our Company to place the name of HKSCC Nominees on the register of members of our Company as the holder of the Hong Kong Offer Shares allotted in respect of that person's **electronic application instructions** and to send share certificate(s) and/or refund money in accordance with the arrangements separately agreed between our Company and HKSCC;

- confirm that that person has read the terms and conditions and application procedures set out in this prospectus and agrees to be bound by them;

- confirm that that person has only relied on the information and representations in this prospectus in giving that person's **electronic application instructions** or instructing that person's CCASS Clearing/Custodian Participant to give **electronic application instructions** on that person's behalf and will not rely on any other information and representations save as set out in any supplement to this prospectus;

- agree that our Company, the Sole Sponsor, the Underwriters and any of their respective directors, officers, employees, partners, agents or advisers and any other parties involved in the Global Offering are liable only for the information and representations contained in this prospectus and any supplement thereto;

- agree (without prejudice to any other rights which that person may have) that once the application made by HKSCC Nominees is accepted, the application cannot be rescinded for innocent misrepresentation;

- agree to disclose that person's personal data to our Company, the Hong Kong Share Registrar, receiving banker, the Sole Sponsor, the Underwriters and any of their respective advisers and agents and any information which they may require about that person;

- agree that that any application made by HKSCC Nominees on behalf of that person pursuant to **electronic application instructions** given by that person is irrevocable on or before the end of the fifth day after the time of the opening of the application lists (excluding for this purpose any day which is a Saturday, Sunday or public holiday in Hong Kong), such agreement to take effect as a collateral contract with our Company and to become binding when that person gives the instructions and such collateral contract to be in consideration of our Company agreeing that it will not offer any Hong Kong Offer Shares to any person on or before the end of the fifth day after the time of the opening of the application lists (excluding for this purpose any day which is a Saturday, Sunday or public holiday in Hong Kong), except by means of one of the procedures referred to in this prospectus. However, HKSCC Nominees may revoke the application on or before the end of the fifth day after the time of the opening of the application lists (excluding for this purpose any day which is a Saturday, Sunday or public holiday in Hong Kong), if a person responsible for this prospectus under section 40 of the Companies Ordinance gives a public notice under that section which excludes or limits the responsibility of that person for this prospectus;

- agree that once the application made by HKSCC Nominees is accepted, neither that application nor that person's **electronic application instructions** can be revoked, and that acceptance of that application will be evidenced by the announcement of the results of the Hong Kong Public Offering published by our Company;

- agree with our Company (for our Company itself and for the benefit of each of its Shareholders) that Shares in our Company are freely transferable by the holders thereof;

- agree with our Company, for ourselves and for the benefit of each of the Group's Shareholders (and so that the Group will be deemed by the Group's acceptance in whole or in part of the application by HKSCC Nominees to have agreed, for itself and on behalf of each of the Shareholders, with each CCASS Participant giving **electronic application instructions**) to observe and comply with the Cayman Companies Law, the Companies Ordinance and the Memorandum of Association and the Articles of Association;

- agree to the arrangements, undertakings and warranties specified in the participant agreement between that person and HKSCC, read the General Rules of CCASS and the CCASS Operational Procedures, in respect of the giving of **electronic application instructions** relating to Hong Kong Offer Shares; and

- agree that that person's application, any acceptance of it and the resulting contract will be governed by and construed in accordance with the Laws of Hong Kong.

(g) By giving **electronic application instructions** to HKSCC or instructing your CCASS Clearing/Custodian Participant to give such instructions to HKSCC, you (and if you are joint applicants, each of you jointly and severally) are deemed to have done the following things. Neither HKSCC nor HKSCC Nominees shall be liable to our Company or any other person in respect of the things mentioned below:

- instructed and authorised HKSCC to cause HKSCC Nominees (acting as nominee for the relevant CCASS Participants) to apply for the Hong Kong Offer Shares on your behalf;

- instructed and authorised HKSCC to arrange payment of the maximum offer price, and the related brokerage, the SFC transaction levy, and the Stock Exchange trading fee by debiting your designated bank account and, in the case of a wholly or partially unsuccessful application and/or the Offer Price is less than the initial price per Offer Share paid on application, refund of the application monies (in each case including brokerage, the SFC transaction levy, and the Stock Exchange trading fee) by crediting your designated bank account;

- instructed and authorised HKSCC to cause HKSCC Nominees to do on your behalf all the things which it is stated to do on your behalf in the **WHITE** Application Form.

(h) If you are suspected of having made multiple applications or if more than one application is made for your benefit, the number of Hong Kong Offer Shares applied for by HKSCC Nominees will be automatically reduced by the number of Hong Kong Offer Shares in respect of which you have given such instructions and/or in respect of which such instructions have been given for your benefit. Any electronic application instructions to make an application for Hong Kong Offer Shares given by you or for your benefit to HKSCC shall be deemed to be an actual application for the purpose of considering whether multiple applications have been made.

(i) For the purpose of allocating Hong Kong Offer Shares, HKSCC Nominees shall not be treated as an applicant. Instead, each CCASS Participant who gives **electronic application instructions** or each person for whose benefit each such instruction is given shall be treated as an applicant.

(j) The section of the Application Form headed "Personal Data" applies to any personal data held by our Company, the Hong Kong Share Registrar, our receiving bankers, the Sole Sponsor, the Underwriters and any of their respective advisers and agents about you in the same way as it applies to personal data about applicants other than HKSCC Nominees.

(k) For the avoidance of doubt, we and all other parties involved in the preparation of this prospectus acknowledge that each CCASS Participant who gives or causes to give electronic application instructions is a person who may be entitled to compensation under section 40 of the Companies Ordinance.

**Warning**

**Application for Hong Kong Offer Shares by giving electronic application instructions to HKSCC is only a facility provided to CCASS Participants. Our Company, our Directors, the Sole Global Coordinator, the Sole Sponsor, the Underwriters and any other parties involved in the Global Offering take no responsibility for the application and provide no assurance that any CCASS Participant will be allotted any Hong Kong Offer Shares.**

**To ensure that CCASS Investor Participants can give their electronic application instructions to HKSCC through the CCASS Phone System or the CCASS Internet System, CCASS Investor Participants are advised not to wait until the last minute to input their electronic application instructions. If CCASS Investor Participants have problems in connecting to the CCASS Phone System or the CCASS Internet System to submit their electronic application instructions, they should either:**

**(a) submit a WHITE or YELLOW Application Form (as appropriate); or**

**(b) go to HKSCC's Customer Service Centre to complete an input request form for electronic application instructions before 12:00 noon on Wednesday, 19 May 2010 or such later time as described under the paragraph headed "How to Apply for Hong Kong Offer Shares — When to Apply for the Hong Kong Offer Shares — Effect of bad weather conditions on the opening of the application lists" in this prospectus.**

## 10 HOW MANY APPLICATIONS YOU MAY MAKE

Multiple applications or suspected multiple applications are liable to be rejected.

***You may make more than one application for the Hong Kong Offer Shares only if:***

You are a **nominee**, in which case you may both give **electronic application instructions** to HKSCC (if you are a CCASS Participant) and lodge more than one Application Form in your own name on behalf of different beneficial owners. In the box on the Application Form marked "For nominees" you must include:

- an account number; or
- some other identification code

for **each** beneficial owner. If you do not include this information, the application will be treated as being made for your benefit.

***Otherwise, multiple applications are not allowed and will be rejected.***

If you apply by means of the **White Form eIPO** service, once you complete payment in respect of any **electronic application instruction** given by you or for your benefit to the designated White Form eIPO Service Provider to make an application for Hong Kong Offer Shares, an actual application shall be deemed to have been made. For the avoidance of doubt, giving an **electronic application instruction** under the **White Form eIPO** service more than once and obtaining different application reference numbers without effecting full payment in respect of a particular reference number will not constitute an actual application.

If you are suspected of submitting more than one application through the **White Form eIPO** service by giving **electronic application instructions** through the designated website at **www.eipo.com.hk** and completing payment in respect of such **electronic application instructions**, or of submitting one application through the **White Form eIPO** service and one or more applications by any other means, all of your applications are liable to be rejected.

It will be a term and condition of all applications that by completing and delivering an Application Form or submitting an **electronic application instruction**, you:

- (if the application is made for your own benefit) warrant that the application made pursuant to the Application Form or **electronic application instruction** is the only application which will be made for your benefit on a **WHITE** or **YELLOW** Application Form or by giving **electronic application instructions** to HKSCC or to the designated White Form eIPO Service Provider through the **White Form eIPO** service;

- (if you are an agent for another person) warrant that reasonable enquiries have been made of that other person which confirm that this is the only application which will be made for the benefit of that other person on a **WHITE** or **YELLOW** Application Form or by giving **electronic application instructions** to HKSCC or to the designated White Form eIPO Service Provider through the **White Form eIPO** service, and that you are duly authorised to sign the Application Form or give **electronic application instructions** as that other person's agent.

**All** of your applications will be rejected as multiple applications if you, or you and your joint applicant(s) together:

- make more than one application (whether individually or jointly) on a **WHITE** or **YELLOW** Application Form or by giving **electronic application instructions** to HKSCC or to the designated White Form eIPO Service Provider through the **White Form eIPO** service; or

- both apply (whether individually or jointly) on one **WHITE** Application Form and one **YELLOW** Application Form or on one **WHITE** or **YELLOW** Application Form and give **electronic application instructions** to HKSCC or to the designated White Form eIPO Service Provider through the **White Form eIPO** service; or

- apply on one **WHITE** or **YELLOW** Application Form (whether individually or jointly) or by giving **electronic application instructions** to HKSCC or to the designated White Form eIPO Service Provider through the **White Form eIPO** service for more than 50% of the Hong Kong Offer Shares initially being offered for sale under the Hong Kong Public Offering as more particularly described in the section headed "Structure of the Global Offering — The Hong Kong Public Offering" in this prospectus; or

- have indicated an interest for or have been or will be placed International Offer Shares under the International Offering.

All of your applications will also be rejected as multiple applications if more than one application is made for **your benefit** (including the part of an application made by HKSCC Nominees acting on **electronic application instructions**). If an application is made by an unlisted company and:

- the principal business of that company is dealing in securities; and

- you exercise statutory control over that company,

then the application will be treated as being made for your benefit.

"Unlisted company" means a company with no equity securities listed on the Stock Exchange.

"Statutory control" means you:

- control the composition of the board of directors of that Company; or

- control more than one-half of the voting power of that Company; or

- hold more than one-half of the issued share capital of that Company (not counting any part of it which carries no right to participate beyond a specified amount in a distribution of either profits or capital).

**11 CIRCUMSTANCES IN WHICH YOU WILL NOT BE ALLOTTED HONG KONG OFFER SHARES**

Full details of the circumstances in which you will not be allotted Hong Kong Offer Shares are set out in the notes attached to the Application Forms (whether you are making your application by an Application Form, through the **White Form eIPO** service or electronically instructing HKSCC to cause HKSCC Nominees to apply on your behalf), and you should read them carefully. You should note in particular the following situations in which Hong Kong Offer Shares will not be allotted to you:

(a) **If your application is revoked:**

By completing and submitting an Application Form or submitting an **electronic application instruction** to HKSCC or the designated White Form eIPO Service Provider, you agree that your application or the application made by HKSCC Nominees or the White Form eIPO Service Provider on your behalf cannot be revoked on or before Wednesday, 26 May 2010. This agreement will take effect as a collateral contract with us, and will become binding when you lodge your application or submit your **electronic application instructions** to HKSCC or to the White Form eIPO Service Provider. This collateral contract will be in consideration of our Company agreeing that we will not offer any Hong Kong Offer Shares to any person on or before Sunday, 13 June 2010 except by means of one of the procedures referred to in this prospectus.

You may only revoke your application or the application made on your behalf by HKSCC Nominees or the White Form eIPO Service Provider on or before Wednesday, 26 May 2010 if a person responsible for this prospectus under section 40 of the Companies Ordinance gives a public notice under that section which excludes or limits the responsibility of that person for this prospectus.

If any supplement to this prospectus is issued, applicant(s) who have already submitted an application may or may not (depending on the information contained in the supplement) be notified that they can withdraw their applications. If applicant(s) have not been so notified, or if applicant(s) have been notified but have not withdrawn their applications in accordance with the procedure to be notified, all applications that have been submitted remain valid and may be accepted. Subject to the above, an application once made is irrevocable and applicants shall be deemed to have applied on the basis of this prospectus as supplemented.

If your application or the application made on your behalf by HKSCC Nominees or the White Form eIPO Service Provider has been accepted, it cannot be revoked. For this purpose, acceptance of applications which are not rejected will be constituted by notification in the press of the results of allocation, and where such basis of allocation is subject to certain conditions or provides for allocation by ballot, such acceptance will be subject to the satisfaction of such conditions or results of the ballot respectively.

(b) **Full discretion of our Company, the Sole Global Coordinator or the designated White Form eIPO Service Provider or our or their respective agents to reject or accept:**

We, the Sole Global Coordinator or the designated White Form eIPO Service Provider or our or their respective agents have full discretion to reject or accept any application, or to accept only part of any application. No reasons have to be given for any rejection or acceptance.

(c) **If the allotment of Hong Kong Offer Shares is void:**

The allotment of Hong Kong Offer Shares to you or to HKSCC Nominees (if you give **electronic application instruction** to HKSCC or apply by a **YELLOW** Application Form) will be void if the Listing Committee of the Stock Exchange does not grant permission to list the Hong Kong Offer Shares either:

- within three weeks from the closing of the application lists; or
- within a longer period of up to six weeks if the Listing Committee of the Stock Exchange notifies us of that longer period within three weeks of the closing date of the application lists.

(d) **You will not receive any allotment if:**

- you make multiple applications or you are suspected to have made multiple applications;

- you or the person whose benefit you apply for have taken up or indicated an interest or applied for or received or have been or will be placed or allocated (including conditionally and/or provisionally) International Offer Shares in the International Offering. By filling in any of the Application Forms or submitting **electronic application instructions**, you agree not to apply for or indicate an interest for International Offer Shares in the International Offering. Reasonable steps will be taken to identify and reject applications in the Hong Kong Public Offering from investors who have received International Offer Shares in the International Offering, and to identify and reject indications of interest in the International Offering from investors who have received Hong Kong Offer Shares in the Hong Kong Public Offering;

- your **electronic application instructions** through the **White Form eIPO** service are not completed in accordance with the instructions, terms and conditions set out in the designated website at **www.eipo.com.hk**;

- your payment is not made correctly or you pay by cheque or banker's cashier order and the cheque or banker's cashier order is dishonoured upon its first presentation;

- your Application Form is not completed in accordance with the instructions as stated in the Application Form (if you apply by an Application Form);

- the Underwriting Agreements do not become unconditional; or

- the Underwriting Agreements are terminated in accordance with their respective terms.

You should also note that you may apply for Hong Kong Offer Shares under the Hong Kong Public Offering or indicate an interest for International Offer Shares under the International Offering, but may not do both.

### 12 HOW MUCH ARE THE HONG KONG OFFER SHARES

The maximum offer price is HK$3.38 per Hong Kong Offer Share. You must also pay brokerage of 1%, SFC transaction levy of 0.004% and Stock Exchange trading fee of 0.005%. This means that for every board lot of 1,000 Hong Kong Offer Shares, you will pay HK$3,414.11. The Application Forms have tables showing the exact amount payable for the numbers of Hong Kong Offer Shares that may be applied for. You must pay the maximum offer price and related brokerage, SFC transaction levy and the Stock Exchange trading fee in full when you apply for the Hong Kong Offer Shares.

You must pay the amount payable upon application for the Hong Kong Offer Shares by a cheque or a banker's cashier order in accordance with the terms set out in the Application Form or this prospectus.

If your application is successful, brokerage is paid to participants of the Stock Exchange or the Stock Exchange. The SFC transaction levy and Stock Exchange trading fee are paid to the Stock Exchange (and in the case of the SFC transaction levy, collected by the Stock Exchange on behalf of the SFC).

## 13 RESULTS OF ALLOCATIONS

Our Company expects to publish the announcement on the level of applications in the Hong Kong Public Offering, the level of indications of interest in the International Offering, the basis of allotment of the Hong Kong Offer Shares and the Offer Price on the website of the Company at **www.youyuan.com.hk** and the website of the Stock Exchange at **www.hkexnews.com.hk** on Wednesday, 26 May 2010. Results of allocations in the Hong Kong Public Offering, including the Hong Kong Identity Card numbers, passport numbers or Hong Kong business registration numbers of successful applicants (where supplied) and the number of Hong Kong Offer Shares successfully applied for under **WHITE** Application Forms, or **YELLOW** Application Forms or by giving **electronic application instructions** to HKSCC via CCASS to the designated White Form eIPO Service Provider through the **White Form eIPO** service (**www.eipo.com.hk**) will be made available at the times and dates and in the manner specified below:

- results of allocations in the Hong Kong Public Offering can be found in our announcement to be posted on the website of the Stock Exchange at **www.hkexnews.com.hk** and our Company's website at **www.youyuan.com.hk** no later than 9:00 a.m. on Wednesday, 26 May 2010;

- results of allocations in the Hong Kong Public Offering will be available from the Hong Kong Public Offering allocation results telephone enquiry line. Applicants may find out whether or not their applications have been successful and the number of Hong Kong Offer Shares allocated to them, if any, by calling **2862 8669** between 9:00 a.m. and 10:00 p.m. from Wednesday, 26 May 2010 to Saturday, 29 May 2010;

- results of allocations in the Hong Kong Public Offering will be available from our designated results of allocations website at **www.iporesults.com.hk** on a 24-hour basis from 8:00 a.m. on Wednesday, 26 May 2010 to 12:00 midnight on Tuesday, 1 June 2010. The user will be required to key in the Hong Kong identity card/passport/Hong Kong business registration number provided in his/her/its application to search for his/her/its own allocation result;

- special allocation results booklets setting out the results of allocations will be available for inspection during the opening hours of individual branches and sub-branches from Wednesday, 26 May 2010 to Friday, 28 May 2010 at all the receiving bank branches and sub-branches at the addresses set out in "How to Apply for Hong Kong Offer Shares — Where to Collect the Application Forms" in this section.

If you apply by giving **electronic application instructions** to HKSCC, HKSCC Nominees will not be treated as an applicant for the purposes of allocating Hong Kong Offer Shares. Instead, each CCASS Participant who gives **electronic application instructions** or each person for whose benefit each such instruction is given will be treated as an applicant.

## 14 DESPATCH/COLLECTION OF SHARE CERTIFICATES/e-REFUND PAYMENT INSTRUCTIONS /REFUND CHEQUES

If an application is rejected, not accepted or accepted in part only, or if the Offer Price as finally determined is less than the maximum offer price per Offer Share (excluding brokerage, SFC transaction levy and Stock Exchange trading fee thereon) initially paid on application, or if the conditions of the Global Offering are not fulfilled in accordance with the section headed "Structure of the Global Offering — Conditions" in this prospectus or if any application is revoked or any allotment pursuant thereto has become void, the application monies, or the appropriate portion thereof, together with the related brokerage, SFC transaction levy and Stock Exchange trading fee, will be refunded, without interest. All such interest accrued prior to the date of despatch of refund cheques or e-Refund payment instructions will be retained for our benefit. It is intended that special efforts will be made to avoid any undue delay in refunding application monies where appropriate.

No temporary document of title will be issued in respect of the Hong Kong Offer Shares. No receipt will be issued for sums paid on application. Subject as mentioned below, in due course, there will be sent to you (or, in the case of joint applicants, to the first-named applicant) by ordinary post, at your own risk, to the address specified on the application:

(a) share certificate(s) for all the Hong Kong Offer Shares applied for, if the application is wholly successful; or (ii) share certificate(s) for the number of Hong Kong Offer Shares successfully applied for, if the application is partially successful (except for wholly successful and partially successful applicants on **YELLOW** Application Forms or electronic instructions to HKSCC whose share certificates will be deposited into CCASS as described below); and/or

(b) refund cheque(s), for applicants on **WHITE** or **YELLOW** Application Forms, crossed "Account Payee Only" in favour of the applicant (or, in the case of joint applicants, the first-named applicant) for (i) the surplus application monies for the Hong Kong Offer Shares unsuccessfully applied for, if the application is partially unsuccessful; or (ii) all the application monies, if the application is wholly unsuccessful; and/or (iii) the difference between the Offer Price and the initial price per Offer Share paid on application in the event that the Offer Price is less than the initial price per Offer Share paid on application, in each case including related brokerage at the rate of 1%, SFC transaction levy of 0.004% and Stock Exchange trading fee of 0.005% attributable to such refund/surplus monies, but without interest.

Part of your Hong Kong Identity Card number/passport number, or, if you are joint applicants, part of the Hong Kong Identity Card number/passport number of the first-named applicant, provided by you may be printed on your refund cheque, if any. Such data would also be transferred to a third party for refund purposes. Your banker may require verification of your Hong Kong Identity Card number/passport number before encashment of your refund cheque. Inaccurate completion of your Hong Kong Identity Card number/passport number may lead to delay in encashment of or may invalidate your refund cheque.

Subject as mentioned below, refund cheques for surplus application monies (if any) in respect of wholly or partially unsuccessful applications and share certificates for wholly or partially successful applicants under **WHITE** Application Forms are expected to be posted on or before Wednesday, 26 May 2010. Our Company reserves the right to retain any share certificates and any surplus application monies pending clearance of cheque(s).

In a contingency situation involving a substantial over-application, at the discretion of our Company and the Sole Global Coordinator, cheques for applications made on Application Forms for certain small denominations of Hong Kong Offer Shares (apart from successful applications) may not be cleared.

**If you apply using a WHITE Application Form:**

If you have applied for 1,000,000 Hong Kong Offer Shares or more and you have elected on your **WHITE** Application Form to collect your refund cheque(s) (where applicable) and/or share certificate(s) (where applicable) in person, you may collect your refund cheque(s) (where applicable) and/or share certificate(s) (where applicable) from our Hong Kong Share Registrar, Computershare Hong Kong Investor Services Limited at Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, from 9:00 a.m. to 1:00 p.m. on Wednesday, 26 May 2010. If you are an individual, you must not authorise any other person to make the collection on your behalf. If you are a corporate applicant, you must attend by your authorised representative bearing a letter of authorisation from your corporation stamped with your company chop. Both individuals and authorised representatives (if applicable) must produce, at the time of collection, evidence of identity acceptable to our Hong Kong Share Registrar, Computershare Hong Kong Investor Services Limited at Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong. If you do not collect your refund cheque (s) and share certificate(s) within the time period specified for collection, they will be despatched thereafter to you by ordinary post to the address as specified in your Application Form at your own risk.

If you have applied for 1,000,000 Hong Kong Offer Shares or above and have not indicated on your Application Forms that you will collect your share certificate(s) and/or refund cheque(s) (if any) in person, or you have applied for less than 1,000,000 Hong Kong Offer Shares or if your application is rejected, not accepted or accepted in part only, or the Offer Price as finally determined is set below the price initially paid on your application, or if the conditions of the Hong Kong Public Offering are not fulfilled in accordance with the section headed "Structure of the Global Offering — Conditions" in this prospectus, or if your application is revoked or any allotment pursuant thereto has become void, your share certificate(s) (where applicable) and/or refund cheque(s) (where applicable) in respect of the application monies or the appropriate parties thereof, together with the related brokerage, Stock Exchange trading fee and SFC transaction levy, if any, (without interest) will be sent to the address on your Application Form on Wednesday, 26 May 2010 by ordinary post and at your own risk.

**If you apply using a YELLOW Application Form or give an electronic application instruction to HKSCC via CCASS:**

If you apply for Hong Kong Offer Shares using a **YELLOW** Application Form and your application is wholly or partially successful, your share certificates will be issued in the name of HKSCC Nominees and deposited into CCASS for the credit of the stock account of the CCASS Participant or your CCASS Investor Participant stock account at the close of business on Wednesday, 26 May 2010, or in the event of a contingency, on any other date as shall be determined by HKSCC or HKSCC Nominees.

We expect to publish the application results of CCASS Participants (and where the CCASS Participant is a CCASS Clearing/Custodian Participant, we will include information relating to the relevant beneficial owner, if supplied), your Hong Kong identity card/passport number or other identification code (Hong Kong business registration number for corporations) and the basis of allotment of the Hong Kong Public Offering on the website of the Company at **www.youyuan.com.hk** and the website of the Stock Exchange at **www.hkex.com.hk** on Wednesday, 26 May 2010. You should check the announcement published by us and report any discrepancies to HKSCC before 5:00 p.m. on Wednesday, 26 May 2010 or such other date as shall be determined by HKSCC or HKSCC Nominees.

If you have instructed your CCASS Clearing/Custodian Participant to give **electronic application instructions** on your behalf, you can also check the number of Hong Kong Offer Shares allotted to you and the amount of refund monies (if any) payable to you with that CCASS Clearing/Custodian Participant.

If you have applied as a CCASS Investor Participant, you can also check the number of Hong Kong Offer Shares allotted to you and (if you give an electronic application instruction to HKSCC via CCASS) the amount of refund monies (if any) payable to you via the CCASS Phone System and the CCASS Internet System (under the procedures contained in HKSCC's "An Operating Guide for Investor Participants" in effect from time to time) on Wednesday, 26 May 2010. Immediately following the credit of the Hong Kong Offer Shares to your CCASS Investor Participant stock account and the credit of refund monies (if any) to your bank account, HKSCC will also make available to you an activity statement showing the number of Hong Kong Offer Shares credited to your CCASS Investor Participant stock account and the amount of refund monies (if any) credited to your designated bank account.

Refund of your application monies (if any) in respect of wholly and partially unsuccessful applications and/or the difference between the Offer Price and the initial price per Hong Kong Offer Share paid on application, in each case including the related brokerage of 1%, SFC transaction levy of 0.004% and Stock Exchange trading fee of 0.005%, will be credited to your designated bank account or the designated bank account of your CCASS Clearing/Custodian Participant on Wednesday, 26 May 2010. No interest will be paid thereon.

If you apply for 1,000,000 Hong Kong Offer Shares or more and you have elected on your **YELLOW** Application Form to collect your refund cheque (where applicable) in person, please follow the same instructions as those for **WHITE** Application Form applicants as described above.

If you have applied for 1,000,000 Hong Kong Offer Shares or above and have not indicated on your Application Forms that you will collect your refund cheque(s) (if any) in person, or you have applied for less than 1,000,000 Hong Kong Offer Shares or if your application is rejected, not accepted or accepted in part only or the Offer Price as finally determined is set below the price initially paid on your application, or if the conditions of the Hong Kong Public Offering are not fulfilled in accordance with the section headed "Structure of the Global Offering — Conditions" in this prospectus, or if your application is revoked or any allotment pursuant thereto has become void, your refund cheque(s) (where applicable) in respect of the application monies or the appropriate portion thereof, together with the related brokerage, Stock Exchange trading fee and SFC transaction levy, if any, (without interest) will be sent to the address on your Application Form on Wednesday, 26 May 2010 by ordinary post and at your own risk.

**If you apply through the White Form eIPO service**

If you apply for 1,000,000 Hong Kong Offer Shares or more through the **White Form eIPO** service by submitting an electronic application to the designated White Form eIPO Service Provider through the designated website at **www.eipo.com.hk** and your application is wholly or partially successful, you may collect your Share certificate(s) (where applicable) in person from Computershare Hong Kong Investor Services Limited at Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, from 9:00 a.m. to 1:00 p.m. on Wednesday, 26 May 2010, or such other date as notified by our Company in the newspapers as the date of despatch/collection of Share certificates/e-Refund payment instructions/refund cheques.

If you do not collect your Share certificate(s) personally within the time specified for collection, they will be sent to the address specified in your application instructions to the designated White Form eIPO Service Provider promptly thereafter by ordinary post and at your own risk.

If you apply for less than 1,000,000 Hong Kong Offer Shares, your Share certificate(s) (where applicable) will be sent to the address specified in your application instructions to the designated White Form eIPO Service Provider through the designated website at **www.eipo.com.hk** on Wednesday, 26 May 2010 by ordinary post and at your own risk.

If you paid the application monies from a single bank account, e-Refund payment instructions (if any) will be despatched to your application payment bank account on Wednesday, 26 May 2010; if you used multi-bank accounts to pay the application monies, refund cheque (if any) will be despatched to you on Wednesday, 26 May 2010.

Please also note the additional information relating to refund of application monies overpaid, application money underpaid or applications rejected by the designated White Form eIPO Service Provider set out in "How to Apply for Hong Kong Offer Shares — How to Apply through the White Form eIPO Service — Additional information" in this section.

## 15 COMMENCEMENT OF DEALINGS IN THE SHARES

Dealings in the Shares on the Stock Exchange are expected to commence on Thursday, 27 May 2010.

The Shares will be traded in board lots of 1,000 each. The stock code of the Shares is 2268.

## 16 SHARES WILL BE ELIGIBLE FOR ADMISSION INTO CCASS

Subject to the granting of listing of, and permission to deal in, the Shares on the Stock Exchange and our Company's compliance with the stock admission requirements of HKSCC, the Shares will be accepted as eligible securities by HKSCC for deposit, clearance and settlement in CCASS with effect from the date of commencement of dealings in the Shares on the Stock Exchange or any other date as HKSCC chooses. Settlement of transactions between participants of the Stock Exchange is required to take place in CCASS on the second Business Day after any trading day. All activities under CCASS are subject to the General Rules of CCASS and CCASS Operational Procedures in effect from time to time. Investors should seek the advice of their stockbroker or other professional adviser for details of the settlement arrangements as such arrangements will affect their rights and interests. All necessary arrangements have been made for the Shares to be admitted into CCASS.

Deloitte.
德勤

德勤・關黃陳方會計師行
香港金鐘道88號
太古廣場一座35樓

Deloitte Touche Tohmatsu
35/F One Pacific Place
88 Queensway
Hong Kong

14 May 2010

The Directors
Youyuan International Holdings Limited
The Hongkong and Shanghai Banking Corporation Limited

Dear Sirs,

We set out below our report on the financial information (the "Financial Information") relating to Youyuan International Holdings Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group") for the three years ended 31 December 2009 (the "Track Record Period") for inclusion in the prospectus of the Company dated 14 May 2010 (the "Prospectus") in connection with the initial listing of the shares of the Company on The Stock Exchange of Hong Kong Limited (the "Stock Exchange").

The Company was incorporated in the Cayman Islands as an exempted company with limited liability under the Companies Law (2007 Revision) Chapter 22 of the Cayman Islands on 12 October 2009. Pursuant to a group reorganisation, as more fully explained in the section headed "Statutory and General Information" in Appendix VI to the Prospectus (the "Group Reorganisation"), the Company became the holding company of the entities now comprising the Group on 14 January 2010.

As at the date of this report, the Company has the following indirectly held, unless otherwise stated, subsidiaries:

| Name of subsidiary | Place and date of incorporation/ establishment | Issued and fully paid-up share capital/ registered capital | Equity interest attributable to the Group as at 31 December 2007 | 2008 | 2009 | Date of this report | Principal activities |
|---|---|---|---|---|---|---|---|
| | | | % | % | % | % | |
| Xi Yuan Paper Limited ("Xi Yuan BVI") | British Virgin Islands (the "BVI") 10 July 2009 | US$1 | n/a | n/a | 100.00 (directly) | 100.00 (directly) | Investment holding |
| Sunwell Trading (HK) Company Limited ("Sunwell") | Hong Kong 13 September 2005 | HK$10,000,000[1] | 100.00 | 100.00 | 100.00 | 100.00 | Investment holding |

| Name of subsidiary | Place and date of incorporation/ establishment | Issued and fully paid-up share capital/ registered capital | Equity interest attributable to the Group as at 31 December 2007 | 2008 | 2009 | Date of this report | Principal activities |
|---|---|---|---|---|---|---|---|
| | | | % | % | % | % | |
| 泉州華祥紙業有限公司 Quanzhou Huaxiang Paper Industry Co., Ltd. ("Huaxiang")[2] | The People's Republic of China (the "PRC") [3] 9 March 2006 | RMB60,000,000 | 95.00 | 95.00 | 100.00 | 100.00 | Manufacture of high grade paper |
| 福建希源紙業有限公司 Fujian Xiyuan Paper Co., Ltd. ("Xiyuan") [2] | The PRC[3] 18 January 2006 | HK$68,980,000 | 96.50 | 96.50 | 100.00 | 100.00 | Manufacture of high grade paper |
| 福建省晉江優蘭發紙業有限公司 Youlanfa Paper Co., Ltd. Fujian ("Youlanfa") [2] | The PRC[3] 11 November 1994 | RMB128,880,000 | 94.92 | 94.92 | 100.00 | 100.00 | Manufacture of high grade paper |

1 Sunwell was incorporated on 13 September 2005 with issued and fully paid share capital of HK$10,000. On 28 August 2009, Sunwell issued and allotted 9,990,000 shares at par value of HK$1 to Xi Yuan BVI at a consideration of HK$1 per share. Upon such allotment, the issued and fully paid-up share capital of Sunwell increased to HK$10,000,000.

2 These entities are subsidiaries of Xi Yuan BVI.

3 These entities are foreign-invested enterprises established in the PRC.

The financial year end date of all the entities now comprising the Group is 31 December.

No statutory financial statements have been prepared for the Company and Xi Yuan BVI since their respective dates of incorporation as there are no statutory requirements in the Cayman Islands and the BVI. For the purpose of this report, we have, however, reviewed all the relevant transactions of the Company and Xi Yuan BVI since their respective dates of incorporation and carried out such procedures as we considered necessary for inclusion of their financial statements in the Financial Information.

The statutory financial statements of Sunwell were prepared in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA"). The statutory financial statements of Huaxiang, Xiyuan and Youlanfa were prepared in accordance with relevant accounting principles and financial regulations in the PRC. They were audited by the following certified public accountants registered in Hong Kong and the PRC, as appropriate:

| Name of subsidiary | Financial year | Name of auditor |
|---|---|---|
| Sunwell | Three years ended 31 December 2007, 2008 and 2009 | LKKC C.P.A. Limited |
| Huaxiang | Three years ended 31 December 2007, 2008 and 2009 | 晉江德誠有限責任會計師事務所 Jinjiang Decheng Limited Liabilities Certified Public Accountants |
| Xiyuan | Three years ended 31 December 2007, 2008 and 2009 | 晉江德誠有限責任會計師事務所 Jinjiang Decheng Limited Liabilities Certified Public Accountants |
| Youlanfa | Three years ended 31 December 2007, 2008 and 2009 | 晉江德誠有限責任會計師事務所 Jinjiang Decheng Limited Liabilities Certified Public Accountants |

For the purpose of this report, the directors of the Company have prepared the consolidated financial statements of Xi Yuan BVI and its subsidiaries for the Track Record Period (the "Underlying Financial Statements") in accordance with International Financial Reporting Standards ("IFRSs"). We have carried out an independent audit on the Underlying Financial Statements in accordance with Hong Kong Standards on Auditing issued by the HKICPA.

We have examined the Underlying Financial Statements in accordance with the Auditing Guideline 3.340 "Prospectuses and the Reporting Accountant" as recommended by the HKICPA.

The Financial Information of the Group for the Track Record Period as set out in this report has been prepared from the Underlying Financial Statements, on the basis set out in Note 2 to the Financial Information. No adjustments are considered necessary to the Underlying Financial Statements in preparing our report on the Financial Information.

The Underlying Financial Statements are the responsibility of the directors of Xi Yuan BVI who approved their issue. The directors of the Company are responsible for the contents of the Prospectus in which this report is included. It is our responsibility to compile the Financial Information set out in this report from the Underlying Financial Statements, to form an opinion on the Financial Information and to report our opinion to you.

In our opinion, on the basis of presentation set out in Note 2 to the Financial Information, the Financial Information gives, for the purpose of this report, a true and fair view of the state of affairs of the Group as at 31 December 2007, 2008 and 2009 and of the combined results and combined cash flows of the Group for the Track Record Period.

