

## **OVERVIEW**

We are a manufacturer and supplier of consumer chemicals and their ingredients, namely ethylene oxide and AEO surfactants which are the core components for household cleansing and cosmetic products. According to the SAI Report, we were the third largest manufacturer and the largest privately-owned manufacturer of ethylene oxide in China in terms of production volume for the three years ended 31 December 2009. We are also the second largest manufacturer and the largest privately-owned manufacturer of AEO surfactants in China in terms of production volume in 2009. Ethylene oxide is an ethylene derivative product and is mainly used for production of surfactants, ethylene glycol, ethanolamines and glycol ethers in China. Our AEO surfactants are mainly used in the manufacture of household cleansing agents such as liquid detergents, cosmetics and ointments products.

In addition to ethylene oxide and AEO surfactants, we also manufacture and supply other types of surfactants products. We also engage in the provision of ethylene oxide and surfactants processing services to our customers as well as the production and supply of other chemical products such as ethylene glycol and industrial gases, namely oxygen, nitrogen and argon.

According to the SAI Report, in terms of market share by production volume, our share in China's ethylene oxide market was approximately 11% in both 2007 and 2008 and increased to approximately 19% in 2009; while our share in China's AEO surfactants market increased from approximately 7% in both 2007 and 2008 to approximately 13% in 2009. Our aggregate designed annual production capacities of ethylene oxide and surfactants were approximately 120,000 MT and 218,000 MT respectively as of the Latest Practicable Date.

We are able to secure a steady and reliable supply of raw materials due to our vertically integrated production process and our established relationship with our suppliers since 2007. For the manufacture of surfactants, we manufacture all the ethylene oxide, the principal raw material for our surfactant production, in-house, and do not have to source ethylene oxide from external suppliers. During the Track Record Period, approximately 1,426 MT, 2,982 MT, 15,274 MT and 4,033 MT of ethylene oxide manufactured by us were utilised for processing into surfactants (excluding surfactant processing services), representing approximately 2.2%, 4.4%, 10.9% and 8.2% of our total production volume of ethylene oxide respectively. The said ethylene oxide manufactured for self-consumption, based on production costs, amounted to approximately RMB13.4 million, RMB28.7 million, RMB91.1 million and RMB33.3 million respectively during the Track Record Period. For the manufacture of ethylene oxide, we source ethylene, the principal raw material for production, from reputable companies in Japan, with whom we have established good business relationship since 2007. In addition, our ethylene storage tank provides a buffer for us to absorb short term price fluctuation of ethylene. Our imported ethylene is stored in our ethylene storage tank which has a storage capacity of approximately 22,000 cubic metres or effectively 12,075 MT of ethylene. Such ethylene storage tank was the largest in China in terms of storage capacity as of 30 April 2010 according to the SAI Report.

We believe that, given the strict requirements on establishment of new ethylene oxide manufacturing facilities and manufacture of ethylene oxide under the PRC laws and regulations, in particular, the requirements on new entrants to the ethylene oxide manufacturing industry, the entry barrier for the ethylene oxide manufacturing industry is high and that potential competitions from new entrants are limited.

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We have been generating most of our revenue from the sales of ethylene oxide and surfactants. During the Track Record Period, our revenue was approximately RMB876.8 million, RMB952.8 million, RMB1,285.5 million and RMB567.5 million respectively, and our net profit attributable to equity holders of the parent was approximately RMB147.4 million, RMB139.1 million, RMB242.1 million and RMB78.7 million respectively. Between 2007 and 2009, the net profit attributable to equity holders of the parent grew at a CAGR of approximately 28.2%. During the same period, we saw continued growth in both our ethylene oxide and surfactant businesses, in particular our surfactant business, where revenue contribution had increased both in absolute amount and as percentage of total revenue. Sale of ethylene oxide as a percentage of our total revenue gradually decreased from approximately 90.7% in 2007 to approximately 87.0% in 2008 and then to approximately 72.0% in 2009 as our Group began to develop our surfactant business. Sales of surfactants as a percentage of our total revenue gradually increased from approximately 3.5% in 2007 to approximately 4.9% in 2008 and then to approximately 16.8% in 2009. For the four months ended 30 April 2010, sales of ethylene oxide as a percentage of our total revenue increased to approximately 83.2% while sales of surfactants as a percentage of our total revenue decreased to approximately 11.1% as we increased our sales of ethylene oxide and allocated more self-manufactured ethylene oxide to provide surfactants processing services.