## I. FINANCIAL INFORMATION

### COMBINED STATEMENTS OF COMPREHENSIVE INCOME

| | Notes | Year ended 31 December 2007 | 2008 | 2009 |
|---|---|---|---|---|
| | | RMB'000 | RMB'000 | RMB'000 |
| Revenue | 8 | 267,586 | 562,019 | 724,793 |
| Cost of sales | | (187,099) | (373,918) | (484,141) |
| Gross profit | | 80,487 | 188,101 | 240,652 |
| Selling and distribution expenses | | (2,075) | (2,994) | (4,066) |
| Administrative expenses | | (12,645) | (25,364) | (37,018) |
| Other income and other gains and losses | 10 | 5,341 | 5,962 | 2,421 |
| Finance costs | 11 | (13,613) | (20,021) | (18,219) |
| Profit before tax | 12 | 57,495 | 145,684 | 183,770 |
| Taxation | 13 | (15,223) | (13,041) | (13,093) |
| Profit and total comprehensive income for the year | | 42,272 | 132,643 | 170,677 |
| Profit and total comprehensive income for the year attributable to: | | | | |
| Owners of the Company | | 40,282 | 126,396 | 165,941 |
| Minority interests | | 1,990 | 6,247 | 4,736 |
| | | 42,272 | 132,643 | 170,677 |
| Earnings per share - Basic (RMB) | 15 | 0.05 | 0.17 | 0.22 |

## STATEMENTS OF FINANCIAL POSITION

| | | The Group | | | The Company |
|---|---|---|---|---|---|
| | | At 31 December | | | At 31 December |
| | Notes | 2007 | 2008 | 2009 | 2009 |
| | | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| NON-CURRENT ASSETS | | | | | |
| Property, plant and equipment | 16 | 401,261 | 533,349 | 621,646 | — |
| Prepaid lease payments | 17 | 115,759 | 113,226 | 259,311 | — |
| Investment properties | 18 | 22,924 | 22,011 | 21,098 | — |
| Deposits paid for acquisition of property, plant and equipment | | 86,850 | 31,920 | 42,957 | — |
| | | 626,794 | 700,506 | 945,012 | — |
| CURRENT ASSETS | | | | | |
| Inventories | 19 | 20,778 | 27,503 | 110,282 | — |
| Trade and other receivables and prepayments | 20 | 62,083 | 129,204 | 154,580 | — |
| Prepaid lease payments | 17 | 2,158 | 2,534 | 5,770 | — |
| Amount due from ultimate controlling shareholder | 26 | 12,090 | — | — | — |
| Amounts due from related parties | 26 | — | 562 | — | — |
| Pledged bank deposits | 21 | 2,592 | 52,826 | 2,860 | — |
| Bank balances and cash | 21 | 5,361 | 5,842 | 86,825 | — |
| | | 105,062 | 218,471 | 360,317 | — |
| CURRENT LIABILITIES | | | | | |
| Trade and other payables | 22 | 59,282 | 174,246 | 118,326 | — |
| Amounts due to related parties | 26 | 123,306 | 44,679 | 8,584 | — |
| Amount due to ultimate controlling shareholder | 26 | 88,626 | 91,917 | 1,649 | — |
| Amount due to immediate holding company | 26 | — | — | 95,605 | — |
| Income tax payables | | 5,128 | 2,978 | 3,318 | — |
| Bank borrowings | 23 | 294,000 | 311,000 | 182,820 | — |
| | | 570,342 | 624,820 | 410,302 | — |
| NET CURRENT LIABILITIES | | (465,280) | (406,349) | (49,985) | — |
| Total assets less current liabilities | | 161,514 | 294,157 | 895,027 | — |
| NON-CURRENT LIABILITIES | | | | | |
| Bank borrowings | 23 | — | — | 340,180 | — |
| | | 161,514 | 294,157 | 554,847 | — |
| CAPITAL AND RESERVES | | | | | |
| Share capital/paid-in capital | 24 | 65,390 | 10 | — | — |
| Reserves | | 83,020 | 274,796 | 554,847 | — |
| Equity attributable to owners of the Company | | 148,410 | 274,806 | 554,847 | — |
| Minority interests | | 13,104 | 19,351 | — | — |
| TOTAL EQUITY | | 161,514 | 294,157 | 554,847 | — |

## COMBINED STATEMENTS OF CHANGES IN EQUITY

| | Share capital/ paid-in capital | Capital reserve | Special reserve | Statutory surplus reserve | Accumulated profits | Attributable to owners of the Company | Minority interests | Total |
|---|---|---|---|---|---|---|---|---|
| | RMB'000 | RMB'000 | RMB'000 (Note 1) | RMB'000 (Note 2) | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| At 1 January 2007 | 65,390 | — | — | 4,362 | 38,376 | 108,128 | 8,864 | 116,992 |
| Profit and total comprehensive income for the year | — | — | — | — | 40,282 | 40,282 | 1,990 | 42,272 |
| Contributions from minority interests | — | — | — | — | — | — | 2,250 | 2,250 |
| Appropriation | — | — | — | 3,972 | (3,972) | — | — | — |
| At 31 December 2007 and 1 January 2008 | 65,390 | — | — | 8,334 | 74,686 | 148,410 | 13,104 | 161,514 |
| Arising on Group Reorganisation | (65,380) | — | 65,380 | — | — | — | — | — |
| Profit and total comprehensive income for the year | — | — | — | — | 126,396 | 126,396 | 6,247 | 132,643 |
| Appropriation | — | — | — | 12,715 | (12,715) | — | — | — |
| At 31 December 2008 and 1 January 2009 | 10 | — | 65,380 | 21,049 | 188,367 | 274,806 | 19,351 | 294,157 |
| Arising on Group Reorganisation | (10) | — | 10 | — | — | — | — | — |
| Profit and total comprehensive income for the year | — | — | — | — | 165,941 | 165,941 | 4,736 | 170,677 |
| Deemed contribution from a shareholder (Note 3) | — | 111,623 | — | — | — | 111,623 | — | 111,623 |
| Acquisition of additional interests in Huaxiang, Xiyuan and Youlanfa | — | — | 2,477 | — | — | 2,477 | (24,087) | (21,610) |
| Appropriation | — | — | — | 17,782 | (17,782) | — | — | — |
| At 31 December 2009 | — | 111,623 | 67,867 | 38,831 | 336,526 | 554,847 | — | 554,847 |

*Note 1:* Special reserve comprises of:

(i) an amount of RMB65,380,000, being the difference between the consideration of US$1.00 paid and paid-in capital of Youlanfa resulted from the acquisition of 94.92% equity interest of Youlanfa from Uniland Box Products Manufacturing ("Uniland") by Sunwell as part of the Group Reorganisation set out in Note 2 to the Financial Information;

(ii) an amount of RMB10,000, being the difference between the consideration of HK$9,990,000 paid and the share capital of Sunwell resulted from the subscription of 99.9% equity interest of Sunwell by Xi Yuan BVI as part of the Group Reorganisation set out in Note 2 to the Financial Information; and

(iii) an amount of RMB2,477,000, being the difference between the carrying amount of the share of net assets acquired and the consideration of RMB21,610,000 resulted from the acquisitions of additional interests in Huaxiang, Xiyuan and Youlanfa.

*Note 2:* According to the relevant laws in the PRC, Huaxiang, Xiyuan and Youlanfa are required to transfer at least 10% of their net profit after taxation, as determined under the PRC accounting regulations, to a statutory surplus reserve until the reserve balance reaches 50% of their registered capital. The transfer to this reserve must be made before the distribution of a dividend to equity owners. The statutory surplus reserve can be used to offset the previous years' losses, if any. The statutory surplus reserve may also be used to increase capital or to meet unexpected or future losses. The statutory surplus reserve is non-distributable other than upon liquidation.

*Note 3:* Pursuant to the agreement dated 30 September 2009, Mr Ke Wen Tuo ("Mr Ke"), the ultimate controlling shareholder of the Group, waived the amount due to him of RMB111,623,000. Such amount is recorded in capital reserve as deemed contribution from a shareholder (see note 27).

## COMBINED STATEMENTS OF CASH FLOWS

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| OPERATING ACTIVITIES | | | |
| Profit before tax | 57,495 | 145,684 | 183,770 |
| Adjustments for: | | | |
| Interest income | (360) | (911) | (1,006) |
| Finance costs | 13,613 | 20,021 | 18,219 |
| (Gain) loss on disposal of property, plant and equipment | — | (31) | 123 |
| Depreciation of property, plant and equipment | 10,349 | 17,027 | 22,895 |
| Depreciation of investment properties | 913 | 913 | 913 |
| Release of prepaid lease payments | 879 | 2,157 | 3,695 |
| Allowance for obsolete inventories | — | — | 179 |
| Operating cash flows before movements in working capital | 82,889 | 184,860 | 228,788 |
| Increase in inventories | (5,939) | (6,725) | (82,958) |
| Increase in trade and other receivables and prepayments | (42,522) | (67,121) | (25,376) |
| (Increase) decrease in amount due from a related party | — | (562) | 562 |
| Increase in amounts due to related parties | — | — | 8,584 |
| Increase (decrease) in trade and other payables | 13,473 | 109,420 | (53,288) |
| Cash generated from operations | 47,901 | 219,872 | 76,312 |
| Income taxes paid | (13,051) | (15,191) | (12,753) |
| NET CASH FROM OPERATING ACTIVITIES | 34,850 | 204,681 | 63,559 |

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| INVESTING ACTIVITIES | | | |
| Payments for acquisition of property, plant and equipment | (257,823) | (85,364) | (120,550) |
| Payments for prepaid lease payments | (61,409) | — | (153,016) |
| Repayment from ultimate controlling shareholder | 93,110 | 12,090 | — |
| Repayments from related parties | 7,140 | — | — |
| Decrease (increase) in pledged bank deposits | 3,600 | (50,234) | 49,966 |
| Consideration paid for acquisition of additional interest in subsidiaries | — | — | (21,610) |
| Interest received | 360 | 911 | 1,006 |
| Proceeds from disposal of property, plant and equipment | — | 71 | 80 |
| NET CASH USED IN INVESTING ACTIVITIES | (215,022) | (122,526) | (244,124) |
| FINANCING ACTIVITIES | | | |
| New bank borrowings raised | 354,000 | 383,450 | 680,500 |
| Advance from ultimate controlling shareholder | 49,308 | 15,026 | 21,355 |
| Advance from immediate holding company | — | — | 95,605 |
| Contributions from minority interests | 2,250 | — | — |
| Repayments to related parties | — | (91,887) | (44,679) |
| Repayments of bank borrowings | (212,800) | (366,450) | (468,500) |
| Interest paid | (14,333) | (21,813) | (22,733) |
| NET CASH FROM (USED IN) FINANCING ACTIVITIES | 178,425 | (81,674) | 261,548 |
| NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS | (1,747) | 481 | 80,983 |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR | 7,108 | 5,361 | 5,842 |
| CASH AND CASH EQUIVALENTS AT END OF YEAR | 5,361 | 5,842 | 86,825 |

## NOTES TO THE FINANCIAL INFORMATION

### 1. GENERAL

The Company was incorporated as an exempted company with limited liability in the Cayman Islands under the Companies Law (2007 Revision) Chapter 22 of the Cayman Islands on 12 October 2009. Its immediate parent is Smart Port Holdings Limited ("Smart Port") (incorporated in the BVI) and its ultimate controlling shareholder is Mr Ke. The registered office of the Company is situated at Cricket Square, Hutchins Drive, PO Box 2681, Grand Cayman KY1-1111, Cayman Islands.

The principal activity of the Company is investment holding. The principal activities of the Group are the manufacture and sale of high grade tissue paper and copy paper in the PRC.

### 2. BASIS OF PRESENTATION OF FINANCIAL INFORMATION

Sunwell, the holding company of Huaxiang and Xiyuan, was incorporated on 13 September 2005 and was owned and controlled by Mr Ke, prior to the Group Reorganisation. Sunwell acquired the 94.92% equity interest in Youlanfa from Uniland, a company 100% owned and controlled by Mr Ke, and became the holding company of Youlanfa on 4 August 2008. Youlanfa, Huaxiang, Xiyuan and Sunwell were under common control of Mr Ke both before and after the transfer of interests in Youlanfa to Sunwell and that the control was not transitory.

Xi Yuan BVI was established on 10 July 2009 by Mr Ke. Xi Yuan BVI subscribed for 99.9% equity interest (comprised of 9,990,000 shares at par value of HK$1) in Sunwell and became the holding company of Sunwell on 24 August 2009, while the remaining 0.1% equity interest of Sunwell continued to be directly held by Mr Ke. Xi Yuan BVI and Sunwell were under the common control of Mr Ke both before and after the transfer of interests in Sunwell to Xi Yuan BVI and that the control was not transitory. On 2 October 2009, Mr Ke transferred his 0.1% equity interest (comprised of 10,000 shares at par value of HK$1) in Sunwell to Xi Yuan BVI at a consideration of HK$1 per share. Upon the completion of such transfer, Sunwell became a wholly-owned subsidiary of Xi Yuan BVI.

On 12 October 2009, Mr Ke set up the Company. Pursuant to the Group Reorganisation as set out in the section headed "Statutory and General Information" in Appendix VI to the Prospectus, the Company acquired the 100% equity interest in Xi Yuan BVI and became the holding company of Xi Yuan BVI on 14 January 2010. The Group resulting from the Group Reorganisation continued to be controlled by Mr Ke and therefore is regarded as a continuing entity.

Accordingly, the Financial Information of the Group has been prepared as if the Company had always been the holding company of Xi Yuan BVI. The combined statements of comprehensive income, combined statements of changes in equity and combined statements of cash flows of the Group for the Track Record Period have been prepared as if the current group structure had been in existence throughout the Track Record Period, or since the respective dates of incorporation/establishment of the relevant entities now comprising the Group where this is a shorter period. The combined statements of financial position of the Group as at 31 December 2007, 2008 and 2009 have been prepared to present the assets and liabilities of the entities now comprising the Group which were in existence at those dates.

The Financial Information is presented in Renminbi ("RMB"), the currency of the primary economic environment in which the Company and the majority of the group entities operate.

## 3. APPLICATION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS

For the purpose of preparing and presenting the Financial Information for the Track Record Period, the Group has consistently early adopted the relevant International Accounting Standards ("IASs"), International Financial Reporting Standards ("IFRSs"), amendments and the related Interpretations ("IFRICs"), which are effective for the financial year beginning on 1 January 2009 throughout the Track Record Period.

At the date of this report, the International Accounting Standards Board has issued the following new and revised standards, amendments and interpretations which are not yet effective:

| | |
|---|---|
| IFRSs (Amendments) | Amendment to IFRS 5 as part of Improvements to IFRSs May 2008[1] |
| IFRSs (Amendments) | Improvements to IFRSs April 2009[2] |
| IAS 24 (Amendment) | Related Party Disclosures - Revised Definition of Related Parties[3] |
| IAS 27 (Revised) | Consolidated and Separate Financial Statements[1] |
| IAS 32 (Amendment) | Classification of Rights Issues[4] |
| IAS 39 (Amendment) | Eligible Hedged Items[1] |
| IFRS 1 (Amendment) | Additional Exemptions for First-time Adopters[5] |
| IFRS 1 (Amendment) | Limited exemption from comparative IFRS 7 Disclosures for First-time Adopters[6] |
| IFRS 2 (Amendment) | Group Cash-settled Share-based Payment Transactions[5] |
| IFRS 3 (Revised) | Business Combinations[1] |
| IFRS 9 | Financial Instruments[7] |
| IFRIC-Int 14 (Amendment) | Prepayment of a Minimum Funding Requirement[3] |
| IFRIC-Int 17 | Distributions of Non-cash Assets to Owners[1] |
| IFRIC-Int 19 | Extinguishing Financial Liabilities with Equity Instruments[6] |

1 Effective for annual periods beginning on or after 1 July 2009

2 Amendments that are effective for annual periods beginning on or after 1 July 2009 and 1 January 2010, as appropriate

3 Effective for annual periods beginning on or after 1 January 2011

4 Effective for annual periods beginning on or after 1 February 2010

5 Effective for annual periods beginning on or after 1 January 2010

6 Effective for annual periods beginning on or after 1 July 2010

7 Effective for annual periods beginning on or after 1 January 2013

The Group has not early adopted these new and revised standards, amendments and interpretations in the preparation of the Financial Information. The application of IFRS 3 (Revised) may affect the Group's accounting for business combination for which the acquisition date is on or after 1 January 2010. IAS 27 (Revised) will affect the accounting treatment for changes in a parent's ownership interest in a subsidiary. The directors of the Company anticipate that the application of the other new and revised standards, amendments or interpretations will have no material impact on the combined financial statements of the Group.

## 4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Financial Information has been prepared on the historical cost basis and in accordance with the accounting policies set out below which conform to IFRSs.

In addition, the Financial Information includes applicable disclosures required by the Rules Governing the Listing of Securities on the Stock Exchange and by the Hong Kong Companies Ordinance.

### Basis of combination

The Financial Information incorporates the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of (other than business combinations involving entities under common control) during the Track Record Period are included in the combined statements of comprehensive income from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All significant intra-group transactions, balances, income and expenses are eliminated in full on combination.

Minority interests in the net assets of combined subsidiaries are presented separately from the Group's equity therein. Minority interests in the net assets consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

***Changes in the Group's ownership interests in existing subsidiaries***

Changes in the Group's ownership interest in a subsidiary are accounted for as equity transactions. The difference between the consideration paid and the carrying amounts of the minority interests is recognised directly in equity and attributed to owners of the Company.

**Merger accounting for business combination involving entities under common control**

The Financial Information incorporates the financial statement items of the combining entities or businesses in which the common control combination occurs as if they had been combined from the date when the combining entities or businesses first came under the control of the controlling party.

The net assets of the combining entities or businesses are combined using the existing book values from the controlling parties' perspective. No amount is recognised in respect of goodwill or excess of acquirer's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over cost at the time of common control combination, to the extent of the continuation of the controlling party's interest.

The combined statements of comprehensive income includes the results of each of the combining entities or businesses from the earliest date presented or since the date when the combining entities or businesses first came under common control, where this is a shorter period, regardless of the date of the common control combination.

**Revenue recognition**

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods sold in the normal course of business, net of discounts and sales related taxes.

Revenue from sales of goods are recognised when goods are delivered and title has been passed.

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

**Leasing**

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

***The Group as lessor***

Rental income from operating leases is recognised in profit or loss on a straight-line basis over the term of the relevant lease.

***The Group as lessee***

Rentals payable under operating leases are charged to profit or loss on a straight-line basis over the term of the relevant lease.

***Leasehold land and building***

The land and building elements of a lease of land and building are considered separately for the purpose of lease classification, unless the lease payments cannot be allocated reliably between the land and building elements, in which case, the entire lease is generally treated as a finance lease and accounted for as property, plant and equipment. To the extent the allocation of the lease payments can be made reliably, leasehold interests in land are accounted for as operating leases.

**Prepaid lease payments**

The up-front payments to acquire leasehold interest in land are accounted for as operating leases and are stated at cost and charged to profit or loss over the lease term on a straight-line basis.

**Government grants**

Unconditional discretionary government grants from local authorities are recognised in profit or loss as other income to match them with the related costs when there is reasonable assurance that the grants will be received.

**Borrowing costs**

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, are capitalised as part of the cost of those assets. Capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in profit or loss in the year in which they are incurred.

**Foreign currencies**

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in the respective functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchanges prevailing on the dates of the transactions. At the end of the reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the end of the reporting period. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are recognised in profit or loss in the period in which they arise.

**Property, plant and equipment**

Property, plant and equipment including buildings held for use in the production or supply of goods or services, or for administrative purposes (other than construction in progress) are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

Depreciation is provided to write off the cost of items of property, plant and equipment (other than construction in progress) over their estimated useful lives and after taking into account of their estimated residual value, using the straight-line method.

Construction in progress includes property, plant and equipment in the course of construction for production or for its own use purposes. Construction in progress is carried at cost less any recognised impairment loss. Construction in progress is classified to the appropriate category of property, plant and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in profit or loss in the period in which the item is derecognised.

**Investment properties**

Investment properties are properties held to earn rentals and/or for capital appreciation. On initial recognition, investment properties are measured at cost, including any directly attributable expenditure. Subsequent to initial recognition, investment properties are stated at cost less subsequent accumulated depreciation and any accumulated impairment losses. Depreciation is charged so as to write off the cost of investment properties, over their estimated useful lives and after taking into account of their estimated residual value, using the straight-line method.

An investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use or no future economic benefits are expected from its disposals. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss in the period in which the item is derecognised.

**Retirement benefit costs**

Payments to defined contribution retirement benefit plans or state-owned retirement benefit schemes are charged as an expense when employees have rendered services entitling them to the contributions.

**Taxation**

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the combined statements of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the combined statements of financial position and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset is realised, based on the tax rate (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. Deferred tax is recognised in profit or loss, except when it relates to items that are recognised in other comprehensive income or directly in equity, in which case the deferred tax is also recognised in other comprehensive income or directly in equity respectively.

**Impairment of tangible assets**

At the end of the reporting period, the Group reviews the carrying amounts of its tangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

**Inventories**

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the weighted average method.

**Financial Instruments**

Financial assets and financial liabilities are recognised in the combined statements of financial position when a group entity becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

***Financial assets***

The Group's financial assets are classified into loans and receivables.

***Effective interest method***

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Interest income is recognised on an effective interest basis.

*Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables (including trade and other receivables, amount due from ultimate controlling shareholder, amounts due from related parties, pledged bank deposits and bank balances and cash) are carried at amortised cost using the effective interest method, less any identified impairment losses (see accounting policy on impairment loss on financial assets below).

*Impairment of financial assets*

Financial assets are assessed for indicators of impairment at the end of the reporting period. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial assets have been affected.

Objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation.

For certain categories of financial asset, such as trade receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period, observable changes in national or local economic conditions that correlate with default on receivables.

For financial assets carried at amortised cost, an impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited to profit or loss.

For financial assets measured at amortised cost, if, in a subsequent period, the amount of impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment losses was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

***Financial liabilities and equity***

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

***Effective interest method***

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Interest expense is recognised on an effective interest basis.

*Financial liabilities*

Financial liabilities including bank borrowings, trade and other payables, amounts due to related parties, amount due to ultimate controlling shareholder and amount due to immediate holding company are subsequently measured at amortised cost, using the effective interest method.

*Equity instruments*

Equity instruments issued by a group entity are recorded at the proceeds received, net of direct issue costs.

***Financial guarantee contracts***

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument. A financial guarantee contract issued by the Group and not designated as at fair value through profit or loss is recognised initially at its fair value less transaction costs that are directly attributable to the issue of the financial guarantee contract. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount determined in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18 *Revenue*.

***Derecognition***

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and receivable is recognised in profit or loss.

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

## 5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, which are described in Note 4, management is required to make estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

### Key sources of estimation uncertainty

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next year.

***Useful lives and impairment of property, plant and equipment***

The Group's management determines the estimated useful lives and related depreciation charges for its property, plant and equipment. This estimate is based on the historical experience of the actual useful lives of property, plant and equipment of similar nature and functions. Management will increase the depreciation charge where useful lives are expected to be shorter than estimated, or it will write off or write down obsolete or non-strategic assets that have been abandoned. Change in these estimations may have a material impact on the results of the Group.

***Estimated impairment of trade receivables***

When there is objective evidence of impairment of trade receivables, the Group takes into consideration the estimation of future cash flows. The amount of the impairment loss is measured as the difference between the receivable's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). Where the actual future cash flows are less than expected, a material impairment loss may arise. As at 31 December 2007, 2008 and 2009, the carrying amount of trade receivable is RMB58,644,000, RMB92,489,000 and RMB134,035,000, respectively. No allowance for doubtful debts is recognised as at 31 December 2007, 2008 and 2009.

## 6. CAPITAL RISK MANAGEMENT

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to shareholders through optimisation of the debt and equity balance. The Group's overall strategy remains unchanged during the Track Record Period.

The capital structure of the Group consists of net debt (which includes bank borrowings), cash and cash equivalents and equity attributable to owners of the Company, comprising share capital/paid-in capital, capital reserve, special reserve, statutory surplus reserve, and accumulated profits.

The management of the Group reviews the capital structure periodically. The Group considers the cost of capital and the risks associate with each class of capital and will balance its overall capital structure through the payment of dividends, new share issues and share buy-backs as well as the issue of new debt or the redemption of existing debt.

## 7. FINANCIAL INSTRUMENTS

### 7a. Categories of financial instruments

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Financial assets: | | | |
| Loans and receivables (including cash and cash equivalents) | 78,727 | 151,719 | 224,016 |
| Financial liabilities: | | | |
| Amortised cost | 551,302 | 597,412 | 716,419 |

### 7b. Financial risk management objectives and policies

The Group's major financial instruments include trade and other receivables, amounts due from (to) related parties, amounts due from (to) ultimate controlling shareholder, pledged bank deposits, bank balances and cash, trade and other payables, amount due to immediate holding company and bank borrowings. Details of the financial instruments are disclosed in respective notes. The risks associated with these financial instruments include market risk (currency risk and interest rate risk), credit risk and liquidity risk. The policies on how to mitigate these risks are set out below. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

***Market risk***

(i) *Currency risk*

Several subsidiaries of the Company have financial assets and liabilities denominated in foreign currencies, which expose the Group to foreign currency risk.

The carrying amounts of the Group's foreign currency denominated monetary assets and monetary liabilities at the reporting dates are as follows:

| | Assets | | | Liabilities | | |
|---|---|---|---|---|---|---|
| | At 31 December | | | At 31 December | | |
| | 2007 | 2008 | 2009 | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| Hong Kong Dollar ("HK$") . . . . | 109 | 74 | 43 | 88,626 | 91,917 | 1,649 |
| United States Dollar ("US$") . . | — | — | 62,037 | — | 7,174 | 108,840 |

Sensitivity analysis

The Group is mainly exposed to foreign currency risk relating to HK$ and US$.

The following table details the Group's sensitivity to a 5% increase and decrease in RMB against the relevant foreign currencies. 5% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currencies denominated monetary items. A positive number below indicates an increase in post-tax profit where RMB strengthens 5% against the relevant foreign currencies. A negative number indicates a decrease in post-tax profit. For a 5% weakening of RMB against the relevant foreign currencies, there would be an equal and opposite impact on post-tax profit.

| | HK$ | | | US$ | | |
|---|---|---|---|---|---|---|
| | At 31 December | | | At 31 December | | |
| | 2007 | 2008 | 2009 | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| Profit or loss (i) . . . . . | 4,426 | 4,592 | 80 | — | 359 | 2,340 |

(i) This is mainly attributable to the exposure on HK$ and US$ denominated notes payable, bank balances and amounts due to ultimate controlling shareholder and immediate holding company at respective year end dates.

(ii) *Interest rate risk*

The Group's fair value interest rate risk relates primarily to fixed-rate pledged bank deposits and bank borrowings. The Group's cash flow interest rate risk relates primarily to bank balances, loan payable to a related party, amount due from ultimate controlling shareholder and variable-rate bank borrowings (see notes 26 and 23 for details of these borrowings).

The Group currently does not have an interest rate hedging policy. However, the management monitors interest rate risk exposure and will consider hedging significant interest rate risk should the need arises.

The Group's exposures to interest rates on financial liabilities are detailed in the liquidity risk management section of this note. The Group cash flow interest rate risk is mainly concentrated on the fluctuation of Benchmark Borrowing Rate of The People's Bank of China ("Benchmark Rate") arising from the Group's RMB denominated borrowings.

Sensitivity analysis

In the management's opinion, the Group does not have significant exposure to interest rate risk related to its variable-rate bank balances during the Track Record Period.

The sensitivity analyses below have been determined based on the exposure to interest rate risk for variable-rate amount due to related parties and bank borrowings. The analysis is prepared assuming these financial instruments outstanding at the end of the reporting period were outstanding for the whole year. A 50 basis point increase or decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the reasonably possible change in interest rates.

At the end of the respective reporting periods, if interest rates had been increased/decreased by 50 basis points and all other variables were held constant, the Group's post-tax profit for the year would decrease/increase by approximately RMB380,000, RMB755,000 and RMB1,313,000 for the years ended 31 December 2007, 2008 and 2009.

***Credit risk***

The Group's maximum exposure to credit risk which will cause a financial loss to the Group due to failure to discharge an obligation by the counterparties is arising from the carrying amounts of the respective recognised financial assets as stated in the combined statements of financial position and the financial guarantees provided by the Group as disclosed in note 26(c).

In order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade debt at the end of each reporting period to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is significantly reduced.

In addition, the Group is also exposed to credit risk in respect of guarantees given to a bank and a financial institution for banking facilities granted to its related companies as at 31

December 2007 and 2008. The guarantees were fully released during the year ended 31 December 2009 (See note 26(c)). In the opinion of the directors of the Company, the credit risk given to a bank and a financial institution is considered insignificant as the related companies are in good financial positions.

Although the bank balances are concentrated on certain counterparties, the credit risk on liquid funds is limited because the counterparties are state-owned banks located in the PRC or those banks with high credit ratings.

The Group has concentration of credit risk as 33%, 30% and 27% of the total trade receivables was due from the Group's five largest customers as at 31 December 2007, 2008 and 2009, respectively. In order to minimise the credit risk, management continuously monitors the level of exposure to ensure that follow-up actions and/or corrective actions are taken promptly to lower the risk exposure or to recover overdue balances.

***Liquidity risk***

In the management of the liquidity risk, the Group monitors and maintains a level of cash and cash equivalents deemed adequate by the management to finance the Group's operations and mitigate the effects of fluctuations in cash flows. The management monitors the utilisation of bank borrowings and ensures compliance with loan covenants.

As at 31 December 2007, 2008 and 2009, the Group has available unutilised bank loan facilities of approximately RMB1,500,000, RMB56,250,000 and RMB120,000,000, respectively.

As at 31 December 2007, 2008 and 2009, the Group has net current liabilities of RMB465 million, RMB406 million and RMB50 million, respectively. This was primarily attributable to (i) investments in long-term assets (such as property, plant and equipment) as it expands its factories; and (ii) utilisation of short-term notes payable to partly finance its operation, short-term borrowings from banks and immediate holding company for expanding its operation. The nature of the Group's business is such that the majority of its liabilities are short-term, consisting mainly of trade and other payables, amounts due to related parties, amount due to ultimate controlling shareholder, amount due to immediate holding company and short-term bank borrowings, giving rise to its net current liabilities positions on those dates. The Group has not breached the repayment terms of any of its bank borrowings. The Group currently services its debts primarily through cash generated from operations, renewal of short-term bank borrowings and raise of long-term bank borrowings. The Group has not experienced any difficulty in raising funds by rolling over the short-term loans borrowed or obtaining new long-term loans from various commercial banks in the PRC during the Track Record Period and accordingly the directors of the Company are satisfied that the Group will be able to meet in full its financial obligations as they fall due for the foreseeable future.

The following table details the Group's remaining contractual maturity for its financial liabilities as at 31 December 2007, 2008 and 2009. The table has been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay. The table includes both interest and principal cash flows.

Liquidity tables

| | Weighted average interest rate | Repayable on demand | Less than 1 year | 1-2 years | 2-5 years | Total undiscounted cash flows | Carrying amount |
|---|---|---|---|---|---|---|---|
| | % | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| **At 31 December 2007** | | | | | | | |
| Trade and other payables | — | — | 45,370 | — | — | 45,370 | 45,370 |
| Amounts due to related parties | — | 123,306 | — | — | — | 123,306 | 123,306 |
| Amount due to ultimate controlling shareholder | — | 88,626 | — | — | — | 88,626 | 88,626 |
| Bank borrowings | | | | | | | |
| - fixed rate | 6.82 | — | 196,120 | — | — | 196,120 | 190,000 |
| - variable rate | 7.39 | — | 108,236 | — | — | 108,236 | 104,000 |
| Financial guarantee contract | — | 7,500 | — | — | — | — | — |
| | | 219,432 | 349,726 | — | — | 561,658 | 551,302 |
| **At 31 December 2008** | | | | | | | |
| Trade and other payables | — | — | 149,816 | — | — | 149,816 | 149,816 |
| Amounts due to related parties | | | | | | | |
| - interest bearing | 6.40 | 21,250 | — | — | — | 21,250 | 21,250 |
| - non-interest bearing | — | 23,429 | — | — | — | 23,429 | 23,429 |
| Amount due to ultimate controlling shareholder | — | 91,917 | — | — | — | 91,917 | 91,917 |
| Bank borrowings | | | | | | | |
| - fixed rate | 6.54 | — | 135,322 | — | — | 135,322 | 131,000 |
| - variable rate | 7.04 | — | 192,672 | — | — | 192,672 | 180,000 |
| Financial guarantee contract | — | 20,000 | — | — | — | — | — |
| | | 156,596 | 477,810 | — | — | 614,406 | 597,412 |
| **At 31 December 2009** | | | | | | | |
| Trade and other payables | — | — | 87,581 | — | — | 87,581 | 87,581 |
| Amounts due to related parties | — | 8,584 | — | — | — | 8,584 | 8,584 |
| Amount due to ultimate controlling shareholder | — | 1,649 | — | — | — | 1,649 | 1,649 |
| Amount due to immediate holding company | — | 95,605 | — | — | — | 95,605 | 95,605 |
| Bank borrowings | | | | | | | |
| - fixed rate | 4.78 | — | 178,141 | — | — | 178,141 | 173,000 |
| - variable rate | 4.86 | — | 29,581 | 86,110 | 275,404 | 391,095 | 350,000 |
| | | 105,838 | 295,303 | 86,110 | 275,404 | 762,655 | 716,419 |

The amount included above for financial guarantee contracts are the maximum amounts the Group could be required to settle under the arrangement for the full guaranteed amount if that amount is claimed by the counterparty to the guarantee. Based on expectations at the end of the reporting period, the Group considers that it is more likely than not that no amount will be payable under the arrangement. However, this estimate is subject to change depending on the probability of the counterparty claiming under the guarantee which is a function of the likelihood that the financial receivables held by the counterparty which are guaranteed suffer credit losses.

7c. **Fair value**

The fair value of financial assets and financial liabilities is determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions.

The directors of the Company consider that the carrying amounts of financial assets and financial liabilities recorded at amortised cost in the Financial Information approximate their fair values.

## 8. REVENUE

An analysis of the Group's revenue is as follows:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Revenue from the sales of: | | | |
| Double-sided Machine Finished ("MF") Tissue Paper | 147,890 | 299,438 | 470,426 |
| Single-sided MF Tissue Paper | 46,039 | 171,450 | 168,609 |
| Copy paper | 73,657 | 91,131 | 85,758 |
| | 267,586 | 562,019 | 724,793 |

## 9. SEGMENT INFORMATION

### (a) Products within each operating segment

The chief operating decision maker of the Group has been identified as the Chief Executive Officer. For management purposes, the Group is organised into three operating segments - Double-sided MF Tissue Paper, Single-sided MF Tissue Paper and Copy Paper. These operating segments form the basis on which the Group's Chief Executive Officer makes decisions about resources allocation and performance assessment. The principal products within each of these operating segments are as follows:

- Double-sided MF Tissue Paper — manufacturing and marketing of Double-sided MF Tissue Paper;
- Single-sided MF Tissue Paper — manufacturing and marketing of Single-sided MF Tissue Paper; and
- Copy Paper — manufacturing and marketing of copy paper.

### (b) Segment revenue and segment results

| | Segment revenue | | | Segment results | | |
|---|---|---|---|---|---|---|
| | Year ended 31 December | | | Year ended 31 December | | |
| | 2007 | 2008 | 2009 | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| Double-sided MF Tissue Paper | 147,890 | 299,438 | 470,426 | 47,207 | 99,371 | 154,118 |
| Single-sided MF Tissue Paper | 46,039 | 171,450 | 168,609 | 11,761 | 57,048 | 57,742 |
| Copy Paper | 73,657 | 91,131 | 85,758 | 21,519 | 31,682 | 28,792 |
| | 267,586 | 562,019 | 724,793 | 80,487 | 188,101 | 240,652 |
| Selling and distribution expenses | | | | (2,075) | (2,994) | (4,066) |
| Administrative expenses | | | | (12,645) | (25,364) | (37,018) |
| Other income and other gains and losses | | | | 5,341 | 5,962 | 2,421 |
| Finance costs | | | | (13,613) | (20,021) | (18,219) |
| Profit before tax | | | | 57,495 | 145,684 | 183,770 |
| Taxation | | | | (15,223) | (13,041) | (13,093) |
| Profit and total comprehensive income for the year | | | | 42,272 | 132,643 | 170,677 |

Revenue reported above represents revenue generated from external customers. There were no intersegment sales during the Track Record Period.

The accounting policies of the operating segments are the same as the Group's accounting policies described in note 4. Segment results represent the gross profit of each operating segment. This is the measure reported to Chief Executive Officer for the purposes of resources allocation and performance assessment.

(c) **Segment assets**

| | Assets | | |
|---|---|---|---|
| | At 31 December | | |
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Double-sided MF Tissue Paper | 132,628 | 242,367 | 243,003 |
| Single-sided MF Tissue Paper | 54,046 | 53,223 | 51,001 |
| Copy Paper | 36,605 | 36,337 | 35,936 |
| Total of all segments | 223,279 | 331,927 | 329,940 |
| Unallocated | 508,577 | 587,050 | 975,389 |
| Combined | 731,856 | 918,977 | 1,305,329 |

Segment assets include certain property, plant and equipment used specifically for the production of different products and inventory.

Segment liabilities are not presented as liabilities are generally incurred for all operating segments.

(d) **Other segment information**

| | Double-sided MF Tissue Paper | Single-sided MF Tissue Paper | Copy Paper | Unallocated | Combined total |
|---|---|---|---|---|---|
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| **Year ended 31 December 2007** | | | | | |
| Capital additions | 64,393 | 43,095 | — | 202,609 | 310,097 |
| Depreciation and amortisation | 4,370 | 1,223 | 1,907 | 4,641 | 12,141 |
| **Year ended 31 December 2008** | | | | | |
| Capital additions | 114,576 | 27 | 1 | 34,551 | 149,155 |
| Depreciation and amortisation | 6,573 | 2,454 | 1,897 | 9,173 | 20,097 |
| Gain on disposal of property, plant and equipment | — | — | — | 31 | 31 |
| **Year ended 31 December 2009** | | | | | |
| Capital additions | 13,358 | — | — | 251,053 | 264,411 |
| Depreciation and amortisation | 10,171 | 2,456 | 1,894 | 12,982 | 27,503 |
| Loss on disposal of property, plant and equipment | — | — | — | 123 | 123 |

(e) **Geographical information**

The Group principally operates in the PRC (country of domicile of the operating subsidiaries). All non-current assets of the Group are located in the PRC.

All of the Group's revenue from external customers is attributed to the group entities' countries of domicile (i.e. the PRC).

(f) **Information about major customers**

During the Track Record Period, there are no individual customers with sales of 10% or more of the Group's total sales.

## 10. OTHER INCOME AND OTHER GAINS AND LOSSES

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Bank interest income | 360 | 911 | 1,006 |
| Gain (loss) on disposal of property, plant and equipment | — | 31 | (123) |
| Net foreign exchange gains | 4,798 | 5,094 | 244 |
| Donation | (1,365) | (1,655) | (5) |
| Government grants (note 1) | 850 | 1,220 | 903 |
| Gross rental income from investment properties | 1,642 | 1,642 | 1,642 |
| Less: direct operating expenses from investment properties | (913) | (913) | (913) |
| Others | (31) | (368) | (333) |
| | 5,341 | 5,962 | 2,421 |

*Note 1:* Government grants represented incentives granted by the local authorities to the Group's subsidiaries located in the PRC for developing innovative production technology and maintaining a good reputation in the business community. There are no unfulfilled conditions and other contingencies attaching to such grants.

## 11. FINANCE COSTS

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Interest on: | | | |
| Bank borrowings wholly repayable within five year | 14,475 | 21,814 | 22,722 |
| Amount due to a related party | — | 1,525 | — |
| Amount due to ultimate controlling shareholder | 171 | — | — |
| Less: Amounts capitalised | (1,033) | (3,318) | (4,503) |
| | 13,613 | 20,021 | 18,219 |

Finance costs of RMB1,033,000 and RMB1,793,000 capitalised for the years ended 31 December 2007 and 2008, respectively arose on general borrowings and are capitalised by applying a capitalisation rate of 5.7% and 5.4% per annum, respectively, to expenditure on qualifying asset.

The borrowing costs of RMB1,525,000 and RMB4,503,000 capitalised during the year ended 31 December 2008 and 2009, respectively are attributable to funds borrowed specifically for the purpose of obtaining particular qualifying assets.

## 12. PROFIT BEFORE TAX

Profit before tax has been arrived at after charging:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Employee benefits expenses (including directors): | | | |
| Salaries and other benefits | 8,109 | 18,834 | 24,573 |
| Retirement benefits scheme contributions | 1,497 | 3,970 | 3,459 |
| | 9,606 | 22,804 | 28,032 |
| Depreciation of property, plant and equipment | 10,349 | 17,027 | 22,895 |
| Depreciation of investment properties | 913 | 913 | 913 |
| Release of prepaid lease payments | 879 | 2,157 | 3,695 |
| Total depreciation and amortisation expenses | 12,141 | 20,097 | 27,503 |
| Auditors' remuneration | 53 | 1,436 | 1,252 |
| Listing expenses | — | 2,002 | 4,956 |
| Cost of inventories recognised as expenses | 187,099 | 373,918 | 484,141 |

During the year ended 31 December 2009, there was an allowance for obsolete raw materials of RMB179,000 recognised and included in cost of sales.

## 13. TAXATION

The income tax expense of the Track Record Period represents the PRC Enterprise Income Tax ("EIT") which is calculated at the prevailing tax rate on the taxable income of the group entities in the PRC.

The Company was incorporated in Cayman Islands and Xi Yuan BVI was incorporated in the BVI and are not subject to any income tax.

Sunwell was incorporated in Hong Kong and has had no assessable profits subject to Hong Kong Profits Tax since its incorporation.

Youlanfa, Xiyuan and Huaxiang (collectively referred as the "PRC Subsidiaries") are Foreign Investment Enterprise registered in the PRC and were subject to EIT at a statutory tax rate of 27% for the year ended 31 December 2007. Xiyuan and Huaxiang, which are entitled to an exemption from EIT for two years starting from their first exemption year, followed by a 50% tax relief for the following three years were approved to enjoy the exemption in 2008 and 2009 (the "Tax Concession") which was their first and second exemption year, respectively.

On 16 March 2007, the PRC promulgated the Law of the PRC on EIT (the "New Tax Law") by Order No. 63 of the President of the PRC. On 6 December 2007, the State Council of the PRC issued Implementation Regulations of the New Tax Law, which have reduced the income tax rate to 25% for the PRC Subsidiaries from 1 January 2008.

Youlanfa is in the process of obtaining a high and new technology enterprise certificate as at 31 December 2009. Upon issuance of the certificate, Youlanfa will be subject to a preferential income tax rate of 15% from 2010 to 2012.

According to the Circular of the State Council on the Implementation of Transitional Preferential Policies for EIT (Guofa [2007] No. 39), the Tax Concession for Xiyuan and Huaxiang are still applicable until the end of the five-year transitional period under the New Tax Law. Huaxiang and Xiyuan were entitled to an exemption from EIT for 2008 and 2009 and subjected to EIT at 12.5% for 2010 to 2012 and 25% from 2013 onwards.

The tax charge for the Track Record Period can be reconciled to the profit before tax per combined statements of comprehensive income as follows:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Profit before tax | 57,495 | 145,684 | 183,770 |
| Tax at the PRC enterprise income tax rate (2007: 27%, 2008 and 2009: 25%) (note) | 15,524 | 36,421 | 45,943 |
| Effect of tax exemptions | — | (22,259) | (34,706) |
| Tax effect of expenses not deductible for tax purpose | 237 | 97 | 1,896 |
| Tax effect of income not taxable for tax purpose | (909) | (1,242) | (158) |
| Others | 371 | 24 | 118 |
| | 15,223 | 13,041 | 13,093 |

*Note:* The applicable income tax rate of 25% adopted is the unified statutory rate of the PRC Subsidiaries effective from 1 January 2008. The applicable income tax rate of 27% adopted for the year ended 31 December 2007 was the domestic rate of Youlanfa and Huaxiang which were the operating entities of the Group for that period.

Under the New Tax Law, withholding tax is imposed on dividends declared in respect of profits earned by the PRC Subsidiaries from 1 January 2008 onwards. Deferred taxation has not been provided for in the Financial Information in respect of temporary differences attributable to accumulated distributable profits of the PRC Subsidiaries amounting to RMB114,832,000 and RMB274,592,000 at 31 December 2008 and 2009, respectively, as the Company is able to control the timing of the reversal of the temporary differences and it is probable that the temporary differences will not reverse in the foreseeable future.

There is no significant unprovided deferred taxation during the Track Record Period or at the end of each reporting period.

## 14. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

### (a) Directors' emoluments

Details of the emoluments paid to the directors of the Company for the Track Record Period are as follows:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Directors' emoluments: | | | |
| - salaries and other benefits | 900 | 900 | 900 |
| - retirement benefit schemes contributions | 6 | 7 | 7 |
| | 906 | 907 | 907 |

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Mr Ke | 603 | 604 | 604 |
| Mr Ke Jixiong | 303 | 303 | 303 |
| Mr Cao Xu | — | — | — |
| Mr Zhang Guoduan | — | — | — |
| Mr Paul Steven Wolansky | — | — | — |
| Prof. Zhang Daopei | — | — | — |
| Prof. Chen Lihui | — | — | — |
| Mr Chow Kwok Wai | — | — | — |
| | 906 | 907 | 907 |

(b) **Employees' emoluments**

Of the five individuals with the highest emoluments in the Group for the Track Record Period, two were directors of the Company whose emoluments are included in the disclosures above for the years ended 31 December 2007, 2008 and 2009. The emoluments of the remaining three individuals for the years ended 31 December 2007, 2008 and 2009, were as follows:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Salaries and other benefits | 388 | 398 | 349 |
| Retirement benefit schemes contributions | — | 7 | 9 |
| | 388 | 405 | 358 |

During the Track Record Period, no emoluments were paid by the Group to any of the directors or the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office. None of the directors waived any emoluments during the Track Record Period.

The emoluments of the five highest paid individuals during the Track Record Period were below HK$1,000,000.

## 15. EARNINGS PER SHARE

The calculation of the basic earnings per share for the Track Record Period is based on the profit attributable to owners of the Company and 750,000,000 shares of the Company, taking into account the share swap pursuant to the Group Reorganisation and adjusted for the effect of the capitalisation issue.

## 16. PROPERTY, PLANT AND EQUIPMENT

| | Buildings | Plant and machinery | Office equipment | Motor vehicles | Construction in progress | Total |
|---|---|---|---|---|---|---|
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| COST | | | | | | |
| At 1 January 2007 | 43,447 | 96,101 | 798 | 503 | 65,079 | 205,928 |
| Additions | — | 3,243 | 1,518 | 437 | 221,593 | 226,791 |
| Transfer | 91,975 | 104,234 | — | — | (196,209) | — |
| At 31 December 2007 and 1 January 2008 | 135,422 | 203,578 | 2,316 | 940 | 90,463 | 432,719 |
| Additions | 2,893 | 3,676 | 1,748 | 543 | 140,295 | 149,155 |
| Transfer | 50,016 | 47,510 | — | — | (97,526) | — |
| Disposals | — | — | (204) | (170) | — | (374) |
| At 31 December 2008 and 1 January 2009 | 188,331 | 254,764 | 3,860 | 1,313 | 133,232 | 581,500 |
| Additions | 20,554 | 4,813 | 1,421 | 3,238 | 81,369 | 111,395 |
| Transfer | 58,425 | 81,746 | — | — | (140,171) | — |
| Disposals | — | — | — | (260) | — | (260) |
| At 31 December 2009 | 267,310 | 341,323 | 5,281 | 4,291 | 74,430 | 692,635 |
| DEPRECIATION | | | | | | |
| At 1 January 2007 | (9,178) | (10,966) | (559) | (406) | — | (21,109) |
| Provided for the year | (2,683) | (7,418) | (176) | (72) | — | (10,349) |
| At 31 December 2007 and 1 January 2008 | (11,861) | (18,384) | (735) | (478) | — | (31,458) |
| Provided for the year | (4,928) | (11,487) | (531) | (81) | — | (17,027) |
| Disposals | — | — | 181 | 153 | — | 334 |
| At 31 December 2008 and 1 January 2009 | (16,789) | (29,871) | (1,085) | (406) | — | (48,151) |
| Provided for the year | (6,655) | (15,131) | (776) | (333) | — | (22,895) |
| Disposals | — | — | — | 57 | — | 57 |
| At 31 December 2009 | (23,444) | (45,002) | (1,861) | (682) | — | (70,989) |
| CARRYING VALUES | | | | | | |
| At 31 December 2007 | 123,561 | 185,194 | 1,581 | 462 | 90,463 | 401,261 |
| At 31 December 2008 | 171,542 | 224,893 | 2,775 | 907 | 133,232 | 533,349 |
| At 31 December 2009 | 243,866 | 296,321 | 3,420 | 3,609 | 74,430 | 621,646 |

The above items of property, plant and equipment are depreciated on straight-line basis at the following rates:

| | |
|---|---|
| Buildings | 30 years |
| Plant and machinery | 10-20 years |
| Office equipment | 5 years |
| Motor vehicles | 5 years |

Buildings are located on land use rights in the PRC with lease term of 50 years.

## 17. PREPAID LEASE PAYMENTS

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| The Group's prepaid lease payments comprise: | | | |
| Leasehold land in the PRC: | | | |
| - Medium-term lease | 117,917 | 115,760 | 265,081 |
| Analysed for reporting purpose as: | | | |
| - Current assets | 2,158 | 2,534 | 5,770 |
| - Non-current assets | 115,759 | 113,226 | 259,311 |
| | 117,917 | 115,760 | 265,081 |

The Group's prepaid lease payments amounts represent the prepayments for land use rights situated in the PRC. The leasehold lands have lease term of 50 years.

## 18. INVESTMENT PROPERTIES

| | RMB'000 |
|---|---|
| COST | |
| At 1 January 2007, 31 December 2007, 31 December 2008 and 31 December 2009 | 30,422 |
| ACCUMULATED DEPRECIATION | |
| At 1 January 2007 | (6,585) |
| Provided for the year | (913) |
| At 31 December 2007 and 1 January 2008 | (7,498) |
| Provided for the year | (913) |
| At 31 December 2008 and 1 January 2009 | (8,411) |
| Provided for the year | (913) |
| At 31 December 2009 | (9,324) |
| CARRYING VALUES | |
| At 31 December 2007 | 22,924 |
| At 31 December 2008 | 22,011 |
| At 31 December 2009 | 21,098 |

The fair value of the Group's investment properties in the PRC, at 31 December 2007, 2008 and 2009 was RMB23,560,000, RMB23,311,000 and RMB22,143,000 respectively. The fair value has been arrived at based on a valuation carried out by Jones Lang LaSalle Sallmanns Limited, independent valuers not connected with the Group. The valuation was determined by capitalising the rental income received from the existing lease with due provision from the reversionary income potential of the properties.

Upon the expiry of the lease contract with Fujian Youlanfa Leathercover Paper Co., Ltd. ("YLF Leathercover") on 31 March 2010, the above properties will be occupied by the Group for their own use and the respective carrying value will be transferred to property, plant and equipment.

The above investment properties are depreciated on a straight-line basis over 30 years.

## 19. INVENTORIES

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Raw materials | 13,367 | 15,852 | 99,483 |
| Work in progress | 755 | 30 | 111 |
| Finished goods | 6,656 | 11,621 | 10,688 |
| | 20,778 | 27,503 | 110,282 |

## 20. TRADE AND OTHER RECEIVABLES AND PREPAYMENTS

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Trade receivables | 58,644 | 92,489 | 134,035 |
| Prepayments to suppliers | 3,216 | 35,572 | 13,658 |
| Other prepayments | 183 | 1,143 | 5,364 |
| Other tax recoverable | — | — | 1,227 |
| Others | 40 | — | 296 |
| | 62,083 | 129,204 | 154,580 |

The Group allows an average credit period of 60 days to its trade customers. The ageing of trade receivables presented based on the invoice date at the end of the reporting period is as follows:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| 0 to 30 days | 34,859 | 60,043 | 90,385 |
| 31 to 60 days | 18,947 | 28,510 | 43,650 |
| 61 to 90 days | 3,600 | 2,669 | — |
| 91 to 180 days | 1,238 | 1,267 | — |
| | 58,644 | 92,489 | 134,035 |

Before accepting any new customer, the Group assesses the potential customer's credit quality and defines credit limits by customer. Limits attributed to customers are reviewed annually.

In determining the recoverability of a trade receivable, the Group considers any change in the credit quality of the trade receivable from the date credit was initially granted up to the reporting date and no impairment is considered necessary for those balances which are not past due.

Included in the Group's trade receivable balance are debtors with aggregate carrying amounts of RMB4,838,000, RMB3,936,000 and Nil which are past due as at 31 December 2007, 2008 and 2009, respectively, which the Group has not provided for impairment loss as there has not been a significant change in credit quality and amounts are still considered recoverable based on historical experience. The Group does not hold any collateral over these balances.

**Ageing of trade receivables which are past due but not impaired**

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| 61 to 90 days | 3,600 | 2,669 | — |
| 91 to 180 days | 1,238 | 1,267 | — |
| Total | 4,838 | 3,936 | — |

The Group will provide fully for all receivables over two years because historical experience is that receivables that are past due beyond two years are generally not recoverable.

**Movement in the allowance for doubtful debts**

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Balance at beginning of the year | — | — | — |
| Impairment losses recognised on receivables | — | — | 68 |
| Amounts written off as uncollectible | — | — | (68) |
| Balance at end of the year | — | — | — |

## 21. PLEDGED BANK DEPOSITS/BANK BALANCES AND CASH

Bank balances and cash comprise cash held by the Group and short-term deposits with an original maturity of three months or less. Pledged bank deposits represent deposits pledged to banks to secure banking facilities granted to the Group.

Bank balances of the Group carry market interest rates of range from 0.06% to 1.00%, 0.36% to 1.00% and 0.01% to 0.36% per annum as at 31 December 2007, 2008 and 2009, respectively.

Pledged bank deposits of the Group carry market interest rates of range from 0.72% to 2.44%, 0.36% to 3.78% and 0.36% to 3.78% per annum as at 31 December 2007, 2008 and 2009, respectively.

## 22. TRADE AND OTHER PAYABLES

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Trade payables | 32,774 | 20,642 | 67,467 |
| Notes payables | 8,640 | 119,674 | 13,235 |
| | 41,414 | 140,316 | 80,702 |
| Other payables for acquisition of plant and equipment | 3,956 | 9,500 | 6,879 |
| Other tax payables | 6,479 | 9,000 | 7,110 |
| Accrued staff costs | 1,427 | 2,253 | 2,787 |
| Accrued employee social security fund | 2,710 | 6,561 | 9,790 |
| Accrued electricity expenses | 1,918 | 3,411 | 4,864 |
| Other accrued expenses | 1,378 | 3,205 | 6,194 |
| | 59,282 | 174,246 | 118,326 |

The following is an aged analysis of trade payables at the end of each reporting period:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Within 30 days | 21,775 | 11,571 | 42,194 |
| 31 to 90 days | 10,939 | 8,923 | 25,269 |
| 91 to 120 days | 52 | 148 | 4 |
| 121 to 180 days | 8 | — | — |
| | 32,774 | 20,642 | 67,467 |

The following is an aged analysis of notes payables at the end of each reporting period:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| 31 to 90 days | 2,140 | 41,500 | — |
| 91 to 120 days | — | 45,714 | 8,660 |
| 121 to 180 days | 6,500 | 32,460 | 4,575 |
| | 8,640 | 119,674 | 13,235 |

Trade payables and notes payables principally comprise amounts outstanding for purchase of goods. The average credit period for purchase of goods is 60 days to 180 days. The Group has financial risk management policies in place to ensure that all payables are within the credit timeframe.

## 23. BANK BORROWINGS

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Secured bank borrowings | 128,000 | 286,500 | 403,000 |
| Unsecured bank borrowings | 166,000 | 24,500 | 120,000 |
| | 294,000 | 311,000 | 523,000 |
| The amount is repayable as follows: | | | |
| Within one year | 294,000 | 311,000 | 182,820 |
| More than one year, but not exceeding two years | — | — | 71,310 |
| More than two years, but not exceeding five years | — | — | 268,870 |
| | 294,000 | 311,000 | 523,000 |
| Less: Amounts due within one year shown under current liabilities | (294,000) | (311,000) | (182,820) |
| | — | — | 340,180 |

The ranges of effective interest rates (which are also equal to contractual interest rates) on the Group's borrowings are as follows:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Effective interest rate: | | | |
| Fixed-rate bank borrowings | 5.51% to 7.47% | 5.31% to 8.22% | 4.78% |
| Variable-rate bank borrowings | Benchmark Rate | Benchmark Rate to 110% of Benchmark Rate | 90% of Benchmark Rate to Benchmark Rate |

The Group's bank borrowings are dominated in RMB. Interest is repriced every month.

The borrowings are guaranteed and/or secured. Details set out as follows:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Type A | 11,000 | — | 10,000# |
| Type B | — | — | 144,000# |
| Type C | — | 60,500 | 59,000# |
| Type D | — | — | 50,000# |
| Type E | — | — | 150,000# |
| Type F | 75,100 | — | 110,000# |
| Type G | 13,000 | 3,500 | — |
| Type H | 45,800 | — | — |
| Type I | 15,400 | — | — |
| Type J | — | 60,000 | — |
| Type K | 45,000 | 19,500 | — |
| Type L | 5,700 | — | — |
| Type M | 10,000 | — | — |
| Type N | 13,000 | — | — |
| Type O | 60,000 | 60,000 | — |
| Type P | — | 24,500 | — |
| Type Q | — | 65,000 | — |
| Type R | — | 18,000 | — |
| | 294,000 | 311,000 | 523,000 |

Type A: Borrowings are guaranteed by Youlanfa Group Industry Co., Ltd. ("YLF Industry"), a minority shareholder.

Type B: Borrowings are guaranteed by YLF Industry, a minority shareholder and secured by assets of related companies which are controlled by Mr Ke's family members.

Type C: Borrowings are guaranteed by YLF Industry, a minority shareholder and secured by assets of related companies which are controlled by Mr Ke's family members and the Group (note).

Type D: Borrowings are guaranteed and secured by the assets of YLF Industry, a minority shareholder.

Type E: Borrowings are guaranteed by Mr Ke and/or his family members and secured by assets of the Group (note).

Type F: Borrowings are guaranteed by related companies which are controlled by Mr Ke's family members.

Type G: Borrowings are secured by assets of the Group (note).

Type H: Borrowings are guaranteed by Mr Ke and/or his family members and third parties.

Type I: Borrowings are guaranteed by Mr Ke and/or his family members.

Type J: Borrowings are guaranteed by Mr Ke and/or his family members and secured by assets of related companies which are controlled by Mr Ke's family members.

Type K: Borrowings are guaranteed by Mr Ke and/or his family members and secured by assets of related companies which are controlled by Mr Ke's family members.

Type L: Borrowings are guaranteed by Mr Ke and/or his family members and related companies which are controlled by Mr Ke's family members.

Type M: Borrowings are guaranteed by related companies which are controlled by Mr Ke's family members and secured by assets of related companies which are controlled by Mr Ke's family members.

Type N: Borrowings are guaranteed by the companies within the Group.

Type O: Borrowings are guaranteed by Mr Ke and/or his family members and secured by assets of minority shareholders and the Group (note).

Type P: Borrowings are guaranteed by Mr Ke and/or his family members, third parties and related companies which are controlled by Mr Ke's family members

Type Q: Borrowings are guaranteed by Mr Ke and/or his family members and related companies which are controlled by Mr Ke's family members and secured by assets of the Group (note).

Type R: Borrowings are guaranteed by Mr Ke and/or his family members and related companies which are controlled by Mr Ke's family members and secured by assets of related companies which are controlled by Mr Ke's family members.

*Note:* The Group has pledged several assets to secure banking facilities granted to the Group. The carrying values of the assets pledged are as follows:

| | At 31 December | | |
|---|---|---|---|
| | **2007** | **2008** | **2009** |
| | **RMB'000** | **RMB'000** | **RMB'000** |
| Property, plant and equipment | 4,938 | 123,324 | 285,203 |
| Land use right | 65,251 | 73,502 | 138,091 |
| | 70,189 | 196,826 | 423,294 |

The above guarantees provided by related parties denoted with asterisk '#' have been released subsequent to 31 December 2009.

## 24. SHARE CAPITAL/PAID-IN CAPITAL

### The Group

The share capital/paid-in capital shown on the combined statements of financial position is as follows:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Share capital/paid-in capital . . . . . . . . | 65,390 | 10 | — |

For the purpose of the Financial Information, the share capital/paid-in capital in the combined statements of financial position represents the combined share capital/paid-in capital of Youlanfa and Sunwell as at 31 December 2007, share capital of Sunwell as at 31 December 2008 and share capital of Xi Yuan BVI as at 31 December 2009.

### The Company

The Company was incorporated in the Cayman Islands as an exempted company with limited liability under the Companies Law (2007 Revision) Chapter 22 of the Cayman Islands on 12 October 2009.

At the date of incorporation, the authorised share capital of the Company was HK$380,000 divided into 3,800,000 shares of HK$0.1 each and of which 1 share amounting to HK$0.1 was issued for cash at par as initial capital of the Company.

## 25. RETIREMENT BENEFITS SCHEME

The employees of the Group in the PRC are members of a state-managed retirement benefit scheme operated by the government of the PRC. The Group is required to contribute a certain percentage of payroll costs to the retirement benefit scheme to fund the benefits. The only obligation of the Group with respect to the retirement benefit scheme is to make the specified contributions.

The total cost charged to income of RMB1,497,000, RMB3,970,000 and RMB3,459,000 represents contributions payable to these schemes by the Group in respect of the years ended 31 December 2007, 2008 and 2009, respectively. Except for the accrued employee social security fund disclosed in note 22, all contributions due in respect of the Track Record Period had been paid over to the schemes as at 31 December 2007, 2008 and 2009.

## 26. RELATED PARTY DISCLOSURES

(a) Names and relationships with related parties during the Track Record Period are as follows:

| Name | Relationships |
|---|---|
| 福建優蘭發塗革紙製品有限公司 YLF Leathercover* | YLF Leathercover was a company ultimately controlled by Mr Ke Jixiong, the son of Mr Ke. |
| 福建晉江優蘭發貿易有限公司 Fujian Jinjiang Youlanfa Trading Company Limited* ("YLF Trading")# | YLF Trading was the minority shareholder of Youlanfa until the Group acquired 5.08% interest in Youlanfa from YLF Trading on 20 August 2009. |
| 晉江優蘭發水汽設備有限公司 JinJiang Youlanfa Vapour Equipment Co., Ltd.* ("YLF Vapour") | YLF Vapour was a company ultimately controlled by Mr Ke Jixiong, the son of Mr Ke. |
| 福建優蘭發集團實業有限公司 YLF Industry* | YLF Industry was a company controlled by Mr Ke Jixiong, the son of Mr Ke. It was also the minority shareholder of Huaxiang until the Group acquired the 5% interest in Huaxiang from YLF Industry on 24 September 2009. |
| 漳州華榮紙業有限公司 Zhangzhou Huarong Paper Co., Ltd.* ("Huarong Paper") | Huarong Paper was a company controlled by the brother-in-law of Mr Ke. |
| 漳州順雄貿易有限公司 Zhangzhou Shunxiong Trading Ltd.* (formerly known as Zhangzhou Huayou Trading Co., Ltd.* 漳州華優貿易有限公司) ("Zhangzhou Shunxiong")## | Zhangzhou Shunxiong was the minority shareholder of Xiyuan until the Group acquired the 3.5% interest in Xiyuan from Zhangzhou Shunxiong on 22 April 2009. |

* *for identification only*

\# YLF Trading was owned as to approximately 16.67% by Ms Cai Lishuang, the spouse of Mr Ke, and as to approximately 83.33% by YLF Industry.

\## Zhangzhou Shunxiong was owned as to approximately 86.25% by Mr Wang Kuannai, an independent third party, and as to approximately 13.75% by Mr Ke Jixiong, the son of Mr Ke. On 6 January 2007, Mr Ke Jixiong, the son of Mr Ke, transferred his shareholding to Mr Zhuang Sixiong, the nephew of Mr Ke.

(b) **Balances with related parties**

At the end of each reporting period, the Group has the following balances with related parties:

| | The Group | | | The Company |
|---|---|---|---|---|
| | At 31 December | | | At 31 December |
| | 2007 | 2008 | 2009 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 | RMB'000 |
| Current assets: | | | | |
| Amount due from ultimate controlling shareholder (note 1) | 12,090 | — | — | — |
| Amounts due from related parties | | | | |
| Zhangzhou Shunxiong (note 3) | — | 562 | — | — |
| | 12,090 | 562 | — | — |
| Current liabilities: | | | | |
| Amount due to ultimate controlling shareholder (note 5) | 88,626 | 91,917 | 1,649 | — |
| Amount due to immediate holding company (note 6) | — | — | 95,605 | — |
| Amounts due to related parties | | | | |
| YLF Leathercover (note 7) | 102,515 | 22,775 | — | — |
| YLF Vapour (note 2) | — | 311 | — | — |
| Huarong Paper (note 2) | 20,287 | 20,287 | — | — |
| Zhangzhou Shunxiong (note 4) | 504 | 504 | 8,584 | — |
| YLF Industry (note 2) | — | 802 | — | — |
| | 123,306 | 44,679 | 8,584 | — |
| | 211,932 | 136,596 | 105,838 | — |

*Notes:*

1. The amount of RMB12,090,000 at 31 December 2007 was interest free, unsecured and repayable on demand. Such amount was of non-trade nature and fully repaid in 2008.

2. The amounts are interest free, unsecured, repayable on demand and of non-trade nature.

3. The amount represented prepayment for purchase of raw materials. The amount was interest free and unsecured and was trading in nature. The amount was aged within 180 days at the end of the respective reporting period. Such amount was fully utilised during the year ended 31 December 2009.

4. The amounts of RMB504,000 and RMB504,000 at 31 December 2007 and 2008, respectively, are interest free, unsecured, repayable on demand and of non-trade nature.

   The amount of RMB8,584,000 at 31 December 2009 are interest free and unsecured and are trading in nature. The amounts are aged within 180 days at the end of the reporting period.

5. In 2007, Mr Ke, the ultimate controlling shareholder, advanced RMB83,250,000 to the Group. The amount was interest bearing at 2.4%, unsecured, repayable on demand and of non-trading nature. The amount together with interest was fully repaid in 2007.

   The amounts due to Mr Ke, the ultimate controlling shareholder as at 31 December 2007 and 2008 were interest free, unsecured and repayable on demand. Such amounts are of non-trade nature. During the year ended 31 December 2009, amount due to Mr Ke, the ultimate controlling shareholder, of RMB111,623,000 was waived by him (see note 27).

6. The amounts are interest free, unsecured and repayable on demand. Subsequent to 31 December 2009, the amount due to immediate holding company of RMB95,605,000 has been waived by the immediate holding company.

7. Included in the amount due to YLF Leathercover are the followings:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Loan payable (i) | — | 21,250 | — |
| Other payable (ii) | 102,515 | 1,525 | — |
| | 102,515 | 22,775 | — |

   (i) The amount was interest bearing at the Benchmark Rate per annum, unsecured and repayable on demand. It was of non-trade nature. Such amount was fully repaid during the year ended 31 December 2009.

   (ii) The amounts were interest free, unsecured, repayable on demand and of non-trade nature.

8. The directors of the Company represented that all interest-bearing related companies balances and related interest have been fully settled as of 31 December 2009. Except for the amount due to immediate holding company which has been waived (see note 6 above), all other balances with related parties (including ultimate controlling shareholder) of 31 December 2009 have been fully settled subsequent to 31 December 2009.

(c) **Related parties transactions**

During the Track Record Period, other than those transaction mentioned in note 23, the Group entered into the following significant transactions with related parties:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| **Rental income** | | | |
| YLF Leathercover | 1,642 | 1,642 | 1,642 |
| **Interest expense** | | | |
| YLF Leathercover | — | 1,525 | — |
| Mr Ke | 171 | — | — |
| | 171 | 1,525 | — |
| **Purchase of goods** | | | |
| Zhangzhou Shunxiong | — | 35,588 | 87,631 |
| YLF Leathercover | 1,376 | 4,738 | 6,221 |
| | 1,376 | 40,326 | 93,852 |
| **Rental expense** | | | |
| YLF Vapour | — | 311 | — |
| YLF Industry | — | 802 | — |
| | — | 1,113 | — |
| **Purchase of land use rights** | | | |
| Huarong Paper | 18,850 | — | 43,487 |
| YLF Industry | 63,891 | — | 37,238 |
| YLF Leathercover | — | — | 17,151 |
| YLF Vapour | — | — | 4,944 |
| | 82,741 | — | 102,820 |
| **Purchase of property, plant and equipment** | | | |
| YLF Industry | — | — | 5,297 |
| YLF Leathercover | — | — | 10,137 |
| YLF Vapour | — | — | 4,097 |
| | — | — | 19,531 |

The above transactions with related parties will be discontinued after the listing of the shares of the Company on the Stock Exchange.

On 22 April 2009, the Group acquired 3.5% interest in Xiyuan from Zhangzhou Shunxiong at a consideration of RMB2,150,000.

On 20 August 2009, the Group acquired 5.08% interest in Youlanfa from YLF Trading at a consideration of RMB10,580,000.

On 24 September 2009, the Group acquired 5% interest in Huaxiang from YLF Industry at a consideration of RMB8,880,000.

In the opinion of the Directors, the transactions above were carried out in the Group's ordinary and usual course of business and on normal commercial terms.

The Group has pledged plant and machinery with carrying values of approximately RMB6,071,000, Nil and Nil at 31 December 2007, 2008 and 2009, respectively to secure banking facilities granted to YLF Industry.

In addition, the Group has given the following guarantee to a bank and a financial institution in respect of banking facilities to YLF Leathercover and YLF Industry free of charge:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Amount guaranteed | 7,500 | 20,000 | — |
| Amount utilised | 7,500 | 20,000 | — |

The fair value of financial guarantees contracts at date of inception is insignificant.

The guarantees were fully released during the year ended 31 December 2009.

(d) **Compensation of key management personnel**

The details of remuneration of key management personnel, represents emolument of directors of the Company paid during the Track Record Period are set out in note 14.

The remuneration of directors and key executives is determined by the remuneration committee having regard to the performance of individuals and market trends.

## 27. MAJOR NON-CASH TRANSACTIONS

During the year ended 31 December 2007, certain non-cash transactions have taken place as follows:

(i) the Group acquired land use right from YLF Industry for an aggregate consideration of RMB2,482,000, which was settled by Mr Ke, the ultimate controlling shareholder, on behalf of the Group;

(ii) the repayment of amount due to ultimate controlling shareholder of RMB102,515,000 was settled by YLF Leathercover on behalf of the Group; and

(iii) the additions of construction in progress of RMB1,439,000 were settled by Huarong Paper on behalf of the Group.

During the year ended 31 December 2008, the repayment of amount due to ultimate controlling shareholder of RMB11,735,000 was settled by YLF Leathercover on behalf of the Group.

During the year ended 31 December 2009, amount due to Mr Ke, the ultimate controlling shareholder, of RMB111,623,000 was waived by him. Such amount is recorded in capital reserve as deemed contribution from a shareholder.

## 28. OPERATING LEASE

### The Group as lessee

The minimum lease payments paid under operating leases for the Group's stores and office premises during the three years ended 31 December 2007, 2008 and 2009 were Nil, RMB1,113,000 and Nil, respectively.

At the end of respective reporting periods, the Group had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Within one year | 1,113 | 1,113 | — |
| In the second to fifth year inclusive | 1,113 | — | — |
| | 2,226 | 1,113 | — |

Operating lease payments represent rentals payable by the Group for certain of its stores and office premises. Leases are negotiated for an average term of two years and rentals are fixed for an average term of two years.

**The Group as lessor**

Property rental income earned during three years ended 31 December 2007, 2008 and 2009 was RMB1,642,000, RMB1,642,000 and RMB1,642,000, respectively. The Group's properties held for rental purposes generate rental yields of 7.16%, 7.46% and 7.78% as at 31 December 2007, 2008 and 2009, respectively. All of the properties held have committed tenant, YLF Leathercover, for the next two years, one year and three months at 31 December 2007, 2008 and 2009, respectively.