### OUR COMPETITIVE STRENGTHS

Our Directors attribute our success to the following competitive strengths:

#### **We have maintained a leading market position and have been benefiting from the rapid market growth**

According to the SAI Report, we were the third largest manufacturer and the largest privately-owned manufacturer of ethylene oxide in China in terms of production volume for the three years ended 31 December 2009. We are also the second largest manufacturer and the largest privately-owned manufacturer of AEO surfactants in China in terms of production volume in 2009. Our aggregate designed annual production capacities of ethylene oxide and surfactants were approximately 120,000 MT and 218,000 MT respectively as of the Latest Practicable Date. Our Directors anticipate that our existing aggregate designed annual production capacity of ethylene oxide will increase to approximately 180,000 MT by early 2011 following the completion of the third phase construction of production facilities of 60,000 MT at our Jiaying Production Plant. According to the SAI Report, since 2007, we have been increasing our lead in market share in the sales of both ethylene oxide and surfactants. Our Directors believe that our leading market position provides us with advantages with regard to product pricing and customer selection. Our large-scale operation also allows us to achieve significant economies of scale with regard to production and procurement. According to the SAI Report, the demand for ethylene oxide in China will experience growth at a CAGR of 17% from 2009 to 2014, reaching 1,564,017 MT in volume or a total value of US\$2,813.6 million by 2014 and the demand for AEO surfactants in China will experience growth at a CAGR of 5% from 2009 to 2014, reaching 529,500 MT in volume or a total value of US\$1,077.6 million by 2014. Our Directors believe that there will be an increasing demand for downstream products of surfactants such as household detergent and cosmetic products due to increasing disposable income, general improvement in living standards and economic conditions in China, which will in turn lead to increasing demand for surfactants, the principal raw materials of such downstream products. Our Directors believe that, given our large scale operation and production capacity, we are well positioned to capture such demand growth.

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### **We manage to increase our profitability through vertical integration and optimisation of our product mix**

Ethylene oxide is an ethylene derivative product which is mainly used for the production of surfactants in China. As we possess both ethylene oxide and surfactant production lines, and that we are capable of manufacturing both ethylene oxide and surfactants, our Directors believe that we have an effective vertically integrated production process, which enables us to respond to the changes in market condition in terms of product pricing and customers' demand in a timely manner by resiliently switching between selling ethylene oxide to our customers and utilising the ethylene oxide manufactured by us to manufacture surfactants. By manufacturing and delivering ethylene oxide, surfactants or mix of both, we can effectively optimise our overall profitability. We also offer a wide range of surfactant products to our customers. We produce over 100 types of surfactants according to the requirement of our customers and believe that we are able to switch to produce between different types of surfactant without much lag time.

### **The strategic location of our production base allows convenient transportation of our raw materials and products at low transportation costs**

Our Jiaxing Production Plant is strategically located in the Zhapu Development Zone of Jiaxing, Zhejiang Province, and is in close proximity to the Port of Zhapu which is a national first class open port for international trade. The Port of Zhapu is connected to the East China Sea, which links Japan and Korea; and is connected to Jing-Hang Canal, which links Beijing and Hangzhou. The strategic location of our production base allows convenient transportation of our raw materials and products by vessel or tankers, which may lower our transportation costs.

Taking advantage of such strategic location, we have installed an ethylene storage tank with a total storage capacity of approximately 22,000 cubic metres on a parcel of land we own adjacent to the Port of Zhapu. Ethylene, our principal raw material for production of ethylene oxide, is transported by sea to the Port of Zhapu and stored in our ethylene storage tank. Ethylene is then transported to our Jiaxing Production Plant through our own pipelines to ensure safe transportation of ethylene.

### **We are able to secure stable and reliable supply of raw materials to ensure stable production by our Group**

A stable and reliable supply of raw materials is, in the opinion of our Directors, imperative to our production. For the manufacture of surfactants, we manufacture all the ethylene oxide, the principal raw material for our production, in house, and do not have to source ethylene oxide from external suppliers. For the manufacture of ethylene oxide, we source ethylene, the principal raw material for production, from reputable companies from Japan, with whom we have established good business relationship since 2007. We enter into contracts with most of our suppliers on a yearly basis to fix the quantity of ethylene to be supplied to us in that year. During the Track Record Period, we did not experience any shortage of supply of raw materials.

Our ethylene storage tank located in the Port of Zhapu is the largest in China in terms of storage capacity according to the SAI Report. With a total storage capacity of approximately 22,000 cubic metres as of 30 April 2010, the tank can effectively store 12,075 MT of ethylene which we import. Ethylene is transported from our ethylene storage tank to our Jiaxing Production Plant which is in close proximity to the Port of Zhapu through our own pipelines. Our large storage tank can ensure a safe storage and stable supply of ethylene which is essential to our production of ethylene oxide. In addition, our ethylene

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storage tank enables us to absorb short term price fluctuation of ethylene with an aim to have better cost control. The close proximity of our storage tank to our Jiaying Production Plant has a definite geographical advantage in ensuring safe transportation of ethylene to our production plant. Please refer to the subsection headed “Production capacities, production plant and storage facility – Ethylene storage facility” in this section for further details on our ethylene storage facility.

### **High entry barrier to the ethylene oxide manufacturing industry thereby limiting competition from new entrants**

According to the Industrial Restructuring Catalogue and the Land Catalogue, ethylene oxide construction projects with an annual capacity of less than 200,000 MT are expressly banned by the PRC government. According to the Production Licence Notice, the National Production Licence for Industrial Products, which is a requisite licence for the production of ethylene oxide in the PRC, shall not be issued to ethylene oxide production enterprises with an annual production capacity of less than 200,000 MT. Please refer to the section headed “Laws and regulations in relation to establishment of ethylene oxide manufacturing facilities” as set out in Appendix V to this prospectus for further details on the requirements of the aforementioned regulations.

In light of the above, new entrants to the industry is barred unless their ethylene oxide construction project reaches an annual capacity of 200,000 MT or more and the National Production Licence for Industrial Products is obtained. Our Directors believe that the relatively large initial capital investment provides a high entry barrier for the industry in particular for non-state owned entrants. According to the SAI Report, it is anticipated that save for Sanjiang Honam, which is the sino-foreign joint venture company jointly established by Honam Petrochemical Corp. and us and which will enter into the market by the end of 2011, no new commercial producers will enter into the market until 2013.

Given the aforesaid high entry barrier and our leading position in the industry, our Directors consider that we are well-positioned to capture the growth of this industry with limited competition from new entrants.