At the end of each reporting periods, the Group has contracted with YLF Leathercover for the following future minimum lease payments:

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Within one year | 1,642 | 1,642 | 410 |
| In the second to fifth year inclusive | 1,642 | — | — |
| | 3,284 | 1,642 | 410 |

## 29. CAPITAL COMMITMENTS

| | At 31 December | | |
|---|---|---|---|
| | 2007 | 2008 | 2009 |
| | RMB'000 | RMB'000 | RMB'000 |
| Capital expenditure contracted for but not provided in the Financial Information in respect of: | | | |
| Acquisition of property, plant and equipment | 48,715 | 7,064 | 83,403 |
| Acquisition of additional interest in subsidiaries from minority interests | — | 2,150 | — |
| | 48,715 | 9,214 | 83,403 |

## II. DIRECTORS' REMUNERATION

Save as disclosed in note 14 to the Financial Information, no remuneration has been paid or payable by the group entities or any of the subsidiaries in respect of the Track Record Period.

## III. EVENTS AFTER THE END OF THE REPORTING PERIOD

On 14 January 2010, the Company and Smart Port entered into a share transfer agreement pursuant to which Smart Port transferred its entire interest in Xi Yuan BVI to the Company in consideration of the Company issuing 9,999 shares credited as fully paid to Smart Port.

On 30 April 2010, shareholders' resolutions were passed to approve the matters set out in the paragraph headed "Written resolutions of our Shareholders passed on 30 April 2010" in Appendix VI to the Prospectus, which mainly includes:

(a) The authorised share capital of the Company was increased from 3,800,000 shares to 10,000,000,000 shares by the creation of 9,996,200,000 shares with par value of HK$0.10 each.

(b) Conditional on the share premium account of the Company being credited as a result of the proposed listing of the shares of the Company on the Stock Exchange, the sum of HK$74,999,000 be capitalised and be applied in paying up in full at par 749,990,000 shares for allotment and issue to the shareholders whose names were on the register of members of our Company as of the close of business on 30 April 2010.

On 5 May 2010, amount due to immediate holding company, Smart Port, amounted to RMB139,950,000 on that date (including RMB95,605,000 as of 31 December 2009) was waived by Smart Port. Such amount is accounted for as contribution from a shareholder.

## IV. SUBSEQUENT FINANCIAL STATEMENTS

No audited financial statements of the Group, the Company or any of its subsidiaries have been prepared in respect of any period subsequent to 31 December 2009.

Yours faithfully,
**Deloitte Touche Tohmatsu**
*Certified Public Accountants*
Hong Kong

## A. UNAUDITED PRO FORMA ADJUSTED NET TANGIBLE ASSETS

For illustration purpose only, the following statement of unaudited pro forma adjusted combined net tangible assets of the Group is set out here to illustrate the effect of the Global Offering on the combined net tangible assets attributable to owners of the Company as if it had taken place on 31 December 2009 and based on the audited combined net tangible assets attributable to owners of the Company as of 31 December 2009 as shown in the accountants' report, the text of which is set out in Appendix I to this prospectus, and adjusted as follows:

| | Audited combined net tangible assets of the Group attributable to owners of the Company as of 31 December 2009 | Estimated net proceeds from the Global Offering(1) | Unaudited pro forma adjusted combined net tangible assets of the Group attributable to owners of our Company | Unaudited pro forma adjusted net tangible assets per Share(2)(3) | |
|---|---|---|---|---|---|
| | RMB'000 | RMB'000 | RMB'000 | RMB(2) | HK$(3) |
| Based on an Offer Price of HK$ 2.58 per Offer Share . . | 554,847 | 524,360 | 1,079,207 | 1.08 | 1.23 |
| Based on an Offer Price of HK$ 3.38 per Offer Share . . | 554,847 | 692,684 | 1,247,531 | 1.25 | 1.42 |

*Notes:*

(1) The estimated net proceeds from the Global Offering are based on 250,000,000 new Shares at the indicative Offer Price of HK$2.58 and HK$3.38 per Offer Share, respectively, after deduction of the underwriting fees and other related expenses payable by the Company (excluding other related expenses of approximately RMB12.6 million which have been paid or accrued as of 31 December 2009). No account has been taken of the Shares that may be issued pursuant to any exercise of Over-allotment Option.

(2) The unaudited pro forma adjusted net tangible assets per Share is based on 1,000,000,000 Shares expected to be in issue immediately following completion of the Global Offering. No account has been taken of the Shares that may be issued pursuant to any exercise of Over-allotment Option.

(3) The unaudited pro forma adjusted net tangible assets per Share is translated into Hong Kong dollar at an exchange rate of RMB0.87898 to HK$1.00, the rate of The People's Bank of China prevailing on 6 May 2010. No representation is made that the Renminbi amounts have been, could have been or may be converted to Hong Kong dollars, or vice versa, at that rate.

(4) By comparing the valuation of the Group's property interests of RMB539.3 million as set out in Appendix IV to this prospectus and the unaudited net book value of these properties including buildings held for own use, investment properties and prepaid lease payments of RMB539.8 million as of 28 February 2010, there is net valuation deficit of approximately RMB0.5 million. Accordingly, there is no additional annual depreciation expense.

## B. UNAUDITED PRO FORMA FORECAST EARNINGS PER SHARE

The following unaudited pro forma forecast earnings per share for the six months ending 30 June 2010 has been prepared on the basis of the notes set out below for the purpose of illustrating the effect of the Global Offering as if it had taken place on 1 January 2010. This unaudited pro forma forecast earnings per share has been prepared for illustrative purpose only and because of its nature, it may not give a true picture of the financial results of the Group following the Global Offering.

| | |
|---|---|
| Forecast combined profit attributable to owners of the Company for the six months ending 30 June 2010[(1)(3)] | Not less than RMB82 million |
| Unaudited pro forma forecast earnings per Share[(2)(3)] | Not less than RMB0.08 (approximately HK$0.09) |

*Notes:*

(1) The bases on which the above profit forecast for the six months ending 30 June 2010 has been prepared are summarised in Appendix III to this prospectus. The forecast combined profit attributable to owners of the Company for the six months period ending 30 June 2010 prepared by the Directors is based on the unaudited management accounts for the two months ended 28 February 2010 and a forecast of the combined results of the Group for the remaining four months ending 30 June 2010.

(2) The unaudited pro forma forecast earnings per share is calculated by dividing the forecast combined profit attributable to owners of the Company for the six months ending 30 June 2010 by a total of 1,000,000,000 shares, assuming that the share in issue as at 14 January 2010 and the shares to be issued under the Capitalisation Issue and Global Offering had been completed on 1 January 2010 (without taking into account the Over-allotment Option).

(3) The pro forma forecast earnings per Share is translated into HK$ at an exchange rate of RMB0.87898 to HK$1.00, the rate of The People's Bank of China prevailing on 6 May 2010. No representation is made that the Renminbi amounts have been, could have been or may be converted to Hong Kong dollars, or vice versa, at that rate.

## C. ACCOUNTANTS' REPORT ON UNAUDITED PRO FORMA FINANCIAL INFORMATION RELATING TO THE UNAUDITED PRO FORMA ADJUSTED NET TANGIBLE ASSETS AND UNAUDITED PRO FORMA FORECAST EARNINGS PER SHARE

Deloitte.
德勤

德勤・關黃陳方會計師行
香港金鐘道88號
太古廣場一座35樓

Deloitte Touche Tohmatsu
35/F One Pacific Place
88 Queensway
Hong Kong

**ACCOUNTANTS' REPORT ON UNAUDITED PRO FORMA FINANCIAL INFORMATION TO THE DIRECTORS OF YOUYUAN INTERNATIONAL HOLDINGS LIMITED**

We report on the unaudited pro forma financial information of Youyuan International Holdings Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group"), which has been prepared by the directors of the Company for illustrative purposes only, to provide information about how the proposed global offering might have affected the financial information presented, for inclusion in Appendix II to the prospectus dated 14 May 2010 (the "Prospectus"). The basis of preparation of the unaudited pro forma financial information is set out on pages II-1 and II-2 to the Prospectus.

**Respective responsibilities of directors of the Company and reporting accountants**

It is the responsibility solely of the directors of the Company to prepare the unaudited pro forma financial information in accordance with paragraph 29 of Chapter 4 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and with reference to Accounting Guideline 7 "Preparation of Pro Forma Financial Information for Inclusion in Investment Circulars" issued by the Hong Kong Institute of Certified Public Accountants.

It is our responsibility to form an opinion, as required by paragraph 29(7) of Chapter 4 of the Listing Rules, on the unaudited pro forma financial information and to report our opinion to you. We do not accept any responsibility for any reports previously given by us on any financial information used in the compilation of the unaudited pro forma financial information beyond that owed to those to whom those reports were addressed by us at the dates of their issue.

**Basis of opinion**

We conducted our engagement in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 300 "Accountants' Reports on Pro Forma Financial Information in Investment Circulars" issued by the Hong Kong Institute of Certified Public Accountants. Our work consisted primarily of comparing the unadjusted financial information with source documents, considering the evidence supporting the adjustments and discussing the unaudited pro forma financial information with the directors of the Company. This engagement did not involve independent examination of any of the underlying financial information.

We planned and performed our work so as to obtain the information and explanations we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the unaudited pro forma financial information has been properly compiled by the directors of the Company on the basis stated, that such basis is consistent with the accounting policies of the Group and that the adjustments are appropriate for the purpose of the unaudited pro forma financial information as disclosed pursuant to paragraph 29(1) of Chapter 4 of the Listing Rules.

Our work has not been carried out in accordance with the auditing standards or other standards and practices generally accepted in the United States of America or auditing standards of the Public Company Accounting Oversight Board (United States) and accordingly should not be relied upon as if it has been carried out in accordance with those standards.

The unaudited pro forma financial information is for illustrative purpose only, based on the judgements and assumptions of the directors of the Company, and, because of its hypothetical nature, does not provide any assurance or indication that any event will take place in future and may not be indicative of:

- the financial position of the Group as at 31 December 2009 or any future date; or
- the earnings per share of the Group for the six months ending 30 June 2010 or any future period.

**Opinion**

In our opinion:

a) the unaudited pro forma financial information has been properly compiled by the directors of the Company on the basis stated;

b) such basis is consistent with the accounting policies of the Group; and

c) the adjustments are appropriate for the purposes of the unaudited pro forma financial information as disclosed pursuant to paragraph 29(1) of Chapter 4 of the Listing Rules.

**Deloitte Touche Tohmatsu**
*Certified Public Accountants*
Hong Kong
14 May 2010

*The forecast of the combined profit attributable to equity holders of our Company for the six months ending 30 June 2010 is set out in the section headed "Management's Discussion and Analysis of Financial Condition and Result of Operations — Profit Forecast for the Six Months Ending 30 June 2010" in this prospectus. The Company undertakes that the interim report for the six months ending 30 June 2010 will be audited pursuant to Rule 11.18 of the Listing Rules.*

## (A) BASES AND ASSUMPTIONS

Our Directors have prepared the forecast of the combined profit attributable to owners of our Company for the six months ending 30 June 2010 based on the unaudited management accounts for the two months ended 28 February 2010 and a forecast of the combined results of the Group for the remaining four months ending 30 June 2010. The forecast has been prepared on the basis of the accounting policies consistent in all material respects with those currently adopted by our Group as set out in Note 3 of "Appendix I — Accountants' Report" to this prospectus and is based on the following principal assumptions:

(a) there will be no significant changes in existing political, legal, fiscal, market or economic conditions in the PRC, including changes in legislation, regulations, or rules, which may have a material adverse effect on the Group's income;

(b) there will be no significant changes in the government policies in the PRC in which we operate including, but not limited to, those in relation to paper industry, which may adversely affect the Group's business or operations;

(c) there will be no material changes in the inflation rate, interest rates or foreign currency exchange rates in the PRC;

(d) there will be no material change in the bases or rates of taxation, both direct and indirect, in the PRC;

(e) the Group's operations and business will not be severely interrupted by any force majeure events or unforeseeable factors or any unforeseeable reasons that are beyond the control of the Directors, including the occurrence of natural disasters or catastrophes (such as floods and typhoons), epidemics or serious accidents;

(f) there will be no material impacts of subsequent revisions of the accounting standards, which the Group currently adopted for preparation of the Group's financial statements, to the Group's financial reporting;

(g) there will be no material change in the Group's dividend policy. The Group might or might not declare dividend in the future. The timing, amount and form of future dividends, if any, will mainly depend on our results of operations and cash flows, our future prospects, general business conditions and our capital requirements and surplus;

(h) There will be no significant changes in the Group's expansion plans of business; and

(i) There will be no material change in the timing of global offering.

**(B) LETTERS**

(i) *Letter from Deloitte Touche Tohmatsu*

*The following is the text of a letter, prepared for inclusion in this prospectus, received by the Directors and the Sole Sponsor from the Company's reporting accountants, Deloitte Touche Tohmatsu, Certified Public Accountants, Hong Kong, in connection with the forecast of the Group's combined profit attributable to owners of the Company for the six months ending 30 June 2010.*

**Deloitte.**
**德勤**

德勤・關黃陳方會計師行
香港金鐘道88號
太古廣場一座35樓

Deloitte Touche Tohmatsu
35/F One Pacific Place
88 Queensway
Hong Kong

14 May 2010

The Directors
Youyuan International Holdings Limited
The Hongkong and Shanghai Banking Corporation Limited

Dear Sirs,

We have reviewed the accounting policies adopted and calculations made in arriving at the forecast of the combined profit of Youyuan International Holdings Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group") for the six months ending 30 June 2010 attributable to owners of the Company (the "Forecast"), for which the directors of the Company are solely responsible, as set out in the prospectus dated 14 May 2010 (the "Prospectus") issued by the Company. The Forecast is prepared based on the unaudited management accounts for the two months ended 28 February 2010 and a forecast of the combined results of the Group for the remaining four months ending 30 June 2010.

In our opinion, the Forecast, so far as the accounting policies and calculations are concerned, has been properly compiled on the basis of the assumptions made by the directors of the Company as set out in "Bases and assumptions" of Appendix III to the Prospectus and is presented on a basis consistent in all material respects with the accounting policies normally adopted by the Group as set out in our accountants' report of the financial information on the Group for the three years ended 31 December 2009 as set out in Appendix I to the Prospectus.

Yours faithfully,
**Deloitte Touche Tohmatsu**
*Certified Public Accountants*
Hong Kong

(ii) *Letter from the Sole Sponsor*

*The following is text of a letter prepared by the Sole Sponsor, for the purpose of incorporation in this prospectus, in connection with the forecast of the consolidated profit attributable to the shareholders of the Company for the six months ending 30 June 2010.*

HSBC

**The Hongkong and Shanghai Banking Corporation Limited**
HSBC Main Building
1 Queen's Road Central
Hong Kong

The Directors
Youyuan International Holdings Limited

14 May 2010

Dear Sirs,

We refer to the forecast (the "Forecast") of the consolidated profit attributable to the equity shareholders of Youyuan International Holdings Limited (the "Company") and its subsidiaries (the "Group") for the six months ending 30 June 2010 (the "Profit Forecast") as set out in the prospectus issued by the Company dated 14 May 2010 (the "Prospectus").

The Profit Forecast for which the directors of the Company are solely responsible has been prepared by them based on the unaudited management accounts for the two months ended 28 February 2010 and a forecast of the combined results of the Group for the remaining four months ending 30 June 2010.

We have discussed with you the bases and assumptions made by the directors of the Company as set out in Appendix III to the Prospectus upon which the Profit Forecast has been made. We have also considered, and relied upon, the letter dated 14 May 2010 addressed to yourselves and ourselves from Deloitte Touche Tohmatsu regarding the accounting policies, calculations and assumptions upon which the Profit Forecast has been made.

On the basis of the information comprising the Profit Forecast and on the basis of the accounting policies and calculations adopted by you and reviewed by Deloitte Touche Tohmatsu, we are of the opinion that the Profit Forecast, for which you as the directors of the Company are solely responsible, has been made after due and careful enquiry.

Yours faithfully,

For and on behalf of
**The Hongkong and Shanghai Banking Corporation Limited**

**Ivan So**
**Managing Director, Global Banking**

*The following is the text of a letter, summary of values and valuation certificates, prepared for the purpose of incorporation in this prospectus received from Jones Lang LaSalle Sallmanns Limited, an independent valuer, in connection with its valuation as at 28 February 2010 of the property interests of the Group.*

Jones Lang LaSalle Sallmanns Limited
17/F Dorset House Taikoo Place
979 King's Road Quarry Bay Hong Kong
tel +852 2169 6000 fax +852 2169 6001
Licence No: C-030171

14 May 2010

The Board of Directors
Youyuan International Holdings Limited
Cricket Square
Hutchins Drive
PO Box 2681
Grand Cayman
KYI-1111
Cayman Islands

Dear Sirs,

In accordance with your instructions to value the properties in which Youyuan International Holdings Limited (the "Company") and its subsidiaries (hereinafter together referred to as the "Group") have interests in the People's Republic of China (the "PRC"), we confirm that we have carried out inspections, made relevant enquiries and searches and obtained such further information as we consider necessary for the purpose of providing you with our opinion of the capital values of the property interests as at 28 February 2010 (the "date of valuation").

Our valuation of the property interests represents the market value which we would define as intended to mean "the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently, and without compulsion".

We have valued the interests of property nos. 4 to 6 in Group II by direct comparison approach assuming sale of the properties in their existing state with the benefit of immediate vacant possession and by making reference to comparable sales transactions as available in the relevant market.

Where, due to the nature of the buildings and structures of property nos. 1, 3 and Part A and Part C of property no. 2 in Group I and the particular locations in which they are situated, there are unlikely to be relevant market comparable sales readily available and the property interests have therefore been valued on the basis of their depreciated replacement cost.

Depreciated replacement cost is defined as “the current cost of replacing an asset with its modern equivalent asset less deductions for physical deterioration and all relevant forms of obsolescence and optimisation.” It is based on an estimate of the market value for the existing use of the land, plus the current cost of replacement (reproduction) of the improvements, less deductions for physical deterioration and all relevant forms of obsolescence and optimisation. The depreciated replacement cost of the property interest is subject to adequate potential profitability of the concerned business.

We have attributed no commercial value to the property interest in Group IV, which is leased by the Group, due either to the short-term nature of the lease or the prohibition against assignment or sub-letting or otherwise due to the lack of substantial profit rent.

In valuing the remaining portion (Part B) of property no. 2 in Group I and property no. 7 in Group III which are currently under construction, we have assumed that they will be developed and completed in accordance with the latest development proposal provided to us by the Group. In arriving at our opinion of value, we have taken into account the construction cost and professional fees relevant to the stage of construction as at the date of valuation and the remainder of the cost and fees to be expended to complete the development.

Our valuation has been made on the assumption that the seller sells the property interests in the market without the benefit of a deferred term contract, leaseback, joint venture, management agreement or any similar arrangement, which could serve to affect the values of the property interests.

No allowance has been made in our report for any charge, mortgage or amount owing on any of the property interests valued nor for any expense or taxation which may be incurred in effecting a sale. Unless otherwise stated, it is assumed that the properties are free from encumbrances, restrictions and outgoings of an onerous nature, which could affect their values.

In valuing the property interests, we have complied with all requirements contained in Chapter 5 and Practice Note 12 of the Rules Governing the Listing of Securities issued by The Stock Exchange of Hong Kong Limited; the RICS Valuation Standards (6th Edition) published by the Royal Institution of Chartered Surveyors; and the HKIS Valuation Standards on Properties (1st Edition 2005) published by the Hong Kong Institute of Surveyors.

We have relied to a very considerable extent on the information given by the Group and have accepted advice given to us on such matters as tenure, planning approvals, statutory notices, easements, particulars of occupancy, lettings, and all other relevant matters.

We have been provided with tenancy agreement relating to the property interest in Group IV and have caused searches to be made at the Hong Kong Land Registry. However, we have not searched the original documents to verify the ownership or to ascertain any amendment.

We have been shown copies of various title documents including State-owned Land Use Rights Certificates, Building Ownership Certificates and official plans relating to the property interests and have made relevant enquiries. Where possible, we have examined the original documents to verify the existing title to the property interests in the PRC and any material encumbrance that might be attached to the property interests or any tenancy amendment. We have relied considerably on the advice given by the Company's PRC legal advisers — King & Wood, concerning the validity of the property interests in the PRC.

We have not carried out detailed measurements to verify the correctness of the areas in respect of the properties but have assumed that the areas shown on the title documents and official site plans handed to us are correct. All documents and contracts have been used as reference only and all dimensions, measurements and areas are approximations. No on-site measurement has been taken.

We have inspected the exterior and, where possible, the interior of the properties. However, we have not carried out investigation to determine the suitability of the ground conditions and services for any development thereon. Our valuation has been prepared on the assumption that these aspects are satisfactory and that no unexpected cost and delay will be incurred during construction. Moreover, no structural survey has been made, but in the course of our inspection, we did not note any serious defect. We are not, however, able to report whether the properties are free of rot, infestation or any other structural defect. No tests were carried out on any of the services.

We have had no reason to doubt the truth and accuracy of the information provided to us by the Group. We have also sought confirmation from the Group that no material factors have been omitted from the information supplied. We consider that we have been provided with sufficient information to arrive an informed view, and we have no reason to suspect that any material information has been withheld.

Unless otherwise stated, all monetary figures stated in this report are in Renminbi (RMB).

Our valuation is summarized below and the valuation certificates are attached.

Yours faithfully,
for and on behalf of
**Jones Lang LaSalle Sallmanns Limited**
**Paul L. Brown**
*B.Sc. FRICS FHKIS*
*Director*

*Note:* Paul L. Brown is a Chartered Surveyor who has 27 years' experience in the valuation of properties in the PRC and 30 years of property valuation experience in Hong Kong and the United Kingdom, as well as relevant experience in the Asia-Pacific region, France and Germany.

## SUMMARY OF VALUES

**Group I — Property interests held and occupied by the Group in the PRC**

| No. | Property | Capital value in existing state as at 28 February 2010<br>*RMB* | Interest attributable to the Group | Capital value attributable to the Group as at 28 February 2010<br>*RMB* |
|---|---|---|---|---|
| 1. | 10 parcels of land, various buildings and structures located at Xibin Farm Industrial Zone Xibin Town Jinjiang City Fujian Province The PRC | 106,354,000 | 100% | 106,354,000 |
| 2. | 6 parcels of land, various buildings and structures located at Xibin Farm Industrial Zone Xibin Town Jinjiang City Fujian Province The PRC | 161,643,000 | 100% | 161,643,000 |
| 3. | 3 parcels of land, various buildings and structures located at Wuzhai Village Jiaomei Town Longhai City Fujian Province The PRC | 134,660,000 | 100% | 134,660,000 |
| | **Sub-total:** | **402,657,000** | | **402,657,000** |

**Group II — Property interests held for future development by the Group in the PRC**

| No. | Property | Capital value in existing state as at 28 February 2010 *RMB* | Interest attributable to the Group | Capital value attributable to the Group as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| 4. | A parcel of land located at Xibin Farm Industrial Zone Xibin Town Jinjiang City Fujian Province The PRC | 472,000 | 100% | 472,000 |
| 5. | 4 parcels of land located at Xibin Farm Industrial Zone Xibin Town Jinjiang City Fujian Province The PRC | 40,137,000 | 100% | 40,137,000 |
| 6. | 4 parcels of land located at Wuzhai Village Jiaomei Town Longhai City Fujian Province The PRC | 36,028,000 | 100% | 36,028,000 |
| | **Sub-total:** | **76,637,000** | | **76,637,000** |

**Group III — Property interest held under development by the Group in the PRC**

| No. | Property | Capital value in existing state as at 28 February 2010 *RMB* | Interest attributable to the Group | Capital value attributable to the Group as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| 7. | 2 parcels of land and 3 industrial buildings under construction located at Wuzhai Village Jiaomei Town Longhai City Fujian Province The PRC | 30,007,000 | 100% | 30,007,000 |
| | **Sub-total:** | **30,007,000** | | **30,007,000** |

**Group IV — Property interest leased and occupied by the Group in Hong Kong**

| No. | Property | Capital value in existing state as at 28 February 2010 *RMB* |
|---|---|---|
| 8. | Unit 4 on 13th Floor Bank of America Tower No. 12 Harcourt Road Hong Kong | No commercial value |
| | **Sub-total:** | Nil |

| | Capital value in existing state as at 28 February 2010 *RMB* | Capital value attributable to the Group as at 28 February 2010 *RMB* |
|---|---|---|
| **Grand total:** | 509,301,000 | 509,301,000 |

## VALUATION CERTIFICATE

**Group I — Property interests held and occupied by the Group in the PRC**

| No. | Property | Description and tenure | Particulars of occupancy | Capital value in existing state as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| 1. | 10 parcels of land, various buildings and structures located at Xibin Farm Industrial Zone Xibin Town Jinjiang City Fujian Province The PRC | The property comprises 10 parcels of land with a total site area of approximately 81,164 sq.m. and 53 buildings and various ancillary structures erected thereon which were completed in various stages between 1993 and 2004. ("**Part A**") | Part A of the property is currently occupied by the Group for production, storage, office, staff quarters and ancillary purposes except for portions with a total gross floor area of approximately 5,825.28 sq.m. which are currently occupied by a tenant (please refer to note 11), whilst, Part B of the property is currently occupied by the Group for storage and ancillary purposes. | 106,354,000<br><br>100% interest attributable to the Group: RMB106,354,000 |

The buildings of Part A have a total gross floor area of approximately 65,339.428 sq.m. and the details of uses and their respective gross floor areas are set out as follows:

| **Use** | **No. of Item** | **Gross Floor Area** *(sq.m.)* |
|---|---:|---:|
| Production | 19 | 26,799.325 |
| Office | 3 | 3,535.501 |
| Canteen | 1 | 810 |
| Staff quarters | 5 | 9,723.051 |
| Warehouse | 11 | 19,823.131 |
| Ancillary | 14 | 4,648.42 |
| **Total** | 53 | 65,339.428 |

The structures of Part A mainly include boundary fences, roads, sewage tanks, bleaching tanks, sedimentation tanks and gates.

The land use rights of Part A of the property have been granted for terms of 50 years with the expiry dates between 28 August 2050 and 28 August 2056 for industrial use.

In addition to Part A, the property also comprises 2 warehouses and an ancillary building with a total gross floor area of approximately 1,014 sq.m. which are adjacent to Part A. ("**Part B**")

The buildings of Part B are located outside the land parcels of Part A and have not obtained any title certificates.

*Notes:*

1. Pursuant to 2 Land Use Rights Transfer Agreements dated 20 June 2007 entered into between Fujian Jinjiang Youlanfa Paper Company Limited ("Youlanfa", a wholly-owned subsidiary of the Company) and Fujian Youlanfa Group Industry Company Limited (福建優蘭發集團實業有限公司) ("YLF Industry", a connected party to the Company), the land use rights of 2 parcels of land with a total site area of approximately 8,549 sq.m. were contracted to be transferred to Youlanfa at a total consideration of RMB2,482,300.

2. Pursuant to a Land Use Rights Transfer Agreement dated 6 July 2009 entered into between Youlanfa and YLF Industry, the land use rights of a parcel of land with a site area of approximately 6,525 sq.m. and various buildings erected thereon with a total gross floor area of approximately 9,890 sq.m. were contracted to be transferred to Youlanfa at a total consideration of RMB10,222,000.

3. Pursuant to a Land Use Rights Transfer Agreement dated 6 July 2009 entered into between Youlanfa and Jinjiang Youlanfa Vapour Equipment Company Limited (晉江優蘭發水汽設備有限公司) (a connected party to the Company), the land use rights of a parcel of land with a site area of approximately 6,480 sq.m. and various buildings erected thereon with a total gross floor area of approximately 4,194.94 sq.m. were contracted to be transferred to Youlanfa at a total consideration of RMB9,041,000.

4. Pursuant to an Asset Transfer Agreement dated 25 August 2009 entered into between Youlanfa and Fujian Youlanfa Leathercover Paper Company Limited ("YLF Leathercover", a connected party to the Company), the land use rights of a parcel of land with a site area of approximately 15,432 sq.m. and various buildings and structures erected thereon with a total gross floor area of approximately 5,825.28 sq.m. together with 3 sets of equipment were contracted to be transferred to Youlanfa at a total consideration of RMB40,000,000.

5. Pursuant to 10 State-owned Land Use Rights Certificates - Jin Guo Yong (2006) Di Nos. 01061, 01062, 01064, 01068, 01070, Jin Guo Yong (2007) Di Nos. 00951, 00952 and Jin Guo Yong (2009) Di Nos. 00747 to 00749, the land use rights of 10 parcels of land with a total site area of approximately 81,164 sq.m. have been granted to Youlanfa for terms of 50 years with the expiry dates between 28 August 2050 and 28 August 2056 for industrial use.

6. Pursuant to a Building Ownership Certificate - Jin Fang Quan Zheng Xi Bin Zi Di No. 001603, 7 buildings with a total gross floor area of approximately 10,804.01 sq.m. are owned by Youlanfa.

7. Pursuant to a Building Ownership Certificate - Jin Fang Quan Zheng Xi Bin Zi Di No. 001601, 38 buildings with a total gross floor area of approximately 42,711.418 sq.m. and portions of 8 buildings with a total gross floor area of approximately 10,204.674 sq.m. are owned by Youlanfa.

   As advised by the Group, the aforesaid 8 buildings have a total gross floor area of approximately 11,824 sq.m. which consists of portions of approximately 10,204.674 sq.m. with building ownership certificate and the remaining portions of approximately 1,619.326 sq.m. without relevant title certificates which are located outside the land parcels of the property.

8. For the remaining buildings of Part B of the property with a total gross floor area of approximately 1,014 sq.m., we have not been provided with any title certificates.

   As advised by the Group, the buildings of Part B are located outside the land parcels of the property.

9. Pursuant to a Mortgage Contract of Maximum Amount - No. FJ310622010114-DY dated 26 April 2010, the land use rights of 2 parcels of land of the property with a total site area of approximately 13,005 sq.m. under the State-owned Land Use Rights Certificates - Jin Guo Yong (2009) Di Nos. 00748 and 00749 and various buildings erected thereon with a total gross floor area of approximately 10,804.01 sq.m. under the Building Ownership Certificate - Jin Fang

Quan Zheng Xi Bin Zi Di No. 001603 are subject to a mortgage in favour of Bank of China Limited Jinjiang Branch (the "Bank"), as security to guarantee the principal obligation under a series of contracts entered into between the Bank and Youlanfa for a maximum amount of RMB19,794,000 with the security term from 14 May 2009 to 12 April 2013.

10. Pursuant to a Mortgage Contract of Maximum Amount - No. FJ31062201038-DY dated 12 April 2010, the land use rights of 8 parcels of land of the property under the State-owned Land Use Rights Certificates - Jin Guo Yong (2006) Di Nos. 01061, 01062, 01064, 01068, 01070, Jin Guo Yong (2007) Di Nos. 00951, 00952 and Jin Guo Yong (2009) Di No. 00747 and various buildings erected thereon under the Building Ownership Certificate - Jin Fang Quan Zheng Xi Bin Zi Di No. 001601 together with the land use rights of a parcel of land of property no. 4 with a site area of approximately 1,169 sq.m. are subject to a mortgage in favour of the Bank, as security to guarantee the principal obligation under a series of contracts entered into between the Bank and Youlanfa for a maximum amount of RMB74,000,000 with the security term with the security term from 12 April 2010 to 12 April 2012.

11. According to a Tenancy Agreement dated 1 January 2010 entered into between Youlanfa and YLF Leathercover, portions of the land parcels of the property with a total site area of approximately 15,647 sq.m. and 14 buildings of the property with a total gross floor area of approximately 20,907.84 sq.m. erected thereon are rented to YLF Leathercover for a term commencing from 1 January 2010 and expiring on 31 March 2010 at a monthly rent of RMB136,820 exclusive of management fees, water and electricity charges.

    As advised by the Company, the Tenancy Agreement was expired on 31 March 2010 and has not been renewed till the latest practicable date.

12. According to a Tenancy Agreement dated 1 October 2009 entered into between Youlanfa and YLF Leathercover, a parcel of land of the property with a site area of approximately 15,432 sq.m., 8 buildings of the property with a total gross floor area of approximately 5,825.28 sq.m. and various structures erected thereon are rented to YLF Leathercover for a term commencing from 1 October 2009 and expiring on 31 May 2010 at a monthly rent of RMB82,000 exclusive of management fees, water and electricity charges.

13. In the valuation of this property, we have attributed no commercial value to the buildings of Part B of the property with a total gross floor area of approximately 1,014 sq.m. (as mentioned in note 8) without proper title certificates and 8 buildings of Part A of the property with a total gross floor area of approximately 11,824 sq.m. (as mentioned in note 7) which have not fully obtained the relevant title certificates. However, for reference purpose, we are of the opinion that the aggregate depreciated replacement cost of the buildings (excluding the land) as at the date of valuation would be RMB14,592,000 assuming all relevant title certificates have been fully obtained and the buildings could be freely transferred.

14. We have been provided with a legal opinion regarding the property interest by the Company's PRC legal advisers, which contains, *inter alia*, the following:

    a. The Group has fully paid up the land premium of the property and legally obtained the land use rights of the property and the ownership rights of the buildings mentioned in notes 5 to 7 except for the portions of the 8 buildings with a total gross floor area of approximately 1,619.326 sq.m. which have not obtained the relevant title certificates as mentioned in note 7;

    b. Subject to note 14(c) below, the Group has the rights to occupy, use, lease, transfer, mortgage or otherwise dispose of the land use rights and the buildings mentioned in note 14(a) in accordance with the PRC laws;

    c. For the land use rights and the ownership rights of the buildings which are subject to mortgages mentioned above, the Group should obtain prior written consent from the mortgagee when transferring, re-mortgaging or otherwise disposing of such land use rights and ownership rights of the buildings;

d. Except for the aforesaid mortgages, the land use rights of the property are not subject to any restrictions arising from any other mortgage, sequestration or any third parties rights; and

e. According to 2 Confirmation Letters dated 12 January 2010 and 13 January 2010 issued by the People's Government of Xibin Town and Jinjiang Planning Construction and Building Administration Bureau respectively, Youlanfa could continue using the buildings or portions of the buildings which are located outside the land parcels of the property mentioned above and would neither be ordered to demolish such buildings or portions of buildings nor subject to any penalty.

   According to the aforesaid Confirmation Letters, it is of little probability that such buildings or portions of buildings will be ordered to be demolished within a definite time although the Group cannot legally occupy, use, lease, transfer or otherwise dispose of such buildings or portions of buildings.

## VALUATION CERTIFICATE

| No. | Property | Description and tenure | Particulars of occupancy | Capital value in existing state as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| 2. | 6 parcels of land, various buildings and structures located at Xibin Farm Industrial Zone Xibin Town Jinjiang City Fujian Province The PRC | The property comprises 6 parcels of land with a total site area of approximately 131,243 sq.m. and 24 buildings and various ancillary structures erected thereon which were completed in various stages between 2006 and 2010. ("**Part A**") | Part A is currently occupied by the Group for production, storage, office, staff quarters and ancillary purposes, Part B is currently under construction, whilst, Part C of the property is currently occupied by the Group for ancillary purpose. | 161,643,000<br><br>100% interest attributable to the Group: RMB161,643,000 |

The buildings of Part A have a total gross floor area of approximately 62,111.362 sq.m. and the details of uses and their respective gross floor areas are set out as follows:

| Use | No. of Item | Gross Floor Area *(sq.m.)* |
|---|---|---|
| Production | 8 | 18,162.7 |
| Office | 1 | 5,826.492 |
| Canteen | 1 | 2,059.322 |
| Staff quarters | 4 | 18,186.347 |
| Warehouse | 7 | 17,668.106 |
| Ancillary | 3 | 208.395 |
| **Total** | 24 | 62,111.362 |

The structures of Part A mainly include boundary fences, roads, sewage tanks, bleaching tanks, sedimentation tanks and gates.

The land use rights of Part A of the property have been granted for terms of 50 years with the expiry dates between 27 May 2055 and 20 July 2059 for industrial use.

In addition to Part A, the property also comprises 2 industrial buildings and a staff quarter which are being constructed on the land parcels of Part A. ("**Part B**")

Part B of the property is scheduled to be completed in August 2010. Upon completion, the buildings of Part B will have a total gross floor area of approximately 19,250.2 sq.m.