### **We maintain a strong relationship with quality customers**

We seek to establish a quality customer base. In particular, we target customers with strong financial conditions and corporate reputation, positive corporate image and favourable competitive advantages in their respective markets as we believe that quality customers in general have good credit record and usually place sizeable orders. We believe that by establishing business relationships with quality customers, we are able to mitigate credit risk and obtain steady order flow, as well as enhance the goodwill of our Company, which could in turn create further opportunities with other prestigious customers. To date, we have successfully secured business from a number of customers which are renowned companies in their respective industries such as the industrial and household sectors. Our top ten ethylene oxide customers included 嘉興金燕化工有限公司 (Jiaying Jinyan Chemical Co., Ltd.\*) and 江蘇銀燕化工股份有限公司 (Jiangsu Yinyan Speciality Chemicals Co., Ltd.\*) during the Track Record Period. 嘉興金燕化工有限公司 (Jiaying Jinyan Chemical Co., Ltd.\*) was one of our overall top ten customers for the two years ended 31 December 2009 and the four months ended 30 April 2010. 江蘇銀燕化工股份有限公司 (Jiangsu Yinyan Speciality Chemicals Co., Ltd.\*) was one of our overall top ten customers for the two years ended 31 December 2008. Our top ten surfactants customers included 納愛斯集團有限公司 (Nice Group Co., Ltd\*), 麗水市雕牌化工有限公司 (Lishui City Diao Brand Chemical Co., Ltd.\*) and 浙江傳化股份有限公司 (Zhejiang Transfar Co., Ltd.\*) during the Track Record Period. Please refer to the subsection headed “Sales and marketing – Customers” in this section for further details on our customer base.

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We believe that with our dedication to provide products of the highest quality, together with our reliability and safety record, we have been successful in winning new customers, as well as maintaining and building entrenched relationships with existing customers. In particular, given the size of our operations and our on-going commitment to excel in our productions and services, we believe we have managed to build a high level of customer satisfaction and loyalty in our existing customers. As evident from the success we have enjoyed to date in building a well diversified customer base, we believe we are in a good position to attract further business interests, which should allow us to further expand our customer base.

### **We have an experienced and dedicated management team**

We have a strong management team with substantial experience in the production, sales and marketing of our products. Our senior management team is headed by our founder, Mr. Guan who has over 25 years of experience and knowledge in the petrochemical industry. In addition, most of the senior members of our management team have over 15 years of experience and have served at various companies in the petrochemical and related industries, their experience and knowledge of the industry contribute to the effectiveness and success of our operation. Under Mr. Guan's leadership, we have successfully established ourselves as the largest privately-owned manufacturer of ethylene oxide and AEO surfactants in China. Our Directors believe that the experience and dedication of our management team have contributed substantially to our business growth during the Track Record Period. Our Directors also believe that such experience and dedication will underpin our business revenue for expansion in the future.

### **OUR STRATEGIES**

We aim to maintain and further strengthen our position as the largest privately-owned manufacturer and supplier of ethylene oxide and AEO surfactants in China and to expand our business with an aim to maximise shareholders' value by pursuing the following strategies:

#### **Strengthen our leading market position in China through expansion of our production capacity**

We intend to strengthen our leading market position in China through expanding our ethylene oxide production capacity in phases. As part of our expansion plan, in December 2009, we commenced the third phase construction of ethylene oxide production facilities at our Jiaying Production Plant. We anticipate that upon completion of the third phase construction, our designed annual production capacity of ethylene oxide will increase from approximately 120,000 MT in 2009 to an aggregate designed production capacity of approximately 180,000 MT by early 2011, representing a CAGR of 22.5%. It is projected in the SAI Report that the total production volume of ethylene oxide in the PRC will increase at a CAGR of 10.4% from approximately 725,515 MT in 2009 to 884,000 MT in 2011. Further, we will commence our fourth phase construction of ethylene oxide production facilities with a designed annual production capacity of 100,000 MT following the commencement of the third phase production of ethylene oxide. We anticipate that upon completion of the fourth phase construction, our designed annual production capacity of ethylene oxide will increase from 180,000 MT in 2011 to 280,000 MT by early 2013, representing a CAGR of 24.7%. According to the SAI Report, the total production volume of ethylene oxide in the PRC will increase at a CAGR of 20.5% from approximately 884,000 MT in 2011 to 1,284,000 MT in 2013.

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We anticipate that Sanjiang Honam, the sino-foreign joint venture company jointly established and controlled by Honam Petrochemical Corp. and us, will commence the first phase construction of ethylene oxide production facilities with a designed annual production capacity of 100,000 MT at the end of 2010. We expect completion of the construction will take place by the end of 2011. We anticipate that the second phase construction of ethylene oxide production facilities with a designed annual production capacity of 100,000 MT will commence following the commencement of the first phase production of ethylene oxide.

In April 2009, the second phase construction of surfactant production facilities with a designed annual production capacity of 100,000 MT commenced at our Jiaying Production Plant. Such production facilities commenced production in August 2010, thereby our designed annual production capacity of surfactants increased from approximately 118,000 MT in aggregate to approximately 218,000 MT.

According to the SAI Report, the demand for ethylene oxide in China will experience growth at a CAGR of 17% from 2009 to 2014, reaching 1,564,017 MT in volume or a total value of US\$2,813.6 million by 2014 and the demand for AEO surfactants in China will experience growth at a CAGR of 5% from 2009 to 2014, reaching 529,500 MT in volume or a total value of US\$1,077.6 million by 2014. Our Directors believe that there will be an increasing demand for downstream products of surfactants such as household detergent and cosmetic products due to increasing disposable income, general improvement in living standards and economic conditions in China, which will in turn lead to a direct increase in demand for surfactants and an indirect increase in demand for ethylene oxide, the principal raw material of such downstream products. We believe that, with the abovementioned increase in our production capacity, we are well positioned to capture such demand growth.

### **Expand our product coverage and functionality, improve our product quality and further maximise our profitability**

In view of the rising market demand for variety and functionality of downstream products of surfactants and with an objective to maximise our long-term profitability, we intend to expand our product coverage by developing new types of surfactants and improve the quality of our existing products and production technologies through our research and development team and potential collaboration and/or cooperation with universities in the PRC. In particular, we plan to expand our range of surfactant products to include surfactant products which require more sophisticated and customised production process with higher profit margins so as to maximise our profitability. We will continue to assess and effectively respond to the changes in market condition in terms of product pricing and customers' demand by resiliently switching between selling ethylene oxide to our customers and utilising the ethylene oxide manufactured by us to manufacture surfactants in order to maximise our profitability.

### **Selectively seek acquisition opportunities**

We may consider selective acquisitions of existing surfactant manufacturing or related businesses to further strengthen our leading market position in China. We may also consider selective acquisitions of businesses of the downstream market. We are currently at the initial stage of negotiation with several companies to explore acquisition opportunities. We have not entered into any definitive agreement, letter of intent or framework agreement with these companies.

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### Improve production efficiency and reduce production costs

We will continue to improve our production efficiency by enhancing our production process technologies. To date, we have engaged international technology providers, namely Scientific Design Company, Inc. and Sulzer Ltd., to enhance our production know-how and upgrade our machinery and equipment. Together with the anticipated economies of scale via increase in our production capacity, we will continue our efforts to lower production costs by improving our efficiency in the utilisation of raw materials, energy and utilities during our production process.

### Increase raw material storage capacity by constructing new ethylene storage tank to accommodate increasing production capacity

In order to accommodate our increasing ethylene oxide production capacity, we commenced the construction of an additional ethylene storage tank with a total storage capacity of approximately 22,000 cubic metres at a parcel of land owned by us at Port of Zhapu in the second quarter of 2010. We anticipate the construction will be completed by the second quarter of 2011.

## PRODUCTS AND SERVICES

We are a manufacturer and supplier of consumer chemicals and their ingredients, namely ethylene oxide and AEO surfactants. In addition to ethylene oxide and AEO surfactants, we also manufacture and supply other types of surfactants products. We also engage in the provision of ethylene oxide and surfactant processing services to our customers as well as the production and supply of ethylene glycol and industrial gases, namely oxygen, nitrogen and argon.