The total construction cost of Part B is estimated to be approximately RMB20,699,000, of which RMB16,201,100 had been paid up to the date of valuation.

| No. | Property | Description and tenure | Particulars of occupancy | Capital value in existing state as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| | | Besides Part A and Part B, the property also comprises 3 ancillary buildings with a total gross floor area of approximately 199.25 sq.m. which are adjacent to Part A. (“**Part C**”)<br><br>The buildings of Part C are located outside the land parcels of Part A and have not obtained any title certificates. | | |

*Notes:*

1. Pursuant to a Land Use Rights Transfer Agreement dated 25 May 2009 entered into between Quanzhou Huaxiang Paper Company Limited (“Huaxiang”, a wholly-owned subsidiary of the Company) and Fujian Youlanfa Group Industry Company Limited (“YLF Industry”, a connected party to the Company), the land use rights of 2 parcels of land of the property with a total site area of approximately 43,082 sq.m. and various buildings and structures erected thereon were contracted to be transferred to Huaxiang at a total consideration of RMB32,311,500.

2. Pursuant to a Land Use Rights Transfer Agreement dated 28 June 2007 entered into between Huaxiang and YLF Industry, the land use rights of various parcels of land with a total site area of approximately 81,879 sq.m. and various buildings and structures erected thereon were contracted to be transferred to Huaxiang at a total consideration of RMB61,409,250.

3. Pursuant to a State-owned Land Use Rights Grant Contract dated 1 August 2008 entered into between Quanzhou State-owned Land Resources and Building Administration Bureau and Huaxiang, the land use rights of a parcel of land with a site area of approximately 6,282 sq.m. of the property together with 3 parcels of land with a total site area of approximately 90,789 sq.m. of property no. 5 were contracted to be granted to Huaxiang for industrial use. The total land premium was RMB32,140,000.

4. Pursuant to 6 State-owned Land Use Rights Certificates - Jin Guo Yong (2009) Di Nos. 00750 to 00754 and 00712, the land use rights of 6 parcels of land with a total site area of approximately 131,243 sq.m. have been granted to Huaxiang for terms of 50 years with the expiry dates between 27 May 2055 and 20 July 2059 for industrial use.

5. Pursuant to 4 Building Ownership Certificates - Jin Fang Quan Zheng Xi Bin Zi Di Nos. 000320 to 000322 and 001605, 24 buildings with a total gross floor area of approximately 62,111.362 sq.m. are owned by Huaxiang.

6. For the remaining buildings of Part C of the property with a total gross floor area of approximately 199.25 sq.m., we have not been provided with any title certificates.

   As advised by the Group, the buildings of Part C are located outside the land parcels of the property.

7. Pursuant to 2 Mortgage Contracts of Maximum Amount - 2009 Nian Gao Di Zi Di Nos. 175 and 176-1 dated 15 September 2009, the land use rights of 3 parcels of land with a total site area of approximately 81,879 sq.m. under the State-owned Land Use Rights Certificates - Jin Guo Yong (2009) Di Nos. 00751 to 00753 and various buildings erected thereon under the Building Ownership Certificates - Jin Fang Quan Zheng Xi Bin Zi Di Nos. 000320 to 000322 are subject to mortgages in favour of China Merchants Bank Qianzhou Fengze Sub-Branch (“Bank A”), as security to guarantee the principal obligation under a series of contracts entered into between Bank A and Huaxiang for a total maximum amount of RMB83,100,000 with the security terms from 15 September 2009 to 14 September 2012.

8. Pursuant to a Mortgage Contract of Maximum Amount - 2009 Nian Gao Di Zi Di No. 176-2 dated 15 September 2009, the land use rights of a parcel of land with a site area of approximately 32,894 sq.m. under the State-owned Land Use Rights Certificate - Jin Guo Yong (2009) Di No. 00754 are subject to a mortgage in favour of Bank A, as security to guarantee the principal obligation under a series of contracts entered into between Bank A and Huaxiang for a maximum amount of RMB12,900,000 with the security term from 15 September 2009 to 14 September 2012.

9. Pursuant to a Mortgage Contract of Maximum Amount - No. FJ31062201039-DY dated 22 March 2010, the land use rights of a parcel of land of the property with a site area of approximately 6,282 sq.m. under the State-owned Land Use Rights Certificate - Jin Guo Yong (2009) Di No. 00712 together with the land use rights of 3 parcels of land of property no. 5 with a total site area of approximately 90,789 sq.m. are subject to a mortgage in favour of Bank of China Limited Jinjiang Branch ("Bank B"), as security to guarantee the principal obligation under a series of contracts entered into between Bank B and Huaxiang for a maximum amount of RMB71,347,000 with the security term from 22 March 2010 to 22 March 2012.

10. In the valuation of this property, we have attributed no commercial value to Part B of the property without construction permits and the buildings of Part C of the property with a total gross floor area of approximately 199.25 sq.m. (as mentioned in note 6) without proper title certificates. However, for reference purpose, we are of the opinion that the aggregate depreciated replacement cost of the buildings (excluding the land) as at the date of valuation would be RMB15,413,000 assuming all relevant title certificates and construction permits have been obtained and the buildings could be freely transferred.

11. We have been provided with a legal opinion regarding the property interest by the Company's PRC legal advisers, which contains, *inter alia*, the following:

    a. The Group has fully paid up the land premium of the property and legally obtained the land use rights and the ownership rights of the buildings mentioned in notes 4 and 5;

    b. Subject to note 11(c) below, the Group has the rights to occupy, use, lease, transfer, mortgage or otherwise dispose of the land use rights and buildings mentioned in note 11(a) in accordance with the PRC laws;

    c. For the land use rights of the property and the ownership rights of the buildings which are subject to mortgages mentioned above, the Group should obtain prior written consent from the mortgagee when transferring, re-mortgaging or otherwise disposing of such land use rights and ownership rights of the buildings;

    d. Except for the aforesaid mortgages, the land use rights of the property are not subject to any restrictions arising from any other mortgage, sequestration or any third parties rights; and

    e. According to 2 Confirmation Letters both dated 11 April 2010 issued by the People's Government of Xibin Town and Jinjiang Planning Construction and Building Administration Bureau respectively, Huaxiang could continue using the buildings which are located outside the land parcels of the property mentioned above and would neither be ordered to demolish such buildings nor subject to any penalty.

       According to the aforesaid Confirmation Letters, it is of little probability that such buildings will be ordered to be demolished within a definite time although the Group cannot legally occupy, use, lease, transfer or otherwise dispose of such buildings.

## VALUATION CERTIFICATE

| No. | Property | Description and tenure | Particulars of occupancy | Capital value in existing state as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| 3. | 3 parcels of land, various buildings and structures located at Wuzhai Village Jiaomei Town Longhai City Fujian Province The PRC | The property comprises 3 parcels of land with a total site area of approximately 83,774.84 sq.m. and 15 buildings and various ancillary structures erected thereon which were completed in various stages between 2007 and 2008. | The property is currently occupied by the Group for production, storage, office, residential and ancillary purposes. | 134,660,000<br><br>100% interest attributable to the Group: RMB134,660,000 |

The buildings have a total gross floor area of approximately 52,125.66 sq.m. and the details of uses and their respective gross floor areas are set out as follows:

| Use | No. of Item | Gross Floor Area *(sq.m.)* |
|---|---|---|
| Production | 5 | 19,088.01 |
| Office | 1 | 5,708.43 |
| Canteen | 1 | 2,042 |
| Staff quarters | 4 | 15,821.2 |
| Warehouse | 4 | 9,466.02 |
| **Total** | 15 | 52,125.66 |

The structures mainly include boundary fences, roads, sewage tanks, bleaching tanks, sedimentation tanks and gates.

The land use rights of the property have been granted for terms of 50 years all expiring on 5 March 2056 for industrial use.

*Notes:*

1. Pursuant to a Land Use Rights Transfer Agreement dated 18 January 2007 entered into between Fujian Xiyuan Paper Company Limited ("Xiyuan", a wholly-owned subsidiary of the Company) and Zhangzhou Huarong Paper Company Limited (漳州華榮紙業有限公司) (a connected party to the Company), the land use rights of 3 parcels of land with a total site area of approximately 83,774.84 sq.m. and various buildings and structures erected thereon were contracted to be transferred to Xiyuan at a total consideration of RMB18,849,339.

2. Pursuant to 3 State-owned Land Use Rights Certificates - Long Guo Yong (2009 Jiao Zi) Di Nos. GC0065 to GC0067, the land use rights of 3 parcels of land with a total site area of approximately 83,774.84 sq.m. have been granted to Xiyuan for terms of 50 years all expiring on 5 March 2056 for industrial use.

3. Pursuant to 3 Building Ownership Certificates - Long Fang Quan Zheng Zi Di Nos. 20093854 to 20093856, 15 buildings with a total gross floor area of approximately 52,125.66 sq.m. are owned by Xiyuan.

4. Pursuant to a Mortgage Contract of Maximum Amount - No. FJ31062201096-DY-1 dated 31 March 2010, the land use rights of 3 parcels of land of the property with a total site area of approximately 83,774.84 sq.m. under the State-owned Land Use Rights Certificates - Jin Guo Yong (2009) Di Nos. 00748 and 00749 and various buildings erected thereon with a total gross floor area of approximately 52,125.66 sq.m. under the Building Ownership Certificates - Long Fang Quan Zheng Zi Di Nos. 20093854 to 20093856 are subject to a mortgage in favour of Bank of China Limited Jinjiang Branch (the "Bank"), as security to guarantee the principal obligation under a series of contracts entered into between the Bank and Xiyuan for a maximum amount of RMB114,555,100 with the security term from 31 March 2010 to 31 March 2014.

5. We have been provided with a legal opinion regarding the property interest by the Company's PRC legal advisers, which contains, *inter alia*, the following:

   a. The Group has fully paid up the land premium of the property and legally obtained the land use rights and the ownership rights of the buildings mentioned in notes 2 and 3;

   b. Subject to note 5(c) below, the Group has the rights to occupy, use, lease, transfer, mortgage or otherwise dispose of the land use rights and buildings mentioned in note 5(a) in accordance with the PRC laws;

   c. For the land use rights of the property and the ownership rights of the buildings which are subject to mortgage mentioned above, the Group should obtain prior written consent from the mortgagee when transferring, re-mortgaging or otherwise disposing of such land use rights and ownership rights of the buildings; and

   d. Except for the aforesaid mortgage, the land use rights of the property are not subject to any restrictions arising from any other mortgage, sequestration or any third parties rights.

## VALUATION CERTIFICATE

**Group II — Property interests held for future development by the Group in the PRC**

| No. | Property | Description and tenure | Particulars of occupancy | Capital value in existing state as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| 4. | A parcel of land located at Xibin Farm Industrial Zone Xibin Town Jinjiang City Fujian Province The PRC | The property comprises a parcel of land with a site area of approximately 1,169 sq.m.<br><br>The land use rights of the property have been granted for a term of 50 years expiring on 16 August 2055 for industrial use. | The property is currently vacant. | 472,000<br><br>100% interest attributable to the Group: RMB472,000 |

*Notes:*

1. Pursuant to a State-owned Land Use Rights Certificate - Jin Guo Yong (2006) Di No. 00241, the land use rights of a parcel of land with a site area of approximately 1,169 sq.m. have been granted to Fujian Jinjiang Youlanfa Paper Company Limited ("Youlanfa", a wholly-owned subsidiary of the Company) for a term of 50 years expiring on 16 August 2055 for industrial use.

2. Pursuant to a Mortgage Contract of Maximum Amount - No. FJ31062201038-DY dated 12 April 2010, the land use rights of the property together with the land use rights of 8 parcels of land with a total site area of approximately 68,159 sq.m. of property no. 1 and various buildings erected thereon are subject to a mortgage in favour of Bank of China Limited Jinjiang Branch (the "Bank"), as security to guarantee the principal obligation under a series of contracts entered into between the Bank and Youlanfa for a maximum amount of RMB74,000,000 with the security term from 12 April 2010 to 12 April 2012.

3. We have been provided with a legal opinion regarding the property interest by the Company's PRC legal advisers, which contains, *inter alia*, the following:

   a. The Group has fully paid up the land premium of the property and legally obtained the land use rights of the property;

   b. Subject to note 3(c) below, the Group has the rights to occupy, use, lease, transfer, mortgage or otherwise dispose of the land use rights of the property in accordance with the PRC laws;

   c. For the land use rights which are subject to the mortgage mentioned above, the Group should obtain prior written consent from the mortgagee when transferring, re-mortgaging or otherwise disposing of such land use rights; and

   d. Except for the aforesaid mortgage, the property is not subject to any restrictions arising from any other mortgage, sequestration or any third parties rights.

## VALUATION CERTIFICATE

| No. | Property | Description and tenure | Particulars of occupancy | Capital value in existing state as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| 5. | 4 parcels of land located at Xibin Farm Industrial Zone Xibin Town Jinjiang City Fujian Province The PRC | The property comprises 4 parcels of land with a total site area of approximately 98,223.6 sq.m.<br><br>The land use rights of the property have been granted for terms of 50 years with the expiry dates between 27 May 2055 and 20 July 2059 for industrial use. | The property is currently vacant. | 40,137,000<br><br>100% interest attributable to the Group: RMB40,137,000 |

*Notes:*

1. Pursuant to a Land Use Rights Transfer Agreement dated 1 July 2009 entered into between Quanzhou Huaxiang Paper Company Limited ("Huaxiang", a wholly-owned subsidiary of the Company) and Fujian Youlanfa Leathercover Paper Company Limited (a connected party to the Company), the land use rights of a parcel of land of the property with a site area of approximately 7,434.6 sq.m. were contracted to be transferred to Huaxiang at a consideration of RMB5,546,000.

2. Pursuant to a State-owned Land Use Rights Grant Contract dated 1 August 2008 entered into between Quanzhou State-owned Land Resources and Building Administration Bureau and Huaxiang, the land use rights of 3 parcels of land with a total site area of approximately 90,789 sq.m. of the property together with a parcel of land with a site area of approximately 6,282 sq.m. of property no. 2 were contracted to be granted to Huaxiang for industrial use. The total land premium was RMB32,140,000.

3. Pursuant to 4 State-owned Land Use Rights Certificates - Jin Guo Yong (2009) Di Nos. 00755, 00709 to 00711, the land use rights of 4 parcels of land with a total site area of approximately 98,223.6 sq.m. have been granted to Huaxiang for terms of 50 years with the expiry dates between 27 May 2055 and 20 July 2059 for industrial use.

4. Pursuant to a Mortgage Contract of Maximum Amount - No. FJ31062201039-DY dated 22 March 2010, the land use rights of 3 parcels of land of the property with a total site area of approximately 90,789 sq.m. under the State-owned Land Use Rights Certificates - Jin Guo Yong (2009) Di Nos. 00709 to 00711 together with the land use rights of a parcel of land of property no. 2 with a site area of approximately 6,282 sq.m. are subject to a mortgage in favour of Bank of China Limited Jinjiang Branch (the "Bank"), as security to guarantee the principal obligation under a series of contracts entered into between the Bank and Huaxiang for a maximum amount of RMB71,347,000 with the security term from 22 March 2010 to 22 March 2012.

5. We have been provided with a legal opinion regarding the property interest by the Company's PRC legal advisers, which contains, *inter alia*, the following:

   a. The Group has fully paid up the land premium of the property and legally obtained the land use rights of the property;

   b. Subject to note 5(c) below, the Group has the rights to occupy, use, lease, transfer, mortgage or otherwise dispose of the land use rights of the property in accordance with the PRC laws;

   c. For the land use rights which are subject to the mortgage mentioned above, the Group should obtain prior written consent from the mortgagee when transferring, re-mortgaging or otherwise disposing of such land use rights; and

   d. Except for the aforesaid mortgage, the property is not subject to any restrictions arising from any other mortgage, sequestration or any third parties rights.

## VALUATION CERTIFICATE

| No. | Property | Description and tenure | Particulars of occupancy | Capital value in existing state as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| 6. | 4 parcels of land located at Wuzhai Village Jiaomei Town Longhai City Fujian Province The PRC | The property comprises 4 parcels of land with a total site area of approximately 180,244.07 sq.m.<br><br>The land use rights of the property have been granted for terms of 50 years with the expiry dates between 5 March 2056 and 17 October 2056 for industrial use. | The property is currently vacant. | 36,028,000<br><br>100% interest attributable to the Group: RMB36,028,000 |

*Notes:*

1. Pursuant to a Project Investment Agreement dated 12 May 2006 entered into between Fujian Xiyuan Paper Company Limited ("Xiyuan", a wholly-owned subsidiary of the Company) and the Administration Committee of Jiaomei Industrial Comprehensive Development Zone (角美工業綜合開發區管委會), the land use rights of a parcel of land with a site area of approximately 217.7805 Mu. (145,187 sq.m.) were contracted to be transferred to Xiyuan at a consideration of RMB58,096 per Mu.

2. Pursuant to a Land Use Rights Transfer Agreement dated 28 September 2009 entered into between Xiyuan and Zhangzhou Huarong Paper Company Limited (a connected party to the Company), the land use rights of a parcel of land with a site area of approximately 35,057.07 sq.m. of the property together with 2 parcels of land of property no. 7 with a total site area of approximately 44,608.6 sq.m. were contracted to be transferred to Xiyuan at a total consideration of RMB43,487,100.

3. Pursuant to 4 State-owned Land Use Rights Certificates - Long Guo Yong (2006 Jiao Zi) Di Nos. 0185 to 0187 and Long Guo Yong (2009 Jiao Zi) Di No. GC 0069, the land use rights of 4 parcels of land with a total site area of approximately 180,244.07 sq.m. have been granted to Xiyuan for terms of 50 years with the expiry dates between 5 March 2056 and 17 October 2056 for industrial use.

4. Pursuant to a Mortgage Contract of Maximum Amount - 2009 Quan Qing Yin Xin Gao Di Zi Di No. 200902702 dated 16 July 2009, the land use rights of a parcel of land with a site area of approximately 38,311.1 sq.m. under the State-owned Land Use Rights Certificate - Long Guo Yong (2006 Jiao Zi) Di No. 0186 are subject to a mortgage in favour of China CITIC Bank Quanzhou Branch ("Bank A"), as security to guarantee the principal obligation under a series of contracts entered into between Bank A and Fujian Jinjiang Youlanfa Paper Company Limited (a wholly-owned subsidiary of the Company) for a maximum amount of RMB28,590,000 with the security term from 16 July 2009 to 16 July 2012.

5. Pursuant to a Mortgage Contract of Maximum Amount - No. FJ31062201096-DY-2 dated 31 March 2010, the land use rights of a parcel of land of the property with a site area of approximately 35,057.07 sq.m. under the State-owned Land Use Rights Certificate - Long Guo Yong (2009 Jiao Zi) Di No. GC 0069 together with the land use rights of 2 parcels of land of property no. 7 with a total site area of approximately 44,608.6 sq.m. are subject to a mortgage in favour of Bank of China Limited Jinjiang Branch ("Bank B"), as security to guarantee the principal obligation under a series of contracts entered into between Bank B and Xiyuan for a maximum amount of RMB44,150,700 with the security term from 31 March 2010 to 31 March 2014.

6. We have been provided with a legal opinion regarding the property interest by the Company's PRC legal advisers, which contains, *inter alia*, the following:

   a. The Group has fully paid up the land premium of the property and legally obtained the land use rights of the property;

   b. Subject to note 6(c) below, the Group has the rights to occupy, use, lease, transfer, mortgage or otherwise dispose of the land use rights of the property in accordance with the PRC laws;

   c. For the land use rights which are subject to the mortgages mentioned above, the Group should obtain prior written consent from the mortgagee when transferring, re-mortgaging or otherwise disposing of such land use rights; and

   d. Except for the aforesaid mortgages, the land use rights of the property are not subject to any restrictions arising from any other mortgage, sequestration or any third parties rights.

## VALUATION CERTIFICATE

**Group III — Property interest held under development by the Group in the PRC**

| No. | Property | Description and tenure | Particulars of occupancy | Capital value in existing state as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| 7. | 2 parcels of land and 3 industrial buildings under construction located at Wuzhai Village Jiaomei Town Longhai City Fujian Province The PRC | The property comprises 2 parcels of land with a total site area of approximately 44,608.6 sq.m. and 3 industrial buildings which are being constructed thereon.<br><br>The construction work commenced from October 2009 and is scheduled to be completed in December 2010. Upon completion, the 3 buildings of the property will have a total gross floor area of approximately 22,328 sq.m. and the details are set out as follows:<br><br>Use / No. of Item / Planned Gross Floor Area (sq.m.)<br>Production / 2 / 15,308<br>Warehouse / 1 / 7,020<br>**Total** / 3 / 22,328<br><br>The total construction cost of the 3 buildings is estimated to be approximately RMB42,750,000. As confirmed by the Group, no payment had been made by the Group up to the date of valuation.<br><br>The land use rights of the property have been granted for terms of 50 years expiring on 5 March 2056 for industrial use. | The property is currently under construction. | 30,007,000<br><br>100% interest attributable to the Group: RMB30,007,000 |

| Use | No. of Item | Planned Gross Floor Area *(sq.m.)* |
|---|---|---|
| Production | 2 | 15,308 |
| Warehouse | 1 | 7,020 |
| **Total** | 3 | 22,328 |

*Notes:*

1. Pursuant to a Land Use Rights Transfer Agreement dated 28 September 2009 entered into between Fujian Xiyuan Paper Company Limited ("Xiyuan", a wholly-owned subsidiary of the Company) and Zhangzhou Huarong Paper Company Limited (a connected party to the Company), the land use rights of 2 parcels of land of the property with a total site area of approximately 44,608.6 sq.m. together with a parcel of land of property no. 6 with a site area of approximately 35,057.07 sq.m. were contracted to be transferred to Xiyuan at a total consideration of RMB43,487,100.

2. Pursuant to 2 State-owned Land Use Rights Certificates - Long Guo Yong (2009 Jiao Zi) Di Nos. GC0068 and GC0070, the land use rights of 2 parcels of land with a total site area of approximately 44,608.6 sq.m. have been granted to Xiyuan for terms of 50 years expiring on 5 March 2056 for industrial use.

3. Pursuant to a Construction Work Planning Permit - Jian Zi Di No. 100920038 issued by the Administration Committee of Jiaomei Industrial Comprehensive Development Zone in favour of Xiyuan, 3 industrial buildings with a total gross floor area of approximately 22,328 sq.m. have been approved for construction.

4. Pursuant to a Mortgage Contract of Maximum Amount - No. FJ31062201096-DY-2 dated 31 March 2010, the land use rights of 2 parcels of land of the property with a total site area of approximately 44,608.6 sq.m. under the State-owned Land Use Rights Certificates - Long Guo Yong (2009 Jiao Zi) Di Nos. GC0068 and GC0070 together with the land use rights of a parcel of land of property no. 6 with a site area of approximately 35,057.07 sq.m. are subject to a mortgage in favour of Bank of China Limited Jinjiang Branch (the "Bank"), as security to guarantee the principal obligation under a series of contracts entered into between the Bank and Xiyuan for a maximum amount of RMB44,150,700 with the security term from 31 March 2010 to 31 March 2014.

5. We have been provided with a legal opinion regarding the property interest by the Company's PRC legal advisers, which contains, *inter alia*, the following:

   a. The Group has fully paid up the land premium of the property and legally obtained the land use rights of the property;

   b. Subject to note 5(c) below, the Group has the rights to occupy, use, lease, transfer, mortgage or otherwise dispose of the land use rights of the property in accordance with the PRC laws;

   c. For the land use rights which are subject to the mortgage mentioned above, the Group should obtain prior written consent from the mortgagee when transferring, re-mortgaging or otherwise disposing of such land use rights;

   d. Except for the aforesaid mortgage, the land use rights of the property are not subject to any restrictions arising from any other mortgage, sequestration or any third parties rights; and

   e. The buildings under construction have obtained the relevant construction permits in accordance with the PRC laws as mentioned in note 3.

## VALUATION CERTIFICATE

**Group IV — Property interest leased and occupied by the Group in Hong Kong**

| No. | Property | Description and tenure | Particulars of occupancy | Capital value in existing state as at 28 February 2010 *RMB* |
|---|---|---|---|---|
| 8. | Unit 4 on 13th Floor Bank of America Tower No. 12 Harcourt Road Hong Kong | The property comprises a unit on the 13th floor of a 39-storey office building completed in 1975.<br><br>The unit has a gross area of approximately 1,210 sq.ft. (112.41 sq.m.).<br><br>Pursuant to a Tenancy Agreement made between Sunwell Trading (HK) Company Limited, as tenant and Eriksdale Limited, as landlord (an independent third party), the property is leased by the Group for a term commencing from 18 February 2010 and expiring on 17 February 2012 at a monthly rent of HK$41,140 exclusive of government rates, air-conditioning and management charges. | The property is currently occupied by the Group for office purpose. | No commercial value |

*Notes:*

1. The registered owner of the property is Eriksdale Limited vide Memorial No. UB7247904 dated 15 August 1997.

2. Sunwell Trading (HK) Company Limited is a wholly-owned subsidiary of the Company.

Set out below is a summary of certain provisions of the Memorandum and Articles of Association of the Company and of certain aspects of Cayman company law.

The Company was incorporated in the Cayman Islands as an exempted company with limited liability on 12 October 2009 under the Companies Law. The Memorandum of Association (the "Memorandum") and the Articles of Association (the "Articles") comprise its constitution.

## 1. MEMORANDUM OF ASSOCIATION

(a) The Memorandum states, inter alia, that the liability of members of the Company is limited to the amount, if any, for the time being unpaid on the Shares respectively held by them and that the objects for which the Company is established are unrestricted (including acting as an investment company), and that the Company shall have and be capable of exercising all the functions of a natural person of full capacity irrespective of any question of corporate benefit, as provided in section 27(2) of the Companies Law and in view of the fact that the Company is an exempted company that the Company will not trade in the Cayman Islands with any person, firm or corporation except in furtherance of the business of the Company carried on outside the Cayman Islands.

(b) The Company may by special resolution alter its Memorandum with respect to any objects, powers or other matters specified therein.

## 2. ARTICLES OF ASSOCIATION

The Articles were adopted on 30 April 2010. The following is a summary of certain provisions of the Articles:

(a) **Directors**

(i) *Power to allot and issue shares and warrants*

Subject to the provisions of the Companies Law and the Memorandum and Articles and to any special rights conferred on the holders of any shares or class of shares, any share may be issued with or have attached thereto such rights, or such restrictions, whether with regard to dividend, voting, return of capital, or otherwise, as the Company may by ordinary resolution determine (or, in the absence of any such determination or so far as the same may not make specific provision, as the board may determine). Subject to the Companies Law, the rules of any Designated Stock Exchange (as defined in the Articles) and the Memorandum and Articles, any share may be issued on terms that, at the option of the Company or the holder thereof, they are liable to be redeemed.

The board may issue warrants conferring the right upon the holders thereof to subscribe for any class of shares or securities in the capital of the Company on such terms as it may from time to time determine.

Subject to the provisions of the Companies Law and the Articles and, where applicable, the rules of any Designated Stock Exchange (as defined in the Articles) and without prejudice to any special rights or restrictions for the time being attached to any shares or any class of shares, all unissued shares in the Company shall be at the disposal of the board, which may offer, allot, grant options over or otherwise dispose of them to such persons, at such times, for such consideration and on such terms and conditions as it in its absolute discretion thinks fit, but so that no shares shall be issued at a discount.

Neither the Company nor the board shall be obliged, when making or granting any allotment of, offer of, option over or disposal of shares, to make, or make available, any such allotment, offer, option or shares to members or others with registered addresses in any particular territory or territories being a territory or territories where, in the absence of a registration statement or other special formalities, this would or might, in the opinion of the board, be unlawful or impracticable. Members affected as a result of the foregoing sentence shall not be, or be deemed to be, a separate class of members for any purpose whatsoever.

(ii) *Power to dispose of the assets of the Company or any subsidiary*

There are no specific provisions in the Articles relating to the disposal of the assets of the Company or any of its subsidiaries. The Directors may, however, exercise all powers and do all acts and things which may be exercised or done or approved by the Company and which are not required by the Articles or the Companies Law to be exercised or done by the Company in general meeting.

(iii) *Compensation or payments for loss of office*

Pursuant to the Articles, payments to any Director or past Director of any sum by way of compensation for loss of office or as consideration for or in connection with his retirement from office (not being a payment to which the Director is contractually entitled) must be approved by the Company in general meeting.

(iv) *Loans and provision of security for loans to Directors*

There are provisions in the Articles prohibiting the making of loans to Directors.

(v) *Disclosure of interests in contracts with the Company or any of its subsidiaries.*

A Director may hold any other office or place of profit with the Company (except that of the auditor of the Company) in conjunction with his office of Director for such period and, subject to the Articles, upon such terms as the board may determine, and may be paid such extra remuneration therefor (whether by way of salary, commission, participation in profits or otherwise) in addition to any remuneration provided for by or pursuant to any other Articles. A Director may be or become a director or other officer of, or otherwise interested in, any company promoted by the Company or any other company in which the Company may be interested, and shall not be liable to account to the Company or the members for any remuneration, profits or other benefits received by him as a director, officer or member of, or from his interest in, such other company. Subject as otherwise provided by the Articles, the board may also cause the voting power conferred by the shares in any other company held or owned by the Company to be exercised in such manner in all respects as it thinks fit, including the exercise thereof in favour of any resolution appointing the Directors or any of them to be directors or officers of such other company, or voting or providing for the payment of remuneration to the directors or officers of such other company.

Subject to the Companies Law and the Articles, no Director or proposed or intended Director shall be disqualified by his office from contracting with the Company, either with regard to his tenure of any office or place of profit or as vendor, purchaser or in any other manner whatsoever, nor shall any such contract or any other contract or arrangement in which any Director is in any way interested be liable to be avoided, nor shall any Director so contracting or being so interested be liable to account to the Company or the members for any remuneration, profit or other benefits realised by any such contract or arrangement by reason of such Director holding that office or the fiduciary relationship thereby established. A Director who to his knowledge is in any way, whether directly or indirectly, interested in a contract or arrangement or proposed contract or arrangement with the Company shall declare the nature of his interest at the meeting of the board at which the question of entering into the contract or arrangement is first taken into consideration, if he knows his interest then exists, or in any other case, at the first meeting of the board after he knows that he is or has become so interested.

A Director shall not vote (nor be counted in the quorum), and will abstain from the meeting at which the Board discusses and considers, any resolution approving any contract or arrangement or other proposal in which he or any of his associates is materially interested, unless expressly requested by a majority of independent non-executive Directors to attend and/or vote at the meeting.

(vi) *Remuneration*

The ordinary remuneration of the Directors shall from time to time be determined by the Company in general meeting, such sum (unless otherwise directed by the resolution by which it is voted) to be divided amongst the Directors in such proportions and in such manner as the board may agree or, failing agreement, equally, except that any Director holding office for part only of the period in respect of which the remuneration is payable shall only rank in such division in proportion to the time during such period for which he held office. The Directors shall also be entitled to be prepaid or repaid all travelling, hotel and incidental expenses reasonably expected to be incurred or incurred by them in attending any board meetings, committee meetings or general meetings or separate meetings of any class of shares or of debentures of the Company or otherwise in connection with the discharge of their duties as Directors.

Any Director who, by request, goes or resides abroad for any purpose of the Company or who performs services which in the opinion of the board go beyond the ordinary duties of a Director may be paid such extra remuneration (whether by way of salary, commission, participation in profits or otherwise) as the board may determine and such extra remuneration shall be in addition to or in substitution for any ordinary remuneration as a Director. An executive Director appointed to be a managing director, joint managing director, deputy managing director or other executive officer shall receive such remuneration (whether by way of salary, commission or participation in profits or otherwise or by all or any of those modes) and such other benefits (including pension and/or gratuity and/or other benefits on retirement) and allowances as the board may from time to time decide. Such remuneration may be either in addition to or in lieu of his remuneration as a Director.

The board may establish or concur or join with other companies (being subsidiary companies of the Company or companies with which it is associated in business) in establishing and making contributions out of the Company's monies to any schemes or funds for providing pensions, sickness or compassionate allowances, life assurance or other benefits for employees (which expression as used in this and the following paragraph shall include any Director or ex-Director who may hold or have held any executive office or any office of profit with the Company or any of its subsidiaries) and ex-employees of the Company and their dependents or any class or classes of such persons.

The board may pay, enter into agreements to pay or make grants of revocable or irrevocable, and either subject or not subject to any terms or conditions, pensions or other benefits to employees and ex-employees and their dependents, or to any of such persons, including pensions or benefits additional to those, if any, to which such employees or ex-employees or their dependents are or may become entitled under any such scheme or fund as is mentioned in the previous paragraph. Any such pension or benefit may, as the board considers desirable, be granted to an employee either before and in anticipation of, or upon or at any time after, his actual retirement.

(vii) *Retirement, appointment and removal*

At each annual general meeting, one third of the Directors for the time being (or if their number is not a multiple of three, then the number nearest to but not less than one third) will retire from office by rotation provided that every Director shall be subject to retirement at an annual general meeting at least once every three years. The Directors to retire in every year will be those who have been longest in office since their last re-election or appointment but as between persons who became or were last re-elected Directors on the same day those to retire will (unless they otherwise agree among themselves) be determined by lot. There are no provisions relating to retirement of Directors upon reaching any age limit.

The Directors shall have the power from time to time and at any time to appoint any person as a Director either to fill a casual vacancy on the board or as an addition to the existing board. Any Director appointed to fill a casual vacancy shall hold office until the first general meeting of members after his appointment and be subject to re-election at such meeting and any Director appointed as an addition to the existing board shall hold office only until the next following annual general meeting of the Company and shall then be eligible for re-election. Neither a Director nor an alternate Director is required to hold any shares in the Company by way of qualification.

A Director may be removed by an ordinary resolution of the Company before the expiration of his period of office (but without prejudice to any claim which such Director may have for damages for any breach of any contract between him and the Company) and may by ordinary resolution appoint another in his place. Unless otherwise determined by the Company in general meeting, the number of Directors shall not be less than two. There is no maximum number of Directors.

The office or director shall be vacated:

(aa) if he resigns his office by notice in writing delivered to the Company at the registered office of the Company for the time being or tendered at a meeting of the Board;

(bb) becomes of unsound mind or dies;

(cc) if, without special leave, he is absent from meetings of the board (unless an alternate director appointed by him attends) for six (6) consecutive months, and the board resolves that his office is vacated;

(dd) if he becomes bankrupt or has a receiving order made against him or suspends payment or compounds with his creditors;

(ee) if he is prohibited from being a director by law;

(ff) if he ceases to be a director by virtue of any provision of law or is removed from office pursuant to the Articles.

The board may from time to time appoint one or more of its body to be managing director, joint managing director, or deputy managing director or to hold any other employment or executive office with the Company for such period and upon such terms as the board may determine and the board may revoke or terminate any of such appointments. The board may delegate any of its powers, authorities and discretions to committees consisting of such Director or Directors and other persons as the board thinks fit, and it may from time to time revoke such delegation or revoke the appointment of and discharge any such committees either wholly or in part, and either as to persons or purposes, but every committee so formed shall, in the exercise of the powers, authorities and discretions so delegated, conform to any regulations that may from time to time be imposed upon it by the board.

(viii) *Borrowing powers*

The board may exercise all the powers of the Company to raise or borrow money, to mortgage or charge all or any part of the undertaking, property and assets (present and future) and uncalled capital of the Company and, subject to the Companies Law, to issue debentures, bonds and other securities of the Company, whether outright or as collateral security for any debt, liability or obligation of the Company or of any third party.

*Note:* These provisions, in common with the Articles in general, can be varied with the sanction of a special resolution of the Company.

(ix) *Proceedings of the Board*

The board may meet for the despatch of business, adjourn and otherwise regulate their meetings as they think fit. Questions arising at any meeting shall be determined by a majority of votes. In the case of an equality of votes, the chairman of the meeting shall have an additional or casting vote.

(x) *Register of Directors and Officers*

The Companies Law and the Articles provide that the Company is required to maintain at its registered office a register of directors and officers which is not available for inspection by the public. A copy of such register must be filed with the Registrar of Companies in the Cayman Islands and any change must be notified to the Registrar within thirty (30) days of any change in such directors or officers.

(b) **Alterations to constitutional documents**

The Articles may be rescinded, altered or amended by the Company in general meeting by special resolution. The Articles state that a special resolution shall be required to alter the provisions of the Memorandum, to amend the Articles or to change the name of the Company.