The following is a breakdown of our revenue for the years ended 31 December 2007, 2008 and 2009 and the four months ended 30 April 2009 and 2010:

	Year ended 31 December						Four months ended 30 April			
	2007		2008		2009		2009		2010	
	RMB	%	RMB	%	RMB	%	RMB	%	RMB	%
	million		million		million		million		million	
	(unaudited)									
Sales of ethylene oxide	795.2	90.7	829.3	87.0	925.1	72.0	231.7	62.9	472.0	83.2
Sales of surfactants	30.9	3.5	46.8	4.9	216.6	16.8	67.1	18.2	63.1	11.1
Processing services	3.4	0.4	9.7	1.0	66.4	5.2	54.2	14.7	5.2	0.9
Others <sup>(Note)</sup>	47.3	5.4	67.0	7.1	77.4	6.0	15.4	4.2	27.2	4.8
<b>Total</b>	<b>876.8</b>	<b>100.0</b>	<b>952.8</b>	<b>100.0</b>	<b>1,285.5</b>	<b>100.0</b>	<b>368.4</b>	<b>100.0</b>	<b>567.5</b>	<b>100.0</b>

*Note:* Others mainly comprised of sales from ethylene glycol, ethylene, nitrogen, oxygen and argon.

## **Our products**

Our main products are ethylene oxide and surfactants. Other products include ethylene glycol and industrial gases, namely oxygen, nitrogen and argon.

The following is a brief description of our main products:

### **A. *Ethylene oxide***

Ethylene oxide is an ethylene derivative product and is mainly used for production of surfactants, ethylene glycol, ethanolamines and glycol ethers in China. Ethylene oxide is produced by the oxidation of ethylene with pure oxygen. Ethylene oxide is a highly reactive, colourless, transparent, low-boiling point liquid or gas at room temperature. It is inflammable and explosive and not suitable for long distance transportation.

We commenced our production of ethylene oxide in January 2006 at our Jiaying Production Plant. During the Track Record Period, revenue derived from the sales of ethylene oxide amounted to approximately RMB795.2 million, RMB829.3 million, RMB925.1 million and RMB472.0 million respectively, representing approximately 90.7%, 87.0%, 72.0% and 83.2% of our total revenue of the respective periods. During the Track Record Period, our production volume of ethylene oxide, including the volume of ethylene oxide processed by us, was approximately 65,906 MT, 67,780 MT, 140,515 MT and 49,006 MT respectively. As of the Latest Practicable Date, our aggregate designed annual production capacity of ethylene oxide was approximately 120,000 MT.

#### *Description of ethylene oxide*

Product category : ethylene derivative products

Raw materials : ethylene, oxygen

Formula :  $C_2H_4O$

Synonyms : oxirane, epoxyethane

CAS number : 75-21-8

Characteristics : highly reactive, colourless, transparent, low-boiling point liquid or gas at room temperature with an ether-like odour

#### Scope of applications

Ethylene oxide is an ethylene derivative product and is used to produce surfactants, ethylene glycol, ethanolamines and glycol ethers in China. The downstream sectors of such ethylene derivative products cover various household and industrial products including antifreeze agent, synthetic detergent, emulsifier, non-ionic surfactants, plasticiser, lubricant, adhesive, rubber and synthetic resin.



**B. Surfactants**

Surfactants are major downstream products of ethylene oxide and are complex substances containing phospholipids and a number of apoproteins. Surfactants are wetting agents that lower the surface tension of a liquid, allowing easier spreading, and lower the interfacial tension between two liquids. Surfactants are widely applied in different industries as scouring agent, moisturising agent, emulsifier and solubiliser. Surfactants are also used for production of household cleansing agent, cosmetics and ointments products.

We are able to manufacture over 100 different types of surfactants with various application purposes. Fatty alcohol polyoxyethylene ether (AEO) surfactants, a type of non-ionic surfactants, are our main surfactant product. Our sales volume of AEO surfactants, including the volume of AEO surfactants processed by us, accounted for approximately 75.5%, 78.2%, 76.0% and 78.4% of our total surfactant production and processing volume for the three years ended 31 December 2009 and the four months ended 30 April 2010, respectively. Our AEO surfactants are mainly used in the manufacture of household cleansing agents such as liquid detergents, cosmetics and ointments products.