(c) **Alteration of capital**

The Company may from time to time by ordinary resolution in accordance with the relevant provisions of the Companies Law:

(i) increase its capital by such sum, to be divided into shares of such amounts as the resolution shall prescribe;

(ii) consolidate and divide all or any of its capital into shares of larger amount than its existing shares;

(iii) divide its shares into several classes and without prejudice to any special rights previously conferred on the holders of existing shares attach thereto respectively any preferential, deferred, qualified or special rights, privileges, conditions or restrictions as the Company in general meeting or as the directors may determine;

(iv) sub-divide its shares or any of them into shares of smaller amount than is fixed by the Memorandum, subject nevertheless to the provisions of the Companies Law, and so that the resolution whereby any share is sub-divided may determine that, as between the holders of the shares resulting from such sub-division, one or more of the shares may have any such preferred or other special rights, over, or may have such deferred rights or be subject to any such restrictions as compared with the others as the Company has power to attach to unissued or new shares; or

(v) cancel any shares which, at the date of passing of the resolution, have not been taken, or agreed to be taken, by any person, and diminish the amount of its capital by the amount of the shares so cancelled.

The Company may subject to the provisions of the Companies Law reduce its share capital or any capital redemption reserve or other undistributable reserve in any way by special resolution.

(d) **Variation of rights of existing shares or classes of shares**

Subject to the Companies Law, all or any of the special rights attached to the shares or any class of shares may (unless otherwise provided for by the terms of issue of that class) be varied, modified or abrogated either with the consent in writing of the holders of not less than three-fourths in nominal value of the issued shares of that class or with the sanction of a special resolution passed at a separate general meeting of the holders of the shares of that class. To every such separate general meeting the provisions of the Articles relating to general meetings will *mutatis mutandis* apply, but so that the necessary quorum (other than at an adjourned meeting) shall be two persons holding or representing by proxy not less than one-third in nominal value of the issued shares of that class and at any adjourned meeting two holders present in person or by proxy whatever the number of shares held by them shall be a quorum. Every holder of shares of the class shall be entitled to one vote for every such share held by him.

The special rights conferred upon the holders of any shares or class of shares shall not, unless otherwise expressly provided in the rights attaching to the terms of issue of such shares, be deemed to be varied by the creation or issue of further shares ranking *pari passu* therewith.

(e) **Special resolution-majority required**

Pursuant to the Articles, a special resolution of the Company must be passed by a majority of not less than three-fourths of the votes cast by such members as, being entitled so to do, vote in person or, in the case of such members as are corporations, by their duly authorised representatives or, where proxies are allowed, by proxy at a general meeting of which notice of not less than twenty-one (21) clear days and not less than ten (10) clear business days specifying the intention to propose the resolution as a special resolution, has been duly given. Provided that if permitted by the Designated Stock Exchange (as defined in the Articles), except in the case of an annual general meeting, if it is so agreed by a majority in number of the members having a right to attend and vote at such meeting, being a majority together holding not less than ninety-five per cent. (95%) in nominal value of the shares giving that right and, in the case of an annual general meeting, if so agreed by all Members entitled to attend and vote thereat, a resolution may be proposed and passed as a special resolution at a meeting of which notice of less than twenty-one (21) clear days and less than ten (10) clear business days has been given.

A copy of any special resolution must be forwarded to the Registrar of Companies in the Cayman Islands within fifteen (15) days of being passed.

An ordinary resolution is defined in the Articles to mean a resolution passed by a simple majority of the votes of such members of the Company as, being entitled to do so, vote in person or, in the case of corporations, by their duly authorised representatives or, where proxies are allowed, by proxy at a general meeting held in accordance with the Articles.

(f) **Voting rights**

Subject to any special rights or restrictions as to voting for the time being attached to any shares by or in accordance with the Articles, at any general meeting on a poll every member present in person or by proxy or, in the case of a member being a corporation, by its duly authorised representative shall have one vote for every fully paid share of which he is the holder but so that no amount paid up or credited as paid up on a share in advance of calls or installments is treated for the foregoing purposes as paid up on the share. A member entitled to more than one vote need not use all his votes or cast all the votes he uses in the same way.

At any general meeting a resolution put to the vote of the meeting is to be decided by way of a poll.

If a recognised clearing house (or its nominee(s)) is a member of the Company it may authorise such person or persons as it thinks fit to act as its representative(s) at any meeting of the Company or at any meeting of any class of members of the Company provided that, if more than one person is so authorised, the authorisation shall specify the number and class of shares in respect of which each such person is so authorised. A person authorised pursuant to this provision shall be deemed to have been duly authorised without further evidence of the facts and be entitled to exercise the same powers on behalf of the recognised clearing house (or its nominee(s)) as if such person was the registered holder of the shares of the Company held by that clearing house (or its nominee(s)).

Where the Company has any knowledge that any shareholder is, under the rules of the Designated Stock Exchange (as defined in the Articles), required to abstain from voting on any particular resolution of the Company or restricted to voting only for or only against any particular resolution of the Company, any votes cast by or on behalf of such shareholder in contravention of such requirement or restriction shall not be counted.

(g) **Requirements for annual general meetings**

An annual general meeting of the Company must be held in each year, other than the year of adoption of the Articles (within a period of not more than fifteen (15) months after the holding of the last preceding annual general meeting or a period of eighteen (18) months from the date of adoption of the Articles, unless a longer period would not infringe the rules of any Designated Stock Exchange (as defined in the Articles)) at such time and place as may be determined by the board.

(h) **Accounts and audit**

The board shall cause true accounts to be kept of the sums of money received and expended by the Company, and the matters in respect of which such receipt and expenditure take place, and of the property, assets, credits and liabilities of the Company and of all other matters required by the Companies Law or necessary to give a true and fair view of the Company's affairs and to explain its transactions.

The accounting records shall be kept at the registered office or at such other place or places as the board decides and shall always be open to inspection by any Director. No member (other than a Director) shall have any right to inspect any accounting record or book or document of the Company except as conferred by law or authorised by the board or the Company in general meeting.

A copy of every balance sheet and profit and loss account (including every document required by law to be annexed thereto) which is to be laid before the Company at its general meeting, together with a printed copy of the Directors' report and a copy of the auditors' report, shall not less than twenty-one (21) days before the date of the meeting and at the same time as the notice of annual general meeting be sent to every person entitled to receive notices of general meetings of the Company under the provisions the Articles; however, subject to compliance with all applicable laws, including the rules of the Designated Stock Exchange (as defined in the Articles), the Company may send to such persons summarised financial statements derived from the Company's annual accounts and the directors' report instead provided that any such person may by notice in writing served on the Company, demand that the Company sends to him, in addition to summarised financial statements, a complete printed copy of the Company's annual financial statement and the directors' report thereon.

Auditors shall be appointed and the terms and tenure of such appointment and their duties at all times regulated in accordance with the provisions of the Articles. The remuneration of the auditors shall be fixed by the Company in general meeting or in such manner as the members may determine.

The financial statements of the Company shall be audited by the auditor in accordance with generally accepted auditing standards. The auditor shall make a written report thereon in accordance with generally accepted auditing standards and the report of the auditor shall be submitted to the members in general meeting. The generally accepted auditing standards referred to herein may be those of a country or jurisdiction other than the Cayman Islands. If so, the financial statements and the report of the auditor should disclose this fact and name such country or jurisdiction.

(i) **Notices of meetings and business to be conducted thereat**

An annual general meeting shall be called by notice of not less than twenty-one (21) clear days and not less than twenty (20) clear business days and any extraordinary general meeting at which it is proposed to pass a special resolution shall (save as set out in sub-paragraph (e) above) be called by notice of at least twenty-one (21) clear days and not less than ten (10) clear business days. All other extraordinary general meetings shall be called by notice of at least fourteen (14) clear days and not less than ten (10) clear business days. The notice must specify the time and place of the meeting and, in the case of special business, the general nature of that business. In addition notice of every general meeting shall be given to all members of the Company other than such as, under the provisions of the Articles or the terms of issue of the shares they hold, are not entitled to receive such notices from the Company, and also to the auditors for the time being of the Company.

Notwithstanding that a meeting of the Company is called by shorter notice than that mentioned above if permitted by the rules of the Designated Stock Exchange, it shall be deemed to have been duly called if it is so agreed:

(i) in the case of a meeting called as an annual general meeting, by all members of the Company entitled to attend and vote thereat; and

(ii) in the case of any other meeting, by a majority in number of the members having a right to attend and vote at the meeting, being a majority together holding not less than ninety-five per cent (95%) in nominal value of the issued shares giving that right.

All business shall be deemed special that is transacted at an extraordinary general meeting and also all business shall be deemed special that is transacted at an annual general meeting with the exception of the following, which shall be deemed ordinary business:

(aa) the declaration and sanctioning of dividends;

(bb) the consideration and adoption of the accounts and balance sheet and the reports of the directors and the auditors;

(cc) the election of directors in place of those retiring;

(dd) the appointment of auditors and other officers;

(ee) the fixing of the remuneration of the directors and of the auditors;

(ff) the granting of any mandate or authority to the directors to offer, allot, grant options over or otherwise dispose of the unissued shares of the Company representing not more than twenty per cent (20%) in nominal value of its existing issued share capital; and

(gg) the granting of any mandate or authority to the directors to repurchase securities of the Company.

(j) **Transfer of shares**

All transfers of shares may be effected by an instrument of transfer in the usual or common form or in a form prescribed by the Designated Stock Exchange (as defined in the Articles) or in such other form as the board may approve and which may be under hand or, if the transferor or transferee is a clearing house or its nominee(s), by hand or by machine imprinted signature or by such other manner of execution as the board may approve from time to time. The instrument of transfer shall be executed by or on behalf of the transferor and the transferee provided that the board may dispense with the execution of the instrument of transfer by the transferee in any case in which it thinks fit, in its discretion, to do so and the transferor shall be deemed to remain the holder of the share until the name of the transferee is entered in the register of members in respect thereof. The board may also resolve either generally or in any particular case, upon request by either the transferor or the transferee, to accept mechanically executed transfers.

The board in so far as permitted by any applicable law may, in its absolute discretion, at any time and from time to time transfer any share upon the principal register to any branch register or any share on any branch register to the principal register or any other branch register.

Unless the board otherwise agrees, no shares on the principal register shall be transferred to any branch register nor may shares on any branch register be transferred to the principal register or any other branch register. All transfers and other documents of title shall be lodged for registration and registered, in the case of shares on a branch register, at the relevant registration office and, in the case of shares on the principal register, at the registered office in the Cayman Islands or such other place at which the principal register is kept in accordance with the Companies Law.

The board may, in its absolute discretion, and without assigning any reason, refuse to register a transfer of any share (not being a fully paid up share) to a person of whom it does not approve or any share issued under any share incentive scheme for employees upon which a restriction on transfer imposed thereby still subsists, and it may also refuse to register any transfer of any share to more than four joint holders or any transfer of any share (not being a fully paid up share) on which the Company has a lien.

The board may decline to recognise any instrument of transfer unless a fee of such maximum sum as any Designated Stock Exchange (as defined in the Articles) may determine to be payable or such lesser sum as the Directors may from time to time require is paid to the Company in respect thereof, the instrument of transfer, if applicable, is properly stamped, is in respect of only one class of share and is lodged at the relevant registration office or registered office or such other place at which the principal register is kept accompanied by the relevant share certificate(s) and such other evidence as the board may reasonably require to show the right of the transferor to make the transfer (and if the instrument of transfer is executed by some other person on his behalf, the authority of that person so to do).

The registration of transfers may be suspended and the register closed on giving notice by advertisement in a relevant newspaper and, where applicable, any other newspapers in accordance with the requirements of any Designated Stock Exchange (as defined in the Articles), at such times and for such periods as the board may determine and either generally or in respect of any class of shares. The register of members shall not be closed for periods exceeding in the whole thirty (30) days in any year.

(k) **Power for the Company to purchase its own shares**

The Company is empowered by the Companies Law and the Articles to purchase its own Shares subject to certain restrictions and the Board may only exercise this power on behalf of the Company subject to any applicable requirements imposed from time to time by any Designated Stock Exchange (as defined in the Articles).

(l) **Power for any subsidiary of the Company to own shares in the Company and financial assistance to purchase shares of the Company**

There are no provisions in the Articles relating to ownership of shares in the Company by a subsidiary.

Subject to compliance with the rules and regulations of the Designated Stock Exchange (as defined in the Articles) and any other relevant regulatory authority, the Company may give financial assistance for the purpose of or in connection with a purchase made or to be made by any person of any shares in the Company.

(m) **Dividends and other methods of distribution**

Subject to the Companies Law, the Company in general meeting may declare dividends in any currency to be paid to the members but no dividend shall be declared in excess of the amount recommended by the board.

The Articles provide dividends may be declared and paid out of the profits of the Company, realised or unrealised, or from any reserve set aside from profits which the directors determine is no longer needed. With the sanction of an ordinary resolution dividends may also be declared and paid out of share premium account or any other fund or account which can be authorised for this purpose in accordance with the Companies Law.

Except in so far as the rights attaching to, or the terms of issue of, any share may otherwise provide, (i) all dividends shall be declared and paid according to the amounts paid up on the shares in respect whereof the dividend is paid but no amount paid up on a share in advance of calls shall for this purpose be treated as paid up on the share and (ii) all dividends shall be apportioned and paid pro rata according to the amount paid up on the shares during any portion or portions of the period in respect of which the dividend is paid. The Directors may deduct from any dividend or other monies payable to any member or in respect of any shares all sums of money (if any) presently payable by him to the Company on account of calls or otherwise.

Whenever the board or the Company in general meeting has resolved that a dividend be paid or declared on the share capital of the Company, the board may further resolve either (a) that such dividend be satisfied wholly or in part in the form of an allotment of shares credited as fully paid up, provided that the shareholders entitled thereto will be entitled to elect to receive such dividend (or part thereof) in cash in lieu of such allotment, or (b) that shareholders entitled to such dividend will be entitled to elect to receive an allotment of shares credited as fully paid up in lieu of the whole or such part of the dividend as the board may think fit. The Company may also upon the recommendation of the board by an ordinary resolution resolve in respect of any one particular dividend of the Company that it may be satisfied wholly in the form of an allotment of shares credited as fully paid up without offering any right to shareholders to elect to receive such dividend in cash in lieu of such allotment.

Any dividend, interest or other sum payable in cash to the holder of shares may be paid by cheque or warrant sent through the post addressed to the holder at his registered address, or in the case of joint holders, addressed to the holder whose name stands first in the register of the Company in respect of the shares at his address as appearing in the register or addressed to such person and at such addresses as the holder or joint holders may in writing direct. Every such cheque or warrant shall, unless the holder or joint holders otherwise direct, be made payable to the order of the holder or, in the case of joint holders, to the order of the holder whose name stands first on the register in respect of such shares, and shall be sent at his or their risk and payment of the cheque or warrant by the bank on which it is drawn shall constitute a good discharge to the Company. Any one of two or more joint holders may give effectual receipts for any dividends or other moneys payable or property distributable in respect of the shares held by such joint holders.

Whenever the board or the Company in general meeting has resolved that a dividend be paid or declared the board may further resolve that such dividend be satisfied wholly or in part by the distribution of specific assets of any kind.

All dividends or bonuses unclaimed for one year after having been declared may be invested or otherwise made use of by the board for the benefit of the Company until claimed and the Company shall not be constituted a trustee in respect thereof. All dividends or bonuses unclaimed for six years after having been declared may be forfeited by the board and shall revert to the Company.

No dividend or other monies payable by the Company on or in respect of any share shall bear interest against the Company.

(n) **Proxies**

Any member of the Company entitled to attend and vote at a meeting of the Company is entitled to appoint another person as his proxy to attend and vote instead of him. A member who is the holder of two or more shares may appoint more than one proxy to represent him and vote on his behalf at a general meeting of the Company or at a class meeting. A proxy need not be a member of the Company and shall be entitled to exercise the same powers on behalf of a member who is an individual and for whom he acts as proxy as such member could exercise. In addition, a proxy shall be entitled to exercise the same powers on behalf of a member which is a corporation and for which he acts as proxy as such member could exercise if it were an individual member. Votes may be given either personally (or, in the case of a member being a corporation, by its duly authorised representative) or by proxy.

(o) **Call on shares and forfeiture of shares**

Subject to the Articles and to the terms of allotment, the board may from time to time make such calls upon the members in respect of any monies unpaid on the shares held by them respectively (whether on account of the nominal value of the shares or by way of premium). A call may be made payable either in one lump sum or by installments. If the sum payable in respect of any call or instalment is not paid on or before the day appointed for payment thereof, the person or persons from whom the sum is due shall pay interest on the same at such rate not exceeding twenty per cent. (20%) per annum as the board may agree to accept from the day appointed for the payment thereof to the time of actual payment, but the board may waive payment of such interest wholly or in part. The board may, if it thinks fit, receive from any member willing to advance the same, either in money or money's worth, all or any part of the monies uncalled and unpaid or installments payable upon any shares held by him, and upon all or any of the monies so advanced the Company may pay interest at such rate (if any) as the board may decide.

If a member fails to pay any call on the day appointed for payment thereof, the board may serve not less than fourteen (14) clear days' notice on him requiring payment of so much of the call as is unpaid, together with any interest which may have accrued and which may still accrue up to the date of actual payment and stating that, in the event of non-payment at or before the time appointed, the shares in respect of which the call was made will be liable to be forfeited.

If the requirements of any such notice are not complied with, any share in respect of which the notice has been given may at any time thereafter, before the payment required by the notice has been made, be forfeited by a resolution of the board to that effect. Such forfeiture will include all dividends and bonuses declared in respect of the forfeited share and not actually paid before the forfeiture.

A person whose shares have been forfeited shall cease to be a member in respect of the forfeited shares but shall, notwithstanding, remain liable to pay to the Company all monies which, at the date of forfeiture, were payable by him to the Company in respect of the shares, together with (if the board shall in its discretion so require) interest thereon from the date of forfeiture until the date of actual payment at such rate not exceeding twenty per cent. (20%) per annum as the board determines.

(p) **Inspection of register of members**

Pursuant to the Articles the register and branch register of members shall be open to inspection for at least two (2) hours on every business day by members without charge, or by any other person upon a maximum payment of HK$2.50 or such lesser sum specified by the board, at the registered office or such other place at which the register is kept in accordance with the Companies Law or, upon a maximum payment of HK$1.00 or such lesser sum specified by the board, at the Registration Office (as defined in the Articles), unless the register is closed in accordance with the Articles.

(q) **Quorum for meetings and separate class meetings**

No business shall be transacted at any general meeting unless a quorum is present when the meeting proceeds to business, but the absence of a quorum shall not preclude the appointment of a chairman.

Save as otherwise provided by the Articles the quorum for a general meeting shall be two members present in person (or, in the case of a member being a corporation, by its duly authorised representative) or by proxy and entitled to vote. In respect of a separate class meeting (other than an adjourned meeting) convened to sanction the modification of class rights the necessary quorum shall be two persons holding or representing by proxy not less than one-third in nominal value of the issued shares of that class.

A corporation being a member shall be deemed for the purpose of the Articles to be present in person if represented by its duly authorised representative being the person appointed by resolution of the directors or other governing body of such corporation to act as its representative at the relevant general meeting of the Company or at any relevant general meeting of any class of members of the Company.

(r) **Rights of the minorities in relation to fraud or oppression**

There are no provisions in the Articles relating to rights of minority shareholders in relation to fraud or oppression. However, certain remedies are available to shareholders of the Company under Cayman law, as summarised in paragraph 3(f) of this Appendix.

(s) **Procedures on liquidation**

A resolution that the Company be wound up by the court or be wound up voluntarily shall be a special resolution.

Subject to any special rights, privileges or restrictions as to the distribution of available surplus assets on liquidation for the time being attached to any class or classes of shares (i) if the Company shall be wound up and the assets available for distribution amongst the members of the Company shall be more than sufficient to repay the whole of the capital paid up at the commencement of the winding up, the excess shall be distributed *pari passu* amongst such members in proportion to the amount paid up on the shares held by them respectively and (ii) if the Company shall be wound up and the assets available for distribution amongst the members as such shall be insufficient to repay the whole of the paid-up capital, such assets shall be distributed so that, as nearly as may be, the losses shall be borne by the members in proportion to the capital paid up, or which ought to have been paid up, at the commencement of the winding up on the shares held by them respectively.

If the Company shall be wound up (whether the liquidation is voluntary or by the court) the liquidator may, with the authority of a special resolution and any other sanction required by the Companies Law divide among the members in specie or kind the whole or any part of the assets of the Company whether the assets shall consist of property of one kind or shall consist of properties of different kinds and the liquidator may, for such purpose, set such value as he deems fair upon any one or more class or classes of property to be divided as aforesaid and may determine how such division shall be carried out as between the members or different classes of members. The liquidator may, with the like authority, vest any part of the assets in trustees upon such trusts for the benefit of members as the liquidator, with the like authority, shall think fit, but so that no contributory shall be compelled to accept any shares or other property in respect of which there is a liability.

(t) **Untraceable members**

Pursuant to the Articles, the Company may sell any of the shares of a member who is untraceable if (i) all cheques or warrants in respect of dividends of the shares in question (being not less than three in total number) for any sum payable in cash to the holder of such shares have remained uncashed for a period of 12 years; (ii) upon the expiry of the 12 year period, the Company has not during that time received any indication of the existence of the member; and (iii) the Company has caused an advertisement to be published in accordance with the rules of the Designated Stock Exchange (as defined in the Articles) giving notice of its intention to sell such shares and a period of three (3) months, or such shorter period as may be permitted by the Designated Stock Exchange (as defined in the Articles), has elapsed since the date of such advertisement and the Designated Stock Exchange (as defined in the Articles) has been notified of such intention. The net proceeds of any such sale shall belong to the Company and upon receipt by the Company of such net proceeds, it shall become indebted to the former member of the Company for an amount equal to such net proceeds.

(u) **Subscription rights reserve**

The Articles provide that to the extent that it is not prohibited by and is in compliance with the Companies Law, if warrants to subscribe for shares have been issued by the Company and the Company does any act or engages in any transaction which would result in the subscription price of such warrants being reduced below the par value of a share, a subscription rights reserve shall be established and applied in paying up the difference between the subscription price and the par value of a share on any exercise of the warrants.

## 3. CAYMAN ISLANDS COMPANY LAW

The Company is incorporated in the Cayman Islands subject to the Companies Law and, therefore, operates subject to Cayman law. Set out below is a summary of certain provisions of Cayman company law, although this does not purport to contain all applicable qualifications and exceptions or to be a complete review of all matters of Cayman company law and taxation, which may differ from equivalent provisions in jurisdictions with which interested parties may be more familiar:

### (a) Operations

As an exempted company, the Company's operations must be conducted mainly outside the Cayman Islands. The Company is required to file an annual return each year with the Registrar of Companies of the Cayman Islands and pay a fee which is based on the amount of its authorised share capital.

### (b) Share capital

The Companies Law provides that where a company issues shares at a premium, whether for cash or otherwise, a sum equal to the aggregate amount of the value of the premiums on those shares shall be transferred to an account, to be called the "share premium account". At the option of a company, these provisions may not apply to premiums on shares of that company allotted pursuant to any arrangement in consideration of the acquisition or cancellation of shares in any other company and issued at a premium. The Companies Law provides that the share premium account may be applied by the company subject to the provisions, if any, of its memorandum and articles of association in (a) paying distributions or dividends to members; (b) paying up unissued shares of the company to be issued to members as fully paid bonus shares; (c) the redemption and repurchase of shares (subject to the provisions of section 37 of the Companies Law); (d) writing-off the preliminary expenses of the company; (e) writing-off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company; and (f) providing for the premium payable on redemption or purchase of any shares or debentures of the company.

No distribution or dividend may be paid to members out of the share premium account unless immediately following the date on which the distribution or dividend is proposed to be paid, the company will be able to pay its debts as they fall due in the ordinary course business.

The Companies Law provides that, subject to confirmation by the Grand Court of the Cayman Islands (the "Court"), a company limited by shares or a company limited by guarantee and having a share capital may, if so authorised by its articles of association, by special resolution reduce its share capital in any way.

The Articles includes certain protections for holders of special classes of shares, requiring their consent to be obtained before their rights may be varied. The consent of the specified proportions of the holders of the issued shares of that class or the sanction of a resolution passed at a separate meeting of the holders of those shares is required.

(c) **Financial assistance to purchase shares of a company or its holding company**

Subject to all applicable laws, the Company may give financial assistance to Directors and employees of the Company, its subsidiaries, its holding company or any subsidiary of such holding company in order that they may buy Shares in the Company or shares in any subsidiary or holding company. Further, subject to all applicable laws, the Company may give financial assistance to a trustee for the acquisition of Shares in the Company or shares in any such subsidiary or holding company to be held for the benefit of employees of the Company, its subsidiaries, any holding company of the Company or any subsidiary of any such holding company (including salaried Directors).

There is no statutory restriction in the Cayman Islands on the provision of financial assistance by a company to another person for the purchase of, or subscription for, its own or its holding company's shares. Accordingly, a company may provide financial assistance if the directors of the company consider, in discharging their duties of care and acting in good faith, for a proper purpose and in the interests of the company, that such assistance can properly be given. Such assistance should be on an arm's-length basis.

(d) **Purchase of shares and warrants by a company and its subsidiaries**

Subject to the provisions of the Companies Law, a company limited by shares or a company limited by guarantee and having a share capital may, if so authorised by its articles of association, issue shares which are to be redeemed or are liable to be redeemed at the option of the company or a shareholder. In addition, such a company may, if authorised to do so by its articles of association, purchase its own shares, including any redeemable shares. However, if the articles of association do not authorise the manner or purchase, a company cannot purchase any of its own shares unless the manner of purchase has first been authorised by an ordinary resolution of the company. At no time may a company redeem or purchase its shares unless they are fully paid. A company may not redeem or purchase any of its shares if, as a result of the redemption or purchase, there would no longer be any member of the company holding shares. A payment out of capital by a company for the redemption or purchase of its own shares is not lawful unless immediately following the date on which the payment is proposed to be made, the company shall be able to pay its debts as they fall due in the ordinary course of business.

A company is not prohibited from purchasing and may purchase its own warrants subject to and in accordance with the terms and conditions of the relevant warrant instrument or certificate. There is no requirement under Cayman Islands law that a company's memorandum or articles of association contain a specific provision enabling such purchases and the directors of a company may rely upon the general power contained in its memorandum of association to buy and sell and deal in personal property of all kinds.

Under Cayman Islands law, a subsidiary may hold shares in its holding company and, in certain circumstances, may acquire such shares.

(e) **Dividends and distributions**

With the exception of section 34 of the Companies Law, there is no statutory provisions relating to the payment of dividends. Based upon English case law, which is regarded as persuasive in the Cayman Islands, dividends may be paid only out of profits. In addition, section 34 of the Companies Law permits, subject to a solvency test and the provisions, if any, of the company's memorandum and articles of association, the payment of dividends and distributions out of the share premium account (see paragraph 2(m) above for further details).

(f) **Protection of minorities**

The Cayman Islands courts ordinarily would be expected to follow English case law precedents which permit a minority shareholder to commence a representative action against or derivative actions in the name of the company to challenge (a) an act which is ultra vires the company or illegal, (b) an act which constitutes a fraud against the minority and the wrongdoers are themselves in control of the company, and (c) an irregularity in the passing of a resolution which requires a qualified (or special) majority.

In the case of a company (not being a bank) having a share capital divided into shares, the Court may, on the application of members holding not less than one fifth of the shares of the company in issue, appoint an inspector to examine into the affairs of the company and to report thereon in such manner as the Court shall direct.

Any shareholder of a company may petition the Court which may make a winding up order if the Court is of the opinion that it is just and equitable that the company should be wound up or, as an alternative to a winding up order, (a) an order regulating the conduct of the company's affairs in the future, (b) an order requiring the company to refrain from doing or continuing an act complained of by the shareholder petitioner or to do an act which the shareholder petitioner has complained it has omitted to do, (c) an order authorising civil proceedings to be brought in the name and on behalf of the company by the shareholder petitioner on such terms as the Court may direct, or (d) an order providing for the purchase of the shares of any shareholders of the company by other shareholders or by the company itself and, in the case of a purchase by the company itself, a reduction of the company's capital accordingly.

Generally claims against a company by its shareholders must be based on the general laws of contract or tort applicable in the Cayman Islands or their individual rights as shareholders as established by the company's memorandum and articles of association.

(g) **Management**

The Companies Law contains no specific restrictions on the power of directors to dispose of assets of a company. However, as a matter of general law, every officer of a company, which includes a director, managing director and secretary, in exercising his powers and discharging his duties must do so honestly and in good faith with a view to the best interests of the company and exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

(h) **Accounting and auditing requirements**

A company shall cause proper books of account to be kept with respect to (i) all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure takes place; (ii) all sales and purchases of goods by the company; and (iii) the assets and liabilities of the company.

Proper books of account shall not be deemed to be kept if there are not kept such books as are necessary to give a true and fair view of the state of the company's affairs and to explain its transactions.

(i) **Exchange control**

There are no exchange control regulations or currency restrictions in the Cayman Islands.

(j) **Taxation**

Pursuant to section 6 of the Tax Concessions Law (1999 Revision) of the Cayman Islands, the Company has obtained an undertaking from the Governor-in-Cabinet:

(1) that no law which is enacted in the Cayman Islands imposing any tax to be levied on profits, income, gains or appreciation shall apply to the Company or its operations; and

(2) that the aforesaid tax or any tax in the nature of estate duty or inheritance tax shall not be payable on or in respect of the shares, debentures or other obligations of the Company.

The undertaking for the Company is for a period of twenty years from 27 October 2009.

The Cayman Islands currently levy no taxes on individuals or corporations based upon profits, income, gains or appreciations and there is no taxation in the nature of inheritance tax or estate duty. There are no other taxes likely to be material to the Company levied by the Government of the Cayman Islands save certain stamp duties which may be applicable, from time to time, on certain instruments executed in or brought within the jurisdiction of the Cayman Islands. The Cayman Islands are not party to any double tax treaties.

(k) **Stamp duty on transfers**

No stamp duty is payable in the Cayman Islands on transfers of shares of Cayman Islands companies except those which hold interests in land in the Cayman Islands.

(l) **Loans to directors**

There is no express provision in the Companies Law prohibiting the making of loans by a company to any of its directors.

(m) **Inspection of corporate records**

Members of the Company will have no general right under the Companies Law to inspect or obtain copies of the register of members or corporate records of the Company. They will, however, have such rights as may be set out in the Company's Articles.

An exempted company may, subject to the provisions of its articles of association, maintain its principal register of members and any branch registers at such locations, whether within or without the Cayman Islands, as the directors may, from time to time, think fit. There is no requirement under the Companies Law for an exempted company to make any returns of members to the Registrar of Companies of the Cayman Islands. The names and addresses of the members are, accordingly, not a matter of public record and are not available for public inspection.

(n) **Winding up**

A company may be wound up compulsorily by order of the Court voluntarily; or, under supervision of the Court. The Court has authority to order winding up in a number of specified circumstances including where it is, in the opinion of the Court, just and equitable to do so.

A company may be wound up voluntarily when the members so resolve in general meeting by special resolution, or, in the case of a limited duration company, when the period fixed for the duration of the company by its memorandum or articles expires, or the event occurs on the occurrence of which the memorandum or articles provides that the company is to be dissolved, or, the company does not commence business for a year from its incorporation (or suspends its business for a year), or, the company is unable to pay its debts. In the case of a voluntary winding up, such company is obliged to cease to carry on its business from the time of passing the resolution for voluntary winding up or upon the expiry of the period or the occurrence of the event referred to above.

For the purpose of conducting the proceedings in winding up a company and assisting the Court, there may be appointed one or more than one person to be called an official liquidator or official liquidators; and the Court may appoint to such office such qualified person or persons, either provisionally or otherwise, as it thinks fit, and if more persons than one are appointed to such office, the Court shall declare whether any act hereby required or authorised to be done by the official liquidator is to be done by all or any one or more of such persons. The Court may also determine whether any and what security is to be given by an official liquidator on his appointment; if no official liquidator is appointed, or during any vacancy in such office, all the property of the company shall be in the custody of the Court. A person shall be qualified to accept an appointment as an official liquidator if he is duly qualified in terms of the Insolvency Practitioners Regulations. A foreign practitioner may be appointed to act jointly with a qualified insolvency practitioner.

In the case of a members' voluntary winding up of a company, the company in general meeting must appoint one or more liquidators for the purpose of winding up the affairs of the company and distributing its assets. A declaration of solvency must be signed by all the directors of a company being voluntarily wound up within twenty-eight (28) days of the commencement of the liquidation, failing which, its liquidator must apply to Court for an order that the liquidation continue under the supervision of the Court.

Upon the appointment of a liquidator, the responsibility for the company's affairs rests entirely in his hands and no future executive action may be carried out without his approval. A liquidator's duties are to collect the assets of the company (including the amount (if any) due from the contributories), settle the list of creditors and, subject to the rights of preferred and secured creditors and to any subordination agreements or rights of set-off or netting of claims, discharge the company's liability to them (*pari passu* if insufficient assets exist to discharge the liabilities in full) and to settle the list of contributories (shareholders) and divide the surplus assets (if any) amongst them in accordance with the rights attaching to the shares.

As soon as the affairs of the company are fully wound up, the liquidator must make up an account of the winding up, showing how the winding up has been conducted and the property of the company has been disposed of, and thereupon call a general meeting of the company for the purposes of laying before it the account and giving an explanation thereof. At least twenty-one (21) days before the final meeting, the liquidator shall send a notice specifying the time, place and object of the meeting to each contributory in any manner authorised by the company's articles of association and published in the Gazette in the Cayman Islands.

(o) **Reconstructions**

There are statutory provisions which facilitate reconstructions and amalgamations approved by a majority in number representing seventy-five per cent. (75%) in value of shareholders or class of shareholders or creditors, as the case may be, as are present at a meeting called for such purpose and thereafter sanctioned by the Court. Whilst a dissenting shareholder would have the right to express to the Court his view that the transaction for which approval is sought would not provide the shareholders with a fair value for their shares, the Court is unlikely to disapprove the transaction on that ground alone in the absence of evidence of fraud or bad faith on behalf of management.

(p) **Compulsory acquisition**

Where an offer is made by a company for the shares of another company and, within four (4) months of the offer, the holders of not less than ninety per cent. (90%) of the shares which are the subject of the offer accept, the offeror may at any time within two (2) months after the expiration of the said four (4) months, by notice in the prescribed manner require the dissenting shareholders to transfer their shares on the terms of the offer. A dissenting shareholder may apply to the Court within one (1) month of the notice objecting to the transfer. The burden is on the dissenting shareholder to show that the Court should exercise its discretion, which it will be unlikely to do unless there is evidence of fraud or bad faith or collusion as between the offeror and the holders of the shares who have accepted the offer as a means of unfairly forcing out minority shareholders.

(q) **Indemnification**

Cayman Islands law does not limit the extent to which a company's articles of association may provide for indemnification of officers and directors, except to the extent any such provision may be held by the court to be contrary to public policy (e.g. for purporting to provide indemnification against the consequences of committing a crime).

## 4. GENERAL

Conyers Dill & Pearman, the Company's special legal counsel on Cayman Islands law, have sent to the Company a letter of advice summarising certain aspects of Cayman Islands company law. This letter, together with a copy of the Companies Law, is available for inspection as referred to in the paragraph headed "Documents available for inspection" in Appendix VII. Any person wishing to have a detailed summary of Cayman Islands company law or advice on the differences between it and the laws of any jurisdiction with which he is more familiar is recommended to seek independent legal advice.

## A. FURTHER INFORMATION ABOUT OUR GROUP

### 1. Incorporation

Our Company is incorporated in the Cayman Islands under the Companies Law as an exempted company with limited liability on 12 October 2009 as Youyuan International Holdings Ltd. Pursuant to special resolutions passed by the then sole Shareholder on 25 November 2009, we changed our name from Youyuan International Holdings Ltd. into Youyuan International Holdings Limited (優源國際控股有限公司).

Our Company has been registered as a non-Hong Kong company under Part XI of the Companies Ordinance and our principal place of business in Hong Kong is at Unit 04, 13/F, Bank of America Tower, No. 12 Harcourt Road, Hong Kong. Mr Wong Yat Sum, the company secretary of our Company, has been appointed as the authorised representative of our Company for the acceptance of service of process and notices in Hong Kong.

As our Company is incorporated in the Cayman Islands, it operates subject to the relevant law of the Cayman Islands and its constitution which comprises a memorandum of association and an articles of association. A summary of the relevant aspects of the Companies Law and certain provisions of Articles of Association is set out in Appendix V to this prospectus.

### 2. Changes in share capital of our Company

(a) As at the date of incorporation of our Company, its authorised share capital was HK$380,000 divided into 3,800,000 Shares with par value of HK$0.10 each. On the same date, one Share with par value of HK$0.10 each was allotted and issued as fully paid at par to Codan Trust Company (Cayman) Limited, which was then transferred to Smart Port.

(b) On 14 January 2010, our Company and Smart Port entered into a share transfer agreement pursuant to which Smart Port transferred its entire interest in Xi Yuan BVI to our Company in consideration of our Company issuing 9,999 Shares credited as fully paid to Smart Port.

(c) On 8 April 2010, Smart Port, Cathay Special Paper, Denron, Everproud, Giantwish, Grand Earning and Best Believe entered into a share repurchase agreement pursuant to which Smart Port repurchased all the Smart Port Preferred Shares held by Cathay Special Paper and all ordinary shares of Smart Port held by each of Denron, Everproud, Giantwish, Grand Earning and Best Believe. As consideration of such repurchases, Smart Port transferred 1,178 Shares to Cathay Special Paper, 316 Shares to Denron, 415 Shares to Everproud, 316 Shares to Giantwish, 316 Shares to Grand Earning and 125 Shares to Best Believe.

Immediately following completion of the Global Offering and the Capitalisation Issue and without taking into account of any Shares which may be issued and allotted pursuant to the exercise of options which may be granted under Share Option Scheme or the exercise of Over-allotment Option, the authorised share capital of the Company will be HK$1,000,000,000 divided into 10,000,000,000 Shares with par value of HK$0.10 each, of which 1,000,000,000 Shares will be issued as fully paid or credited as fully paid, and 9,000,000,000 Shares will remain unissued.

Other than pursuant to the general mandate to issue Shares referred to in the paragraph headed "Written resolutions of the Shareholders passed on 30 April 2010" in this Appendix, the exercise of options which may be granted under Share Option Scheme or the exercise of Over-allotment Option, our Directors do not have any present intention to issue any of the authorised but unissued share capital of the Company and, without prior approval of the Shareholders in general meeting of the Company, no issue of Shares will be made which would effectively alter the control of our Company.

Except as disclosed in this prospectus, there has been no alteration in the share capital of the Company since its incorporation.

**3. Changes in share capital or registered capital of our subsidiaries**

On 28 August 2009, the authorised and issued share capital of Sunwell was increased from HK$10,000 of 10,000 shares with par value of HK$1.00 each to HK$10,000,000 by the creation of an additional of 9,990,000 shares with par value of HK$1.00 each, all of which were allotted and issued to Xi Yuan BVI.

On 4 February 2010, Huaxiang increased its total investment from RMB90,000,000 to RMB138,880,000, and increased its registered capital from RMB60,000,000 to RMB88,890,000.

Except as set out in "History and Corporate Structure — Reorganisation" in this prospectus, there has been no alternation in the share capital or registered capital of any of our subsidiaries of our Company within the two years immediately preceding the date of this prospectus.

**4. Written resolutions of our Shareholders passed on 30 April 2010**

Pursuant to the written resolutions of all Shareholders entitled to vote at general meetings of our Company, which were passed on 30 April 2010:

(a) the authorised share capital of our Company was increased from 3,800,000 Shares to 10,000,000,000 Shares by the creation of 9,996,200,000 Shares with par value of HK$0.10 each, which rank pari passu in all respects with the Shares in issue as of the date of passing of the written resolutions;

(b) conditional on the share premium account of our Company being credited as a result of the Global Offering, the sum of HK$74,999,000 be capitalised and be applied in paying up in full at par 749,990,000 Shares for allotment and issue to the Shareholders whose names were on the register of members of our Company as of the close of business on 30 April 2010 and the Shares to be allotted and issued pursuant to the written resolutions shall rank pari passu in all respects with the existing issued Shares;

(c) conditional on (i) the Listing Committee of the Stock Exchange granting the listing of, and permission to deal in, the Shares in issue and to be issued (pursuant to the Global Offering) as mentioned in the prospectus; and (ii) the obligations of the Underwriters under the Underwriting Agreements becoming unconditional (including, if relevant, as a result of the waiver of any condition(s) by the Sole Global Coordinator (on behalf of the Underwriters)) and the Underwriting Agreements not being terminated in accordance with their terms or otherwise:

   (i) the Global Offering were approved and our Directors were authorised to allot and issue the Offer Shares and subject to the terms and conditions stated in this prospectus and in the relevant Application Forms; and

   (ii) the rules of the Share Option Scheme, the principal terms of which are set out in "Share Option Scheme" in this Appendix, were approved and adopted and our Directors or any committee established by the Board were authorised, at their sole discretion, to (i) administer the Share Option Scheme; (ii) modify or amend the Share Option Scheme from time to time as requested by the Stock Exchange; (iii) grant options to subscribe for Shares under the Share Option Scheme up to the limit referred to in such Scheme; (iv) allot, issue and deal with Shares pursuant to the exercise of options granted under the Share Option Scheme; (v) make application at the appropriate time or times to the Stock Exchange for the listing of, and permission to deal in, any Shares or any part thereof that may from time to time be issued and allotted pursuant to the exercise of options granted under the Share Option Scheme; and (vi) to take all such actions as they consider necessary and/or desirable to implement and give effect to the Share Option Scheme;

(d) a general unconditional mandate was given to our Directors to exercise all the powers of our Company to allot, issue and deal with (including the power to make an offer or agreement, or grant securities which would or might require Shares to be allotted and issued), otherwise than by way of Rights Issue, or pursuant to any scrip dividend schemes or similar arrangements providing for the allotment and issue of Shares in lieu of the whole or part of a dividend on Shares in accordance with the Articles of Association or pursuant to the issue of Shares upon the exercise of any subscription rights attached to any warrants of our Company and may be granted under the Share Option Scheme or any other option scheme(s) or similar arrangement for the time being adopted for the grant or issue to directors and/or officers and/or employees of our Group or rights to acquire Shares or pursuant to a specific authority granted by the Shareholders in general meeting, the Shares with an aggregate nominal amount not exceeding 20% of the aggregate nominal amount of the share capital of our Company in issue immediately following completion of the Global Offering;

For the purpose of this paragraph, "Rights Issue" means an offer of our Shares, or offer or issue of warrants, options or other securities giving rights to subscribe for our Shares open for a period fixed by our Directors to holders of our Shares on the register on a fixed record date in proportion to their holdings of our Shares (subject to such exclusion or other arrangements as our Directors may deem necessary or expedient in relation to fractional entitlements, or having regard to any restrictions or obligations under the laws of, or the requirements of, or the expense or delay which may be involved in determining the existence or extent of any restrictions or obligations under the laws of, or the requirements of, any jurisdiction applicable to our Company, or any recognised regulatory body or any stock exchange applicable to our Company);

(e) a general unconditional mandate was given to our Directors to exercise all powers of our Company to repurchase on the Stock Exchange, or on any other stock exchange on which the securities of our Company may be listed and which is recognised by the SFC and the Stock Exchange for this purpose, such number of Shares with an aggregate nominal value not exceeding 10% of the aggregate nominal amount of the share capital of our Company in issue immediately following completion of the Global Offering and the Capitalisation Issue but before the exercise of the Over-allotment Option;

(f) the extension of the general mandate to allot, issue and deal with Shares as mentioned in paragraph (d) above by the addition to the aggregate nominal value of the share capital of our Company which may be allotted or agreed conditionally or unconditionally to be allotted by our Directors pursuant to such general mandate of an amount representing the aggregate nominal value of the share capital of our Company repurchased by our Company pursuant to paragraph (e) above, provided that such extended amount shall not exceed 10% of the aggregate of the total nominal value of the share capital of our Company in issue immediately following the Global Offering; and

(g) the adoption of the Articles of Association.

Each of the general mandates referred to in paragraphs (d), (e) and (f) above will remain in effect until whichever is the earliest of:

(1) the conclusion of our next annual general meeting, unless renewed by an ordinary resolution of our Shareholders in a general meeting, either unconditionally or subject to conditions;

(2) the expiration of the period within which we are required by any applicable law or the Articles of Association to hold our next annual general meeting; or

(3) the time when such mandate is varied or revoked by an ordinary resolution of our Shareholders in a general meeting.

**5. Repurchase of our Shares**

This section includes information relating to the repurchases of securities, including information required by the Stock Exchange to be included in this prospectus concerning such repurchase.

(1) ***Provisions of the Listing Rules***

The Listing Rules permit companies whose primary listing is on the Stock Exchange to repurchase their securities on the Stock Exchange subject to certain restrictions, the most important restrictions are summarised below:

(i) *Shareholders' approval*

All proposed repurchases of Shares must be approved in advance by an ordinary resolution of the Shareholders in a general meeting, either by way of general mandate or by specific approval in relation to a particular transaction.

Pursuant to the written resolutions passed on 30 April 2010 by all our Shareholders, a general unconditional mandate (the "Repurchase Mandate") was given to our Directors to exercise all powers of our Company to repurchase Shares (Shares which may be listed on the Stock Exchange) with a total nominal value of not more than 10 per cent of the aggregate nominal value of our share capital in issue or to be issued immediately following the completion of the Global Offering (without taking into account the exercise of the Over-Allotment Option), details of which have been described above in the paragraph headed "Written resolutions of our Shareholders passed on 30 April 2010".

(ii) *Source of funds*

Any repurchases of Shares by us must be paid out of funds legally available for the purpose in accordance with our Articles of Association, the Listing Rules and the Companies Law. We are not permitted to repurchase our Shares on the Stock Exchange for a consideration other than cash or for settlement otherwise than in accordance with the trading rules of the Stock Exchange from time to time.

(iii) *Shares to be repurchased*

The Listing Rules provide that the Shares which are proposed to be repurchased by us must be fully-paid up.

(2) ***Reasons for repurchases***

Our Directors believe that it is in the best interests of our Company and our Shareholders for our Directors to have general authority from the shareholders to enable them to repurchase Shares in the market. Such repurchases may, depending on market conditions and funding arrangements at the time, lead to an enhancement of the net asset value per Share and/or earnings per Share and will only be made where our Directors believe that such repurchases will benefit our Company and our Shareholders.

(3) ***Funding of repurchases***

In repurchasing Shares, we may only apply funds legally available for such purpose in accordance with our Memorandum of Association and Articles of Association, the Listing Rules, the Companies Law and the applicable laws and regulations of the Cayman Islands.

On the basis of the current financial position of our Company as disclosed in this prospectus and taking into account its current working capital position, our Directors consider that, if the Repurchase Mandate is exercised in full, it might have a material adverse effect on our working capital and/or gearing position as compared with the position disclosed in this prospectus. However, our Directors do not propose to exercise the Repurchase Mandate to such an extent as would, in the circumstances, have a material adverse effect on our working capital requirements or the gearing levels which in the opinion of our Directors are from time to time appropriate for us.

(4) ***General***

None of our Directors nor, to the best of their knowledge having made all reasonable enquiries, any of their associates (as defined in the Listing Rules) currently intends to sell any Shares to us.

Our Directors have undertaken to the Stock Exchange that, so far as the same may be applicable, they will exercise the Repurchase Mandate in accordance with the Listing Rules and the applicable laws and regulations of the Cayman Islands.

If, as a result of any repurchase of Shares, a shareholder's proportionate interest in the voting rights is increased, such increase will be treated as an acquisition for the purposes of the Takeovers Code. Accordingly, a shareholder or a group of shareholders acting in concert could obtain or consolidate control of us and become obliged to make a mandatory offer in accordance with rule 26 of the Takeovers Code. Except as mentioned above, our Directors are not aware of any consequences which would arise under the Takeovers Code as a consequence of any repurchases pursuant to the Repurchase Mandate.

We have not made any repurchases of our own securities in the past six months.

No connected person has notified us that he or she has a present intention to sell Shares to us, or has undertaken not to do so, if the Repurchase Mandate is exercised.

**B. REORGANISATION**

Our Group underwent the Reorganisation prior to the Listing which involved the following steps:

(a) Establishment of our offshore shareholding structure;

(b) Restructuring of our PRC operating subsidiaries; and

(c) Repurchase of Smart Port Preferred Shares and ordinary shares of Smart Port held by each of Denron, Everproud, Giantwish, Grand Earning and Best Believe by Smart Port.

For further details of the Reorganisation, please refer to "History and Corporate Structure — Reorganisation" in this prospectus.

## C. FURTHER INFORMATION ABOUT OUR BUSINESS

### 1. Summary of the material contracts

The following contracts (not being contracts entered into in the ordinary course of business) were entered into by our Group within the two years preceding the date of this prospectus and are or may be material:

(a) an equity transfer agreement dated 23 July 2008 entered into between YLF Trading, Uniland and Sunwell in relation to the transfer of 94.92% equity interest in Youlanfa from Uniland to Sunwell for a consideration of US$1.00;

(b) a supplemental agreement dated 23 July 2008 entered into between YLF Trading and Sunwell in relation to the transfer of 94.92% equity interest in Youlanfa from Uniland to Sunwell;

(c) an equity interest transfer agreement dated 26 December 2008 entered into between Zhangzhou Shunxiong Trading Co., Ltd. (漳州順雄貿易有限公司) and Sunwell in relation to the transfer of 3.5% equity interest in Xiyuan from Zhangzhou Shunxiong Trading Co., Ltd. (漳州順雄貿易有限公司) to Sunwell for a consideration of HK$2,414,300;

(d) an equity interest transfer agreement dated 15 July 2009 entered into between YLF Trading and Sunwell in relation to the transfer of 5.08% equity interest in Youlanfa from YLF Trading to Sunwell for a consideration of RMB10,580,000;

(e) an equity interest transfer agreement dated 13 August 2009 entered into between YLF Industry and Sunwell in relation to the transfer of 5% equity interest in Huaxiang from YLF Industry to Sunwell for a consideration of RMB8,880,000;

(f) the Cathay Subscription Agreement;

(g) the Supplemental Deed;

(h) the Smart Port Loan Agreement;

(i) a shareholder loan agreement dated 27 August 2009 entered into between Xi Yuan BVI and Smart Port in relation to a shareholder loan of US$10.00 million from Smart Port to Xi Yuan BVI;

(j) a shareholder loan agreement dated 10 December 2009 entered into between Xi Yuan BVI and Smart Port in relation to a shareholder loan of US$10.58 million from Smart Port to Xi Yuan BVI;

(k) a share transfer agreement dated 14 January 2010 entered into between our Company, Smart Port and Mr Ke in relation to the transfer of 100% interest in Xi Yuan BVI from Smart Port to our Company in consideration of our Company issuing 9,999 Shares to Smart Port;

(l) a deed of adherence dated 14 January 2010 entered into between Mr Ke, Best Believe, Denron, Everproud, Giantwish, Grand Earning, Cathay Special Paper, Xi Yuan BVI, Smart Port, Sunwell and Mr Ke Jixiong in connection with the deed of transfer relating to the shares of Smart Port whereby Best Believe, Denron, Everproud, Giantwish and Grand Earning agreed to be bound by the same duties, burdens and obligations of Smart Port under the Cathay Subscription Agreement;

(m) a deed of waiver dated 5 May 2010 entered by Smart Port in favour of Xi Yuan BVI in relation to Smart Port waiving all its rights under the shareholder's loans provided to Xi Yuan BVI totalling US$20.58 million;

(n) a placing agreement dated 11 May 2010 entered into between our Company, SD Family Fund L.P. and HSBC in relation to the subscription of International Offer Shares at the Offer Price up to HK$120,000,000 by SD Family Fund L.P.;

(o) the Deed of Non-competition;

(p) the Hong Kong Underwriting Agreement; and

(q) the Deed of Indemnity.

## 2. Intellectual Property Rights of our Group

### *Trademarks*

As at the Latest Practicable Date, we have registered the following trademarks:

| Trademark | Place of Registration | Class | Registration Number | Expiry Date |
|---|---|---|---|---|
| You lan fa 优兰发 ............. | PRC | 1 | 3628362 | 13 May 2015 |
| You lan fa 优兰发 ............. | PRC | 2 | 3628361 | 20 July 2015 |
| You lan fa 优兰发 ............. | PRC | 3 | 3628360 | 6 November 2015 |

| Trademark | Place of Registration | Class | Registration Number | Expiry Date |
|---|---|---|---|---|
| You lan fa 优兰发 | PRC | 4 | 3628359 | 6 March 2015 |
| You lan fa 优兰发 | PRC | 5 | 3628358 | 20 November 2015 |
| 小秀才秀 XIAOXIUCAIXIU | PRC | 5 | 5308604 | 20 October 2019 |
| You lan fa 优兰发 | PRC | 6 | 3628357 | 13 February 2015 |
| You lan fa 优兰发 | PRC | 7 | 3628356 | 6 November 2015 |
| You lan fa 优兰发 | PRC | 14 | 3628355 | 6 September 2015 |
| You lan fa 优兰发 | PRC | 15 | 3628354 | 6 June 2015 |
| You lan fa 优兰发 | PRC | 16 | 1805722 | 13 July 2012 |
| YouLan 优兰 | PRC | 16 | 1924513 | 27 December 2012 |
| 优岛 YOUDAO | PRC | 16 | 1925811 | 27 December 2012 |
| LANYOU 兰优 | PRC | 16 | 1925812 | 13 February 2013 |
| | PRC | 16 | 3278753 | 20 December 2013 |

| Trademark | Place of Registration | Class | Registration Number | Expiry Date |
|---|---|---|---|---|
| 优岛 YOU DAO | PRC | 16 | 3282522 | 27 November 2013 |
| 文举人举 WENJURENJU | PRC | 16 | 3437148 | 27 November 2014 |
| 金状元状 JINZHUANGYUANZHUANG | PRC | 16 | 3437149 | 27 November 2014 |
| 大学士学 DAXUESHIXUE | PRC | 16 | 3437150 | 27 November 2014 |
| 小秀才秀 XIAOXIUCAIXIU | PRC | 16 | 3437151 | 27 November 2014 |
| You lan fa 优兰发 | Macau | 16 | N/045720 | 8 February 2017 |
| 小神童•神 | PRC | 16 | 4493785 | 20 July 2018 |
| 奔冠 | PRC | 16 | 5969694 | 20 December 2019 |
| 小秀才•秀 XIAOXIUCAIXIU | PRC | 16 | 6294102 | 27 February 2020 |
| YouLanFa | PRC | 16 | 6294103 | 27 February 2020 |
| You lan fa 优兰发 | PRC | 17 | 3628353 | 20 April 2015 |
| You lan fa 优兰发 | PRC | 18 | 3628352 | 6 January 2016 |
| 小秀才秀 XIAOXIUCAIXIU | PRC | 18 | 5308600 | 6 August 2019 |

| Trademark | Place of Registration | Class | Registration Number | Expiry Date |
|---|---|---|---|---|
| You lan fa 优兰发 | PRC | 19 | 3628351 | 20 September 2015 |
| You lan fa 优兰发 | PRC | 22 | 3628350 | 27 October 2015 |
| You lan fa 优兰发 | PRC | 23 | 3628349 | 20 November 2015 |
| You lan fa 优兰发 | PRC | 24 | 3628348 | 6 November 2015 |
| You lan fa 优兰发 | PRC | 25 | 3628347 | 13 April 2016 |
| You lan fa 优兰发 | PRC | 26 | 3628346 | 6 December 2015 |
| You lan fa 优兰发 | PRC | 27 | 3628345 | 13 December 2015 |
| You lan fa 优兰发 | PRC | 29 | 3628344 | 6 February 2015 |
| 小秀才秀 XIAOXIUCAIXIU | PRC | 29 | 5308599 | 6 June 2019 |
| You lan fa 优兰发 | PRC | 31 | 3629043 | 13 April 2015 |
| You lan fa 优兰发 | PRC | 32 | 3629042 | 6 February 2015 |

| Trademark | Place of Registration | Class | Registration Number | Expiry Date |
|---|---|---|---|---|
| 小秀才秀 XIAOXIUCAIXIU . . . . . . . . . . . | PRC | 32 | 5308598 | 6 July 2019 |
| You lan fa 优兰发 . . . . . . . . . . . . . . | PRC | 33 | 3629041 | 13 March 2015 |
| You lan fa 优兰发 . . . . . . . . . . . . . . | PRC | 34 | 3629040 | 6 February 2015 |
| You lan fa 优兰发 . . . . . . . . . . . . . . | PRC | 35 | 3629039 | 13 August 2015 |
| You lan fa 优兰发 . . . . . . . . . . . . . . | PRC | 37 | 3629038 | 6 October 2015 |
| You lan fa 优兰发 . . . . . . . . . . . . . . | PRC | 38 | 3629037 | 20 June 2015 |
| You lan fa 优兰发 . . . . . . . . . . . . . . | PRC | 39 | 3629036 | 20 June 2015 |
| You lan fa 优兰发 . . . . . . . . . . . . . . | PRC | 40 | 3629035 | 13 August 2015 |
| You lan fa 优兰发 . . . . . . . . . . . . . . | PRC | 41 | 3629034 | 6 April 2015 |
| You lan fa 优兰发 . . . . . . . . . . . . . . | PRC | 42 | 3629033 | 13 November 2015 |
| You lan fa 优兰发 . . . . . . . . . . . . . . | PRC | 43 | 3629032 | 20 October 2015 |

| Trademark | Place of Registration | Class | Registration Number | Expiry Date |
|---|---|---|---|---|
| | PRC | 44 | 3629031 | 6 August 2015 |
| | Designations under the Madrid Agreement and Protocol *(Note)* | 16 | 869209 | 28 February 2015 |
| | United States of America | Int. Cl 16 | 3145756 | 28 February 2015 |
| | Hong Kong | 16 | 300880146 | 28 May 2017 |

*Note:* This mark was registered in Albania, Algeria, Austria, Australia, Belarus, Croatia, Czech Republic, Democratic People's Republic of Korea, Egypt, Finland, France, Germany, Hungary, Italy, Kenya, Latvia, Morocco, Poland, Republic of Korea, Romania, Russian Federation, Singapore, Slovakia, Spain, Switzerland, United Kingdom, Ukraine and Viet Nam through designations under the Madrid Agreement and Protocol.

As at the Latest Practicable Date, we made applications for the registration of the following trademarks:

| Trademark | Place of Application | Class | Application Number | Application Date |
|---|---|---|---|---|
| | PRC | 16 | 5969693 | 30 March 2007 |
| | PRC | 16 | 6521565 | 21 January 2008 |
| | PRC | 16 | 6521546 | 21 January 2008 |
| | Hong Kong | 16 | 301495846 | 10 December 2009 |

*Notes: International classification of Goods/Services*

| | |
|---|---|
| Class 1: | Chemicals used in industry, science and photography, as well as in agriculture, horticulture and forestry; unprocessed artificial resins, unprocessed plastics; manures; fire extinguishing compositions; tempering and soldering preparations; chemical substances for preserving foodstuffs; tanning substances; adhesives used in industry. |
| Class 2: | Paints, varnishes, lacquers; preservatives against rust and against deterioration of wood; colorants; mordants; raw natural resins; metals in foil and powder form for painters, decorators, printers and artists. |
| Class 3: | Bleaching preparations and other substances for laundry use; cleaning, polishing, scouring and abrasive preparations; soaps; perfumery, essential oils, cosmetics, hair lotions; dentifrices. |
| Class 4: | Industrial oils and greases; lubricants; dust absorbing, wetting and binding compositions; fuels (including motor spirit) and illuminants; candles and wicks for lighting. |
| Class 5: | Pharmaceutical and veterinary preparations; sanitary preparations for medical purposes; dietetic substances adapted for medical use, food for babies; plasters, materials for dressings; material for stopping teeth, dental wax; disinfectants; preparations for destroying vermin; fungicides, herbicides. |
| Class 6: | Common metals and their alloys; metal building materials; transportable buildings of metal; materials of metal for railway tracks; non-electric cables and wires of common metal; ironmongery, small items of metal hardware; pipes and tubes of metal; safes; goods of common metal not included in other classes; ores. |
| Class 7: | Machines and machine tools; motors and engines (except for land vehicles); machine coupling and transmission components (except for land vehicles); agricultural implements other than hand-operated; incubators for eggs. |
| Class 14: | Precious metals and their alloys and goods in precious metals or coated therewith, not included in other classes; jewellery, precious stones; horological and chronometric instruments. |
| Class 15: | Musical instruments. |
| Class 16: | Paper, cardboard and goods made from these materials, not in other classes; printed matter; bookbinding material; photographs; stationery; adhesives for stationery or household purposes; artists' materials; instructional and teaching material (except apparatus); type; printing blocks. |
| Class 17: | Rubber, gutta-percha, gum, asbestos, mica and goods made from these materials and not included in other classes; plastics in extruded form for use in manufacture; packing, stopping and insulating materials; flexible pipes, not of metal. |
| Class 18: | Leather and imitations of leather, and goods made of these materials and not included in other classes; animal skins, hides; trunks and travelling bags; umbrellas, parasols and walking sticks; whips, harness and saddlery. |
| Class 19: | Building materials (non-metallic); non-metallic rigid pipes for building; asphalt, pitch and bitumen; non-metallic transportable buildings; monuments, not of metal. |
| Class 22: | Ropes, string, nets, tents, awnings, tarpaulins, sails, sacks and bags (not included in other classes); padding and stuffing materials (except of rubber or plastics); raw fibrous textile materials. |
| Class 23: | Yarns and threads, for textile use. |

| | |
|---|---|
| Class 24: | Textiles and textile goods, not included in other classes; bed and table covers. |
| Class 25: | Clothing, footwear, headgear. |
| Class 26: | Lace and embroidery, ribbons and braid; buttons, hooks and eyes, pins and needles; artificial flowers. |
| Class 27: | Carpets, rugs, mats and matting, linoleum and other materials for covering existing floors; wall hangings (non-textile). |
| Class 28: | Games and playthings; gymnastic and sporting articles not included in other classes; decorations for Christmas trees. |
| Class 29: | Meat, fish, poultry and game; meat extracts; preserved, frozen, dried and cooked fruits and vegetables; jellies, jams, compotes; eggs, milk and milk products; edible oils and fats. |
| Class 31: | Agricultural, horticultural and forestry products and grains not included in other classes; live animals; fresh fruits and vegetables; seeds, natural plants and flowers; foodstuffs for animals; malt. |
| Class 32: | Beers; mineral and aerated waters and other non-alcoholic drinks; fruit drinks and fruit juices; syrups and other preparations for making beverages. |
| Class 33: | Alcoholic beverages (except beers). |
| Class 34: | Tobacco; smokers' articles; matches. |
| Class 35: | Advertising; business management; business administration; office functions. |
| Class 37: | Building construction; repair; installation services. |
| Class 38: | Telecommunications. |
| Class 39: | Transport; packaging and storage of goods; travel arrangement. |
| Class 40: | Treatment of materials. |
| Class 41: | Education; providing of training; entertainment; sporting and cultural activities. |
| Class 42: | Scientific and technological services and research and design relating thereto; industrial analysis and research services; design and development of computer hardware and software. |
| Class 43: | Services for providing food and drink; temporary accommodation. |
| Class 44: | Medical services; veterinary services; hygienic and beauty care for human beings or animals; agriculture, horticulture and forestry services. |

***Domain Names***

As of the Latest Practicable Date, we have registered the following domain names:

| Domain Name | Registration Date | Expiry Date |
|---|---|---|
| youlanfa.com . . . . . . . . . . . . . . . . . . . . . . . . | 20 April 2002 | 20 April 2015 |
| youyuan.com.hk . . . . . . . . . . . . . . . . . . . . . . | 22 February 2010 | 22 February 2011 |

### *Designs*

As of the Latest Practicable Date, we have registered the following designs:

| Type | Place of Application | Registration Number | Expiry Date |
|---|---|---|---|
| Wrapping bag (Xiaoshentongshen) (包裝袋(小神童•神)) . . . . . . . . . . . . | PRC | ZL 2006 30138948.X | 28 September 2016 |
| Wrapping paper (Xiaoxiucaixiu) (包裝紙(小秀才•秀)) . . . . . . . . . . . . | PRC | ZL 2006 30138949.4 | 28 September 2016 |

### *Patents*

As of the Latest Practicable Date, we have registered the following patents:

| Patents | Place of Registration | Patent Number | Expiry Date |
|---|---|---|---|
| A vacuum water separation machine* (一種真空泵汽水分離器) . . . . . . . . . | PRC | ZL 2007 20006361.2 | 9 February 2017 |
| A device for clarification and adding treatment to sewage water* (一種污水澄清加藥裝置). . . . . . . . . . | PRC | ZL 2007 20006413.6 | 13 February 2017 |
| A method of manufacturing copying paper* (一種拷貝紙生產方法) . . . . . . | PRC | ZL 2007 10008633.7 | 13 February 2027 |
| A cloth roller guiding system for paper manufacturing machines* (造紙機用毛毯導輥系統). . . . . . . . . . | PRC | ZL 2008 20139799.2 | 27 October 2018 |
| A air and pressure filter device for dirt and debris* (氣動送泥污泥壓濾裝置). | PRC | ZL 2008 20139800.1 | 27 October 2018 |

***Copyrights of computer software***

As of the Latest Practicable Date, we have registered the following copyrights:

| Name of Software Registered as a Copyrighted Work | Place of Registration | Software Product Registration Number | Development Completion Date |
|---|---|---|---|
| Paper manufacturing quality management information system version 2.0* (造紙生產質量管理信息系統v2.0) | PRC | 2009SR035913 | 1 December 2008 |
| Paper manufacturing costs analysis information system version 2.0* (造紙生產成本分析信息系統v2.0) | PRC | 2009SR036351 | 3 December 2008 |

Except as disclosed in this sub-section headed "Intellectual property rights of our Group", there are no other trade or service marks, patents, other intellectual property rights which are or may be material in relation to our business.

**3. Further information about our PRC establishments**

(a) ***Youlanfa***

| | | |
|---|---|---|
| (i) | nature of the company: | Wholly-foreign owned enterprise |
| (ii) | incorporation date: | 11 November 1994 |
| (iii) | term of business operation: | 50 years commencing on 11 November 1994 and expiring on 11 November 2044 |
| (iv) | registered capital: | RMB128,880,000 |
| (v) | total investment: | RMB158,880,000 |
| (vi) | attributable interest of the company: | 100% |
| (vii) | scope of business: | Acquisitions of domestic waste paper, production of recycled paper, and production of specialty and cultural paper (excluding marketing materials prohibited by the PRC Government and restricted products) |

(b) ***Xiyuan***

| | | |
|---|---|---|
| (i) | nature of the company: | Wholly-foreign owned enterprise |
| (ii) | incorporation date: | 18 January 2006 |
| (iii) | term of business operation: | 50 years commencing on 18 January 2006 and expiring on 17 January 2056 |
| (iv) | registered capital: | HK$68,980,000 |
| (v) | total investment: | HK$172,450,000 |
| (vi) | attributable interest of the company: | 100% |
| (vii) | scope of business: | production of high grade paper and specialty paper and related paper product; Import and export of goods and (excluding distribution) technologies |

(c) ***Huaxiang***

| | | |
|---|---|---|
| (i) | nature of the company: | Wholly-foreign owned enterprise |
| (ii) | Incorporation date: | 9 March 2006 |
| (iii) | term of business operation: | 50 years commencing on 9 March 2006 and expiring on 8 March 2056 |
| (iv) | registered capital: | RMB88,890,000 |
| (v) | total investment: | RMB138,880,000 |
| (vi) | attributable interest of the company: | 100% |
| (vii) | scope of business: | production of specialty paper product (excluding printing) |

## D. FURTHER INFORMATION ABOUT THE DIRECTORS

### 1. Service contracts and letters of appointment of our Directors

Each of our executive Directors has entered into a service contract with us for an initial fixed term of 3 years commencing from the Listing Date and will continue, subject to approval of our Shareholders in our general meetings, until terminated by not less than 3 months' notice in writing served by either party on the other, which notice shall not expire until after the fixed term.

Each of Mr Paul Steven Wolansky, our non-executive Director, Prof. Zhang Daopei (張道沛), Prof. Chen Lihui (陳禮輝) and Mr Chow Kwok Wai (周國偉), our independent non-executive Directors, has entered into a letter of appointment with our Company on 30 April 2010. Each letter of appointment is for an initial term of 3 years commencing from the Listing Date.

Each of our Directors is entitled to the respective basic fees set out below. Each of the executive Directors is also entitled to a discretionary bonus, provided that the aggregate amount of the bonuses payable to all our executive Directors in respect of any financial year may not exceed 5% of our audited consolidated or combined net profit (after taxation and payment of such bonuses) in respect of that financial year. An executive Director may not vote on any resolution of our Directors regarding the increment of annual salary and the amount of the discretionary bonus payable to him.

The current basic annual fees of our executive Directors, non-executive Director and independent non-executive Directors are as follows:

| Name | Annual Amount |
|---|---|
| | (HK$) |
| Mr Ke Wentuo (柯文托) | 1,580,000 |
| Mr Ke Jixiong (柯吉熊) | 1,280,000 |
| Mr Cao Xu (曹旭) | 160,000 |
| Mr Zhang Guoduan (張國端) | 160,000 |
| Mr Paul Steven Wolansky | 60,000 |
| Prof. Zhang Daopei (張道沛) | 120,000 |
| Prof. Chen Lihui (陳禮輝) | 120,000 |
| Mr Chow Kwok Wai (周國偉) | 180,000 |

Except as disclosed above, none of our Directors has entered or has proposed to enter into any service contract with our Company or any of our subsidiaries (other than contracts expiring or determinable by the employer within 1 year without the payment of compensation (other than statutory compensation)).

**2. Remuneration of the Directors during the Track Record Period**

During the years ended 31 December 2007, 2008 and 2009, the aggregate of the remuneration, including fees, salaries, discretionary bonus, defined contribution plans (including pension), housing and other allowances, and other benefits in kind, paid to our Directors by us and our subsidiaries was approximately RMB906,000, approximately RMB907,000 and approximately RMB907,000, respectively.

Except as disclosed above, no other payments have been made, or are payable, in respect of the three years ended 31 December 2009, by us to our Directors.

Under the arrangements currently in force, we estimate that the aggregate of the remuneration payable to, and benefits in kind receivable by, our Directors (excluding discretionary bonus) for the financial year ending 31 December 2010 will be approximately HK$2,612,000.

## E. DISCLOSURE OF INTERESTS

### 1. Disclosure of Interests

***Interests and short positions of our Directors in our share capital and our associated corporations following the Global Offering and the Capitalisation Issue***

Immediately following completion of the Global Offering and the Capitalisation Issue and taking no account of any Shares which may be allotted and issued pursuant to the Share Option Scheme or the exercise of the Over-allotment Option, the interests or short positions of our Directors and the chief executive in our Shares, underlying Shares and debentures and our associated corporations, within the meaning of Part XV of the SFO which will have to be notified to our Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which he is taken or deemed to have under such provisions of the SFO) or which will be required, pursuant to section 352 of the SFO, to be recorded in the register referred to therein or which will be required to be notified to us and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies contained in the Listing Rules, will be as follows:

Interests and short positions in our Shares, underlying Shares and debentures and our associated corporations:

*Long Positions in our Company*

| Name of director | Capacity/Nature of interest | Number of Shares | Approximate percentage of interest in our Company |
|---|---|---|---|
| Mr Ke | Interest in controlled corporation and interest of spouse[1] | 573,750,000 | 57.38% |
| Mr Ke Jixiong | Interest in controlled corporation[2] | 31,125,000 | 3.11% |
| Mr Paul Steven Wolansky | Interest in controlled corporation[3] | 88,350,000 | 8.84% |

*Note 1:* The 573,750,000 Shares comprise:

(i) 550,050,000 Shares relating to the same block of shares held by Smart Port, which is wholly owned by Mr Ke; and

(ii) 23,700,000 Shares held by Denron, which in turn is wholly beneficially owned by Ms Cai Lishuang, and Mr Ke, being the spouse of Ms Cai Lishuang, is deemed to be interested in the said 23,700,000 Shares held by Denron.

*Note 2:* The 31,125,000 Shares refer to the same block of Shares held by Everproud, which is wholly owned by Mr Ke Jixiong.

*Note 3:* The 88,350,000 Shares refer to the same block of Shares held by Cathay Special Paper, which is wholly owned by Cathay Capital Holdings II, L.P., a limited liability partnership. Cathay Master GP, Ltd. is the general partner of Cathay Capital Holdings II, L.P., in which Mr Paul Steven Wolansky has an effective control of 45%, and pursuant to Part XV of the SFO, Cathay Master GP, Ltd. has *de facto* control and thus Mr Paul Steven Wolansky is deemed to be interested in the same Shares.

***Interests and short positions discloseable under Divisions 2 and 3 of Part XV of the SFO***

Immediately following completion of the Global Offering and the Capitalisation Issue and taking no account of any Shares which may be allotted and issued pursuant to the Share Option Scheme or the exercise of the Over-allotment Option, in addition to the interests disclosed under paragraph (a) above, so far as our Directors are aware, the following persons are expected to have interests or short positions in our Shares or underlying Shares which are required to be disclosed to the provisions of Divisions 2 and 3 of Part XV of the SFO or, are expected to be, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of our Group.

*Interests and short positions in our Shares and underlying Shares:*

| **Name** | **Capacity/Nature of interest** | **Number of Shares** | **Approximate percentage of shareholding** |
|---|---|---|---|
| Smart Port | Beneficial interest[1] | 550,050,000 | 55.01% |
| Ms Cai Lishuang | Interest in controlled corporation and interest of spouse[2] | 573,750,000 | 57.38% |
| Cathay Special Paper | Beneficial interest[3] | 88,350,000 | 8.84% |

*Note 1:* Mr Ke is deemed to be interested in the Shares held by Smart Port by virtue of Smart Port being wholly owned by Mr Ke.

*Note 2:* Ms Cai Lishuang is deemed to be interested in the Shares held by Denron by virtue of Denron being wholly owned by Ms Cai Lishuang. In addition, she is deemed to be interested in the Shares held by Smart Port, which is wholly owned by Mr Ke, by virtue of being the spouse of Mr Ke.

*Note 3:* Paul Steven Wolansky is deemed to be interested in the Shares held by Cathay Special Paper. Cathay Special Paper, which is wholly owned by Cathay Capital Holdings II, L.P., a limited liability partnership. Cathay Master GP, Ltd. is the general partner of Cathay Capital Holdings II, L.P., in which Mr Paul Steven Wolansky has an effective control of 45%, and pursuant to Part XV of the SFO, Cathay Master GP, Ltd. has *de facto* control and thus Mr Paul Steven Wolansky is deemed to be interested in the same Shares.

### 2. Disclaimers

Except as disclosed in the subsection headed "E. Disclosure of interests" of this Appendix VI to this prospectus:

(a) none of our Directors nor any of the parties listed in the section headed "Other Information — Consents of Experts" of this Appendix is interested in the promotion of our Company, or in any assets which have been, within the two years immediately preceding the date of this prospectus, acquired or disposed of by or leased to us or any of its subsidiaries, or are proposed to be acquired or disposed of by or leased to our Company or any of its subsidiaries;

(b) none of our Directors nor any of the parties listed in the section headed "Other Information — Consents of Experts" of this Appendix is materially interested in any contract or arrangement subsisting at the date of this prospectus which is significant in relation to our business; and

(c) none of our Directors or their associates (as defined in the Listing Rules) or the existing Shareholders (who, to the knowledge of our Directors, owns more than 5% of our issued share capital) has any interest in any of the five largest customers or the five largest suppliers of our Group.

## F. SHARE OPTION SCHEME

The following is a summary of principal terms of the Share Option Scheme conditionally approved by a resolution of all the Shareholders passed on 30 April 2010 and adopted by a resolution of the Board on 30 April 2010 (the "Adoption Date"). The terms of the Share Option Scheme are in compliance with the provisions of Chapter 17 of the Listing Rules.

### 1. Purpose

The purpose of the Share Option Scheme is to give the Eligible Persons (as mentioned in the following paragraph) an opportunity to have a personal stake in our Company and help motivate them to optimise their future performance and efficiency to our Group and/or to reward them for their past contributions, to attract and retain or otherwise maintain on-going relationships with such Eligible Persons who are significant to and/or whose contributions are or will be beneficial to the performance, growth or success of our Group, and additionally in the case of Executives (as defined below), to enable our Group to attract and retain individuals with experience and ability and/or to reward them for their past contributions.

### 2. Conditions of the Share Option Scheme

The Share Option Scheme shall come into effect on the date on which the following conditions are fulfilled:

(a) subject to (b) and (c) below, the approval of all the shareholders of our Company for the adoption of the Share Option Scheme;

(b) the approval of the Stock Exchange for the listing of and permission to deal in, a maximum of 100,000,000 Shares to be allotted and issued pursuant to the exercise of the Options in accordance with the terms and conditions of the Share Option Scheme; and

(c) the commencement of dealing of the Shares on the Main Board of the Stock Exchange on the Listing Date.

**3. Who may join**

The Board may, at its absolute discretion, offer options ("Options") to subscribe for such number of Shares in accordance with the terms set out in the Share Option Scheme to:

(a) any executive director of, manager of, or other employee holding an executive, managerial, supervisory or similar position in any member of our Group ("Employee"), any proposed Employee or any full-time or part-time employee, or a person for the time being seconded to work full-time or part-time for any member of our Group ("Executive");

(b) a director or proposed director (including an independent non-executive director) of any member of our Group;

(c) a direct or indirect shareholder of any member of our Group;

(d) a supplier of goods or services to any member of our Group;

(e) a customer, consultant, business or joint venture partner, franchisee, contractor, agent or representative of any member of our Group;

(f) a person or entity that provides design, research, development or other support or any advisory, consultancy, professional or other services to any member of our Group; and

(g) an associate of any of the persons referred to in paragraphs (a) to (f) above.

(The persons referred above are the "Eligible Persons").

**4. Maximum number of Shares**

The maximum number of Shares which may be issued upon exercise of all options to be granted under the Share Option Scheme and any other schemes of our Group shall not in aggregate exceed 10 per cent. of the Shares in issue as of the Listing Date, excluding Shares which may fall to be issued upon the exercise of the Over-allotment Option (the "Scheme Mandate Limit") provided that:

(a) our Company may at any time as the Board may think fit seek approval from our Shareholders to refresh the Scheme Mandate Limit, save that the maximum number of Shares which may be issued upon exercise of all options to be granted under the Share Option Scheme and any other schemes of our Company shall not exceed 10 per cent. of the Shares in issue as of the date of approval by Shareholders in general meeting where the Scheme Mandate Limit is refreshed. Options previously granted under the Share Option Scheme and any other schemes of our Company (including those outstanding, cancelled, lapsed or exercised in accordance with the terms of the Share Option Scheme or any other schemes of our Company) shall not be counted for the purpose of calculating the Scheme Mandate Limit as refreshed. Our Company shall send to our Shareholders a circular containing the details and information required under the Listing Rules.

(b) Our Company may seek separate approval from our Shareholders in general meeting for granting Options beyond the Scheme Mandate Limit, provided that the Options in excess of the Scheme Mandate Limit are granted only to the Eligible Person specified by our Company before such approval is obtained. Our Company shall issue a circular to our Shareholders containing the details and information required under the Listing Rules.

(c) The maximum number of Shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the Share Option Scheme and any other schemes of our Group shall not exceed 30% of our Company's issued share capital from time to time. No options may be granted under the Share Option Scheme and any other share option scheme of our Company if this will result in such limit being exceeded.

**5. Maximum entitlement of each participant**

No Option may be granted to any one person such that the total number of Shares issued and to be issued upon exercise of Options granted and to be granted to that person in any 12 month period exceeds 1% of our Company's issued share capital from time to time. Where any further grant of Options to such an Eligible Person would result in the Shares issued and to be issued upon exercise of all Options granted and to be granted to such Eligible Person (including exercised, cancelled and outstanding Options) in the 12-month period up to and including the date of such further grant representing in aggregate over 1 per cent. of the Shares in issue, such further grant shall be separately approved by the shareholders of our Company in general meeting with such Eligible Person and his associates abstaining from voting. Our Company shall send a circular to our Shareholders disclosing the identity of the Eligible Person, the number and terms of the Options to be granted (and Options previously granted) to such Eligible Person, and containing the details and information required under the Listing Rules. The number and terms (including the subscription price) of the Options to be granted to such Eligible Person must be fixed before the approval of our Company's shareholders and the date of the Board meeting proposing such grant shall be taken as the offer date for the purpose of calculating the subscription price of those Options.

**6. Offer and grant of Options**

Subject to the terms of the Share Option Scheme, the Board shall be entitled at any time within 10 years from the Adoption Date to offer the grant of an Option to any Eligible Person as the Board may in its absolute discretion select to subscribe at the subscription price for such number of Shares as the Board may (subject to the terms of the Share Option Scheme) determine (provided the same shall be a board lot for dealing in the Shares on the Stock Exchange or an integral multiple thereof).

**7. Granting Options to Connected Persons**

Subject to the terms in the Share Option Scheme, only insofar as and for so long as the Listing Rules require, where any offer of an Option is proposed to be made to a director, chief executive or a substantial shareholder (as defined in the Listing Rules) of our Company or any of their respective associates, such offer must first be approved by the independent non-executive Directors of our Company (excluding the independent non-executive Director who or whose associates is the grantee of an Option).

Where any grant of Options to a substantial shareholder (as defined in the Listing Rules) or an independent non-executive Director of our Company, or any of their respective associates, would result in the securities issued and to be issued upon exercise of all Options already granted and to be granted (including Options exercised, cancelled and outstanding) to such person in the 12-month period up to and including the date of such grant:

(a) representing in aggregate over 0.1% of the relevant class of securities in issue; and

(b) (where the securities are listed on the Stock Exchange), having an aggregate value, based on the closing price of the securities at the date of each grant, in excess of HK$5 million,

such further grant of Options must be approved by shareholders of our Company (voting by way of a poll). Our Company shall send a circular to Shareholders containing the information required under the Listing Rules. All Connected Persons of our Company must abstain from voting in favour at such general meeting.

Approval from the shareholders of our Company is required for any change in the terms of Options granted to a participant who is a substantial shareholder or an independent non-executive Director of our Company, or any of their respective associates.

**8. Offer period and number accepted**

An offer of the grant of an Option shall remain open for acceptance by the Eligible Person concerned for a period of 28 days from the offer date provided that no such grant of an Option may be accepted after the expiry of the effective period of the Share Option Scheme. An Option shall be deemed to have been granted and accepted by the Eligible Person and to have taken effect when the duplicate offer letter comprising acceptance of the offer of the Option duly signed by the Grantee together with a remittance in favour of our Company of HK$1.00 by way of consideration for the grant thereof is received by our Company on or before the date upon which an offer of an Option must be accepted by the relevant Eligible Person, being a date not later than 28 days after the Offer Date (the "Acceptant Date"). Such remittance shall in no circumstances be refundable.

Any offer of the grant of an Option may be accepted in respect of less than the number of Shares in respect of which it is offered provided that it is accepted in respect of board lots for dealing in Shares on the Stock Exchange or an integral multiple thereof and such number is clearly stated in the duplicate offer letter comprising acceptance of the offer of the Option. To the extent that the offer of the grant of an Option is not accepted by the Acceptance Date, it will be deemed to have been irrevocably declined.

**9. Restriction on the time of grant of Options**

The Board shall not grant any Option under the Share Option Scheme after a price sensitive development has occurred or a price sensitive matter has been the subject of a decision until such price sensitive information has been announced pursuant to the requirements of the Listing Rules. In particular, no Option shall be granted during the period commencing one month immediately preceding the earlier of the date of the Board meeting (as such date is first notified to the Stock Exchange in accordance with the Listing Rules) for the approval of our Company's results for any year, half-year, quarterly or any other interim period (whether or not required under the Listing Rules) and the deadline for our Company to publish an announcement of its results for any year or half-year under the Listing Rules, or quarterly or any other interim period (whether or not required under the Listing Rules), and ending on the date of the results announcements.

**10. Minimum holding period, vesting and performance target**

Subject to the provisions of the Listing Rules, the Board may in its absolute discretion when offering the grant of an Option impose any conditions, restrictions or limitations in relation thereto in addition to those set forth in the Share Option Scheme as the Board may think fit (to be stated in the letter containing the offer of the grant of the Option) including (without prejudice to the generality of the foregoing) qualifying and/or continuing eligibility criteria, conditions, restrictions or limitations relating to the achievement of performance, operating or financial targets by our Company and/or the grantee, the satisfactory performance or maintenance by the grantee of certain conditions or obligations or the time or period before the right to exercise the Option in respect of all or any of the Shares shall vest provided that such terms or conditions shall not be inconsistent with any other terms or conditions of the Share Option Scheme. For the avoidance of doubt, subject to such terms and conditions as the Board may determine as aforesaid (including such terms and conditions in relation to their vesting, exercise or otherwise) there is no minimum period for which an Option must be held before it can be exercised and no performance target which need to be achieved by the grantee before the Option can be exercised.

**11. Amount payable for Options**

The amount payable on acceptance of an Option is HK$1.00.

**12. Subscription price**

The subscription price in respect of any particular Option shall be such price as the Board may in its absolute discretion determine at the time of grant of the relevant Option (and shall be stated in the letter containing the offer of the grant of the Option) but the subscription price shall not be less than whichever is the highest of:

(a) the nominal value of a Share;

(b) the closing price of a Share as stated in the Stock Exchange's daily quotations sheet on the offer date; and

(c) the average closing price of a Share as stated in the Stock Exchange's daily quotation sheets for the 5 business days (as defined in the Listing Rules) immediately preceding the offer date.

**13. Exercise of Option**

(i) An Option shall be exercised in whole or in part (but if in part only, in respect of a Board Lot or any integral multiple thereof) within the Option Period in the manner as set out in this Share Option Scheme by the grantee (or his legal personal representative(s)) by giving notice in writing to our Company stating that the Option is thereby exercised and specifying the number of Shares in respect of which it is exercised. Each such notice must be accompanied by a remittance for the full amount of the aggregate subscription price for the Shares in respect of which the notice is given. Within 10 days after receipt of the notice and, where appropriate, receipt of a certificate from our auditors pursuant to the Share Option Scheme, our Company shall accordingly allot and issue the relevant number of Shares to the grantee (or his legal personal representative(s)) credited as fully paid with effect from (but excluding) the relevant exercise date and issue to the Grantee (or his legal personal representative(s)) share certificate(s) in respect of the Shares so allotted.

(ii) The exercise of any Option may be subject to a vesting schedule to be determined by the Board in its absolute discretion, which shall be specified in the offer letter.

(iii) The exercise of any Option shall be subject to the members of our Company in general meeting approving any necessary increase in the authorised share capital of our Company.

(iv) Subject as hereinafter provided:

(a) in the event that the grantee dies or becomes permanently disabled before exercising an Option (or exercising it in full), he (or his legal representative(s)) may exercise the Option up to the Grantee's entitlement (to the extent not already exercised) within a period of 12 months following his death or permanent disability or such longer period as the Board may determine;

(b) in the event that the Grantee ceases to be an Executive by reason of his retirement pursuant to such retirement scheme applicable to our Group at the relevant time and none of the following events for termination of employment or engagement under exists with respect to such Grantee:

- he has been guilty of serious misconduct;
- there exists grounds allowing his summary dismissal under his employment contract or under common law;
- he is unable or has no reasonable prospects of being able to pay his debts within the meaning of the Bankruptcy Ordinance (Chapter 6 of the laws of Hong Kong) as amended from time to time (the "Bankruptcy Ordinance") or any other applicable law;

- he has become otherwise insolvent or has made any arrangement or composition with his creditors generally; or

- he has been convicted of any criminal offence involving his integrity or honesty,

his Option (to the extent not already exercised) shall be exercisable up to the Grantee's entitlement immediately prior to his retirement until the expiry of the relevant option period;

(c) in the event that the Grantee ceases to be an Executive by reason of his transfer of employment to a controlling shareholder (as defined in the Listing Rules) of our Company or a subsidiary or an associate of a controlling shareholder of our Company, his Option (to the extent not already exercised) shall be exercisable until the expiry of the relevant option period unless the Board in its absolute discretion otherwise determines in which event the Option (or such remaining part thereof) shall be exercisable within such period as the Board has determined;

(d) in the event that the grantee ceases to be an Executive for any reason (including his employing company ceasing to be a member of our Group) other than his death, permanent disability, retirement pursuant to such retirement scheme applicable to our Group at the relevant time or the transfer of his employment to an affiliate company or the termination of his employment with the relevant member of our Group by resignation or termination on the ground of misconduct, the Option (to the extent not already exercised) shall lapse on the date of cessation of such employment and not be exercisable unless the Board otherwise determines in which event the Option (or such remaining part thereof) shall be exercisable within such period as the Board may in its absolute discretion determine following the date of such cessation;

(e) if:

(i) the Board in its absolute discretion at any time determines that a Grantee has ceased to be an Eligible Person; or

(ii) a Grantee has failed to or no longer satisfies or complies with such criteria or terms and conditions that may be attached to the grant of the Option or which were the basis on which the Option was granted,

the Option (to the extent not already exercised) shall lapse on the date on which the Grantee is notified thereof (in the case of (i)) or on the date on which the Grantee has failed to or no longer satisfies or complies with such criteria or terms and conditions as aforesaid (in the case of (ii)) and not be exercisable unless the Board otherwise determines in which event the Option (or such remaining part thereof) shall be exercisable up to the Grantee's entitlement immediately prior to the determination of the Board (in the case of (i)) or the failure of the Grantee to satisfy or comply with the criteria or terms and conditions attached to the grant of the Option or which were the basis on which the Option was granted (in the case of (ii)) within such period as the Board may in its absolute discretion determine following the date of such notification or the date of such failure, non-satisfaction or non-compliance. In the case of (i), a resolution of the Board resolving that the Grantee's Option has lapsed pursuant to the provision set out in this paragraph 13(e) shall be final and conclusive;

(f) if a Grantee (being a corporation):

(i) has a liquidator or receiver appointed anywhere in the world in respect of the whole or any part of the assets or undertaking of the Grantee; or

(ii) has suspended, ceased or threatened to suspend or cease business; or

(iii) is unable to pay its debts; or

(iv) otherwise becomes insolvent; or

(v) suffers a change in its constitution, management, directors or shareholding which in the opinion of the Board is material; or

(vi) commits a breach of any contract entered into between the Grantee or his associate and any member of our Group,

the Option (to the extent not already exercised) shall lapse on the date of appointment of the liquidator or receiver or on the date of suspension or cessation of business or threatened suspension or cessation of business or on the date when the Grantee is deemed to be unable to pay its debts as aforesaid or otherwise becomes insolvent or on the date of notification by our Company that the said change in constitution, management, directors or shareholding is material or on the date of notification by our Company of the said breach of contract (as the case may be) and not be exercisable unless the Board otherwise determines in which event the Option (or such remaining part thereof) shall be exercisable up to the Grantee's entitlement immediately prior to the occurrence of any of the event(s) mentioned in paragraphs (i) to (vi) above within such period as the Board may in its absolute discretion determine following the date of such occurrence. A resolution of the Board resolving that the Grantee's Option has lapsed pursuant to the provision set out in this paragraph 13(f) by reason of breach of contract or material change in the constitution, management, directors or shareholding as aforesaid shall be final and conclusive;

(g) if a Grantee (being an individual):

(i) is unable or has no reasonable prospects of being able to pay his debts within the meaning of the Bankruptcy Ordinance or any other applicable law or has otherwise become insolvent; or

(ii) has made any arrangement or composition with his creditors generally; or

(iii) has been convicted of any criminal offence involving his integrity or honesty; or

(iv) commits a breach of any contract entered into between the Grantee or his associate and any member of our Group, the Option (to the extent not already exercised) shall lapse on the date on which he is deemed unable or to have no reasonable prospects of being able to pay his debts as aforesaid or on the date on which a petition for bankruptcy has been presented in any jurisdiction or on the date on which he enters into the said arrangement or composition with his creditors or on the date of his conviction or on the date of the said breach of contract (as the case may be) and not be exercisable unless the Board otherwise determines in which event the Option (or such remaining part thereof) shall be exercisable up to the Grantee's entitlement immediately prior to the occurrence of any of the event(s) mentioned in paragraphs (i) to (iv) above within such period as the Board may in its absolute discretion determine following the date of such occurrence. A resolution of the Board resolving that the Grantee's Option has lapsed pursuant to the provision set out in this paragraph 13(g) for breach of contract as aforesaid shall be final and conclusive;

(h) if a general offer is made to all holders of Shares and such offer becomes or is declared unconditional (in the case of a takeover offer) or is approved by the requisite majorities at the relevant meetings of shareholders of our Company (in the case of a scheme of arrangement), the Grantee shall be entitled to exercise the Option (to the extent not already exercised) at any time (in the case of a takeover offer) within one month after the date on which the offer becomes or is declared unconditional or (in the case of a scheme of arrangement) prior to such time and date as shall be notified by our Company;

(i) if a compromise or arrangement between our Company and its members or creditors is proposed for the purpose of or in connection with a scheme for the reconstruction of our Company or its amalgamation with any other company, our Company shall give notice thereof to the Grantees who have Options unexercised at the same time as it despatches notices to all members or creditors of our Company summoning the meeting to consider such a compromise or arrangement and thereupon each Grantee (or his legal representatives or receiver) may until the expiry of the earlier of:

(i) the Option Period (in respect of any particular Option, the period commencing immediately after the business day (as defined in the Listing Rules) on which the Option is deemed to be granted and accepted in accordance with the Share Option Scheme and expiring on a date to be determined and notified by our Directors to each Grantee provided that such period shall not exceed the period of 10 years from the date of the grant of a particular Option but subject to the provisions for early termination thereof contained in the Share Option Scheme);

(ii) the period of two months from the date of such notice; or

(iii) the date on which such compromise or arrangement is sanctioned by the court,

exercise in whole or in part his Option.

(j) in the event a notice is given by our Company to its members to convene a general meeting for the purposes of considering, and if thought fit, approving a resolution to voluntarily wind-up our Company, our Company shall on the same date as or soon after it despatches such notice to each member of our Company give notice thereof to all Grantees and thereupon, each Grantee (or his legal personal representative(s)) shall be entitled to exercise all or any of his options at any time not later than two business days (as defined in the Listing Rules) prior to the proposed general meeting of our Company by giving notice in writing to our Company, accompanied by a remittance for the full amount of the aggregate subscription price for the Shares in respect of which the notice is given whereupon our Company shall as soon as possible and, in any event, no later than the business day (as defined in the Listing Rules) immediately prior to the date of the proposed general meeting referred to above, allot the relevant Shares to the Grantee credited as fully paid.

**14. Ranking of Shares**

The Shares to be allotted upon the exercise of an Option will be subject to all the provisions of the articles of association and the laws of the Cayman Islands from time to time and shall rank pari passu in all respects with the then existing fully paid Shares in issue on the allotment date or, if that date falls on a day when the register of members of our Company is closed, the first date of the re-opening of the register of members, and accordingly will entitle the holders to participate in all dividends or other distributions paid or made on or after the allotment date or, if that date falls on a day when the register of members of our Company is closed, the first day of the re-opening of the register of members, other than any dividend or other distribution previously declared or recommended or resolved to be paid or made if the record date therefore shall be before the allotment date.

A Share issued upon the exercise of an Option shall not carry rights until the registration of the Grantee (or any other person) as the holder thereof.

**15. Life of Share Option Scheme**

Subject to the terms of this Scheme, the Share Option Scheme shall be valid and effective for a period of 10 years from the date on which it becomes unconditional, after which no further options will be granted or offered but the provisions of the Share Option Scheme shall remain in full force and effect to the extent necessary to give effect to the exercise of any subsisting Options granted prior to the expiry of the 10-years period or otherwise as may be required in accordance with the provisions of the Share Option Scheme.

**16. Lapse of Share Option Scheme**

An Option shall lapse automatically and not be exercisable (to the extent not already exercised) on the earliest of:

(a) the expiry of the option period;

(b) the expiry of any of the period referred to paragraphs related to exercise of Option;

(c) subject to the period mentioned in paragraph headed “Exercise of Option” in this section, the date of the commencement of the winding-up of our Company;

(d) there is an unsatisfied judgment, order or award outstanding against the grantee or our Board has reason to believe that the grantee is unable to pay or to have no reasonable prospect of being able to pay his/its debts;

(e) there are circumstances which entitle any person to take any action, appoint any person, commence proceedings or obtain any order of the type mentioned in paragraph 13(f) or in paragraph 16(d) above; or

(f) a bankruptcy order has been made against any director or shareholder of the Grantee (being a corporation) in any jurisdiction.

No compensation shall be payable upon the lapse of any Option, provided that our Board shall be entitled in its discretion to pay such compensation to the grantee in such manner as it may consider appropriate in any particular case.

**17. Adjustment**

In the event of any alteration to the capital structure of our Company while any Option remains exercisable, whether by way of capitalisation of profits or reserves, rights issue, consolidation, reclassification, reconstruction, sub-division or reduction of the share capital of our Company, the Board may, if it considers the same to be appropriate, direct that adjustments be made to:

(a) the maximum number of Shares subject to the Share Option Scheme; and/or

(b) the aggregate number of Shares subject to the Option so far as unexercised; and/or

(c) the subscription price of each outstanding Option.

Where the Board determines that such adjustments are appropriate (other than an adjustment arising from a capitalisation issue), the auditors appointed by our Company shall certify in writing to the Board that any such adjustments are in their opinion fair and reasonable, provided that:

(a) any such adjustments shall be made on the basis that the aggregate Subscription Price payable by the Grantee on the full exercise of any Option shall remain as nearly as practicable the same as (but shall not be greater than) as it was before such event;

(b) no such adjustments shall be made the effect of which would be to enable a Share to be issued at less than its nominal value;

(c) any such adjustments shall be made in accordance with the provisions as stipulated under Chapter 17 of the Listing Rules and supplementary guidance on the interpretation of the Listing Rules issued by the Stock Exchange from time to time (including the supplemental guidance attached to the letter from the Stock Exchange dated 5 September 2005 to all issuers relating to Share Option Schemes); and

(d) the issue of securities as consideration in a transaction shall not be regarded as a circumstance requiring any such adjustments.

**18. Cancellation of Options not exercised**

The Board shall be entitled for the following causes to cancel any Option in whole or in part by giving notice in writing to the Grantee stating that such Option is thereby cancelled with effect from the date specified in such notice (the "Cancellation Date"):

(a) the Grantee commits or permits or attempts to commit or permit a breach of the restriction on transferability of Option or any terms or conditions attached to the grant of the Option;

(b) the Grantee makes a written request to the Board for the Option to be cancelled; or

(c) if the Grantee has, in the opinion of the Board, conducted himself in any manner whatsoever to the detriment of or prejudicial to the interests of our Company or its subsidiary.

The Option shall be deemed to have been cancelled with effect from the Cancellation Date in respect of any part of the Option which has not been exercised as of the Cancellation Date. No compensation shall be payable upon any such cancellation, provided that the Board shall be entitled in its discretion to pay such compensation to the Grantee in such manner as it may consider appropriate in any particular case.

**19. Termination**

Our Company may by resolution in general meeting at any time terminate the operation of the Share Option Scheme. Upon termination of the Share Option Scheme as aforesaid, no further Options shall be offered but the provisions of the Share Option Scheme shall remain in force and effect in all other respects. All Options granted prior to such termination and not then exercised shall continue to be valid and exercisable subject to and in accordance with the Share Option Scheme.

**20. Transferability**

The Option shall be personal to the Grantee and shall not be assignable and no Grantee shall in any way sell, transfer, charge, mortgage, encumber or create any interest (legal or beneficial) in favour of any third party over or in relation to any Option or attempt so to do (save that the Grantee may nominate a nominee in whose name the Shares issued pursuant to the Scheme may be registered), except with the prior written consent of the Board from time to time. Any breach of the foregoing shall entitle our Company to cancel any outstanding Option or part thereof granted to such Grantee.

**21. Amendment**

The Share Option Scheme may be altered in any respect by a resolution of the Board except that the following shall not be carried out except with the prior sanction of an ordinary resolution of the shareholders of our Company in general meeting, provided always that the amended terms of the Scheme shall comply with the applicable requirements of the Listing Rules: (i) any material alteration to its terms and conditions or any change to the terms of Options granted (except where the alterations take effect under the existing terms of the Scheme); (ii) any alteration to the provisions of the Scheme in relation to the matters set out in Rule 17.03 of the Listing Rules to the advantage of Grantee; and (iii) any alteration to the aforesaid termination provisions.

## G. OTHER INFORMATION

### 1. Deed of Indemnity

Our Controlling Shareholders have, under the Deed of Indemnity referred to in paragraph (q) of the sub-section headed "Summary of the material contracts" in this Appendix, given joint and several indemnities to our Company and its subsidiaries in connection with, among other things, (a) any taxation which might be payable by any member of our Group in respect of any income, profits or gains earned, accrued or received, or deemed to be earned or accrued or received on or before the Listing Date; and (b) all damages, losses and liabilities arising from or in connection with any property claim and/or any other liability claim to the extent that the events leading to such damages, losses and liabilities occurred prior to the Listing Date.

Our Controlling Shareholders will however, not be liable under the Deed of Indemnity for taxation claim or liability to the extent that:

- provision or allowance has been made for such taxation in the audited accounts of any member of our Group for the three years ended 31 December 2009;
- such taxation or liability would not have arisen but for, among other things, any act, omission or transaction entered into by the Controlling Shareholder or any member of our Group, otherwise than in the ordinary course of business before the Listing Date; and
- such claim arises or is incurred as a consequence of any retrospective changes in the law coming into effect after the Listing Date or such claim arises or is increased by an increase in rates in taxation after the Listing Date with retrospective effect.

Our Controlling Shareholders have also undertaken to indemnify our Group against any claims (civil, criminal, administrative or otherwise) made against any member of our Group at any time arising from any matter, event or circumstance that occurred prior to the Listing Date; and any damages, losses or liabilities which are or become payable or incurred by any members of our Group as a direct or indirect result of any title defects of the properties of our Group after the Listing. For more information, please see the section headed "Business — Property, Plant and Equipment" in this prospectus.

### 2. Litigation

As of the Latest Practicable Date, neither we nor any of our subsidiaries are/is engaged in any litigation, arbitration or claim of material importance, and no litigation, arbitration or claim of material importance is known to our Directors to be pending or threatened by or against us, that would have a material adverse effect on its results of operations or financial condition.

**3. Preliminary expenses**

Our estimated preliminary expenses are approximately US$3,800 (equivalent to approximately HK$29,500) and have been paid by us.

**4. Sole Sponsor**

The Sole Sponsor made an application on our behalf to the Listing Committee of the Stock Exchange for listing of, and permission to deal in, the Shares in issue as mentioned herein Shares to be issued pursuant to the Capitalisation Issue and any Shares falling to be issued pursuant to the exercise of the Over-allotment Option and, the Shares that may be issued upon the exercise of options that may be granted under the Share Option Scheme. All necessary arrangements have been made to enable such Shares to be admitted into CCASS.

**5. No material adverse change**

Our Directors confirm that there has been no material adverse change in our Company's financial or trading position or prospects since 31 December 2009 (being the date to which our latest audited combined financial statements were made up).

**6. Binding effect**

This prospectus shall have the effect, if an application is made in pursuance hereof, of rendering all persons concerned bound by all the provisions (other than the penal provisions) of sections 44A and 44B of the Companies Ordinance so far as applicable.

**7. Miscellaneous**

(1) Except as disclosed in the subsection headed "Other information" of this Appendix VI to this prospectus:

(a) within the two years immediately preceding the date of this prospectus, no share or loan capital of our Company or any of our subsidiaries has been issued or agreed to be issued fully or partly paid either for cash or for a consideration other than cash;

(b) no share or loan capital of our Company or any of our subsidiaries is under option or is agreed conditionally or unconditionally to be put under option;

(c) neither our Company nor any of our subsidiaries have issued or agreed to issue any founder shares, management shares or deferred shares;

(d) within the two years immediately preceding the date of this prospectus, no commissions, discounts, brokerage or other special terms have been granted in connection with the issue or sale of any shares or loan capital of any member of our Group;

(e) within the two years preceding the date of this prospectus, no commission has been paid or payable (except commissions to the Underwriters) for subscription, agreeing to subscribe, procuring subscription or agreeing to procure subscription of any shares in our Company;

(f) none of the equity and debt securities of our Company is listed or dealt with in any other stock exchange nor is any listing or permission to deal being or proposed to be sought; and

(g) we have no outstanding convertible debt securities.

(2) There has not been any interruption in the business of our Group which may have or have had a significant effect on the financial position of our Group in the twelve (12) months immediately preceding the date of this prospectus.

**8. Qualifications of experts**

The following are the qualifications of the experts who have given opinion or advice which are contained in this prospectus:

| Name | Qualification |
|---|---|
| The Hongkong and Shanghai Banking Corporation Limited | Deemed licensed under the SFO for Type 1 (dealing in securities), Type 4 (advising on securities) and Type 6 (advising on corporate financing) as defined under the SFO |
| Deloitte Touche Tohmatsu | Certified Public Accountants |
| Conyers Dill & Pearman | Cayman Islands attorneys-at-law |
| King & Wood | PRC legal advisers to our Company |
| Jones Lang LaSalle Sallmanns Limited | Property valuer |

**9. Consents of experts**

Each of the Sole Sponsor, Deloitte Touche Tohmatsu, Conyers Dill & Pearman, King & Wood and Jones Lang LaSalle Sallmanns Limited has given and has not withdrawn their respective consent to the issue of this prospectus with the inclusion of its report and/or letter and/or summary of valuations and/or legal opinion (as the case may be) and references to its name included in the form and context in which it respectively appears.

None of the experts named above has any shareholding interests in our Company or any of our subsidiaries or the right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in our Company or any of our subsidiaries.

**10. Bilingual prospectus**

The English language and Chinese language versions of this prospectus are being published separately in reliance upon the exemption provide by section 4 of the Companies Ordinance (Exemption of Companies and Prospectuses from Compliance with Provisions) Notice (Chapter 32L of the Laws of Hong Kong).

## DOCUMENTS DELIVERED TO THE REGISTRAR OF COMPANIES

The documents attached to the copy of this prospectus and delivered to the Registrar of Companies in Hong Kong for registration were copies of the **WHITE, YELLOW, GREEN** Application Forms, the written consents referred to in the paragraph headed "Consents of experts" in Appendix VI and copies of the material contracts referred to in the paragraph headed "Summary of material contracts" in Appendix VI.

## DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents will be available for inspection at the offices of Orrick, Herrington & Sutcliffe at 43rd Floor, Gloucester Tower, The Landmark, 15 Queen's Road Central, Hong Kong during normal business hours from 9:00 a.m. to 5:00 p.m. up to and including the date which is 14 days from the date of this prospectus:

(1) the Memorandum of Association and the Articles of Association;

(2) the Accountants' Report prepared by Deloitte Touche Tohmatsu, the text of which is set out in Appendix I to this prospectus;

(3) the audited financial statements of our PRC subsidiaries for each of the three years ended 31 December 2009;

(4) the letter relating to the unaudited pro forma financial information, the texts of which are set out in Appendix II to this prospectus;

(5) the letters relating to the profit forecast, the texts of which are set out in Appendix III to this prospectus;

(6) the letter, summary of values and valuation certificates relating to the property interests of our Group prepared by Jones Lang LaSalle Sallmanns Limited, the texts of which are set out in Appendix IV to this prospectus;

(7) the material contracts referred to in "Statutory and General Information — Further Information About Our Business — Summary of the material contracts" in Appendix VI to this prospectus;

(8) the service contracts and letters of appointment, as the case may be, with our Directors, referred to in "Statutory and General Information — Further Information About the Directors — Service contracts and letters of appointment of our Directors" in Appendix VI to this prospectus;

(9) the written consents referred to in "Statutory and General Information — Other Information — Consents of experts" of Appendix VI to this prospectus;

(10) the legal opinions prepared by King & Wood, our legal advisers as to the PRC laws in respect of certain aspects of our Group and the property interests of our Group;

(11) the letter prepared by Conyers Dill & Pearman summarising certain aspects of Companies Law referred to in Appendix V to this prospectus;

(12) the Companies Law; and

(13) the rules of the Share Option Scheme.

优源
YOUYUAN

YOUYUAN INTERNATIONAL HOLDINGS LIMITED
優源國際控股有限公司