Hangzhou Haoming commenced the manufacture of surfactants in May 1998. We acquired, among other things, the ethylene oxide trading and surfactant manufacture and sale businesses of Hangzhou Haoming in April 2010. As Hangzhou Haoming is under the common control and management of Mr. Guan and Ms. Han, the results of the business acquired from Hangzhou Haoming had been reflected in our Group's results prior to 31 March 2010 by using merger accounting. Our Jiaxing Production Plant commenced manufacture of surfactants in February 2008. During the Track Record Period, revenue derived from the sales of surfactants amounted to approximately RMB30.9 million, RMB46.8 million, RMB216.6 million and RMB63.1 million respectively, representing approximately 3.5%, 4.9%, 16.8% and 11.1% of our total revenue for the respective periods. During the Track Record Period, our production and processing volume of surfactants amounted to approximately 10,922 MT, 19,815 MT, 52,687 MT and 18,681 MT respectively. As of the Latest Practicable Date, our aggregate designed annual production capacity of surfactants was approximately 218,000 MT.

*AEO surfactants*

In general, AEO surfactants take the form of either colourless liquid or milky paste and can be used as an emulsifier for mineral oil, aliphatic solvents and other substances, or a solubiliser for essential oils and moisturising agent etc. Further, AEO surfactants are important ingredients for producing downstream products such as AES, liquid detergents, cosmetics and ointments products.

Currently, we focus on the production of AEO-2, AEO-3, AEO-5, AEO-7 and AEO-9 surfactants.

*Description of AEO surfactants*

Raw materials : fatty alcohol and ethylene oxide

Formula :  $C_{12-14}H_{25-29}O(CH_2CH_2O)_nH$

CAS number : 9002-92-0

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The following table sets forth the characteristics and scope of applications of our major AEO surfactants:

<b>AEO surfactants</b>	<b>Characteristics</b>	<b>Scope of applications</b>
AEO-2	colourless liquid, highly soluble in oil and polar solvents, possessing good emulsifying properties	emulsifying mineral oil and aliphatic solvents and producing synthetic oils
AEO-3	colourless liquid, highly soluble in oil and polar solvents, possessing good emulsifying properties	emulsifying mineral oil and aliphatic solvents and producing synthetic oils, being primary ingredients for producing AES
AEO-5	colourless liquid, highly soluble in oil and polar solvents, possessing good emulsifying properties	emulsifying mineral oil and aliphatic solvents and producing synthetic oils
AEO-7	milky paste, highly soluble in water and possessing of excellent emulsifying, purifying and moisturising properties	acting as wool detergents and degreasing agents in the wool industry, scouring agents for fabrics and detergents; being an important component of liquid detergents and emulsifiers in the production of cosmetics and ointments
AEO-9	milky paste, highly soluble in water and possessing excellent emulsifying, purifying and moisturising properties	acting as wool detergents and degreasing agents in the wool industry, scouring agents for fabrics and detergents; being an important component of liquid detergents and emulsifiers in the production of cosmetics and ointments

### *Other surfactant products*

Our other surfactant products include nonylphenol polyoxyethylene ether (TX) surfactants, polyethylene glycol (PEG), emulsifier OP, softener SG series auxiliary agent and diglycerol.

**Our other products**

Our other products mainly include ethylene glycol and industrial gases, namely oxygen, nitrogen and argon.

Ethylene glycol is produced as one of the side-products during the production process of ethylene oxide. It is subsequently extracted and sold to our customers.

Our air separation plant separates oxygen, argon and nitrogen from air. Some of the nitrogen extracted is used as stabilising gas in the production of ethylene oxide and surfactants, whilst the unused nitrogen is sold to our customers. Oxygen and argon extracted are also sold to our customers in liquid state.

**Our processing services**

We provide ethylene oxide and surfactants processing services to our customers.

Ethylene is provided by our customer and delivered to our Sanjiang Production Plants for processing into ethylene oxide.

Raw materials such as fatty alcohol are provided by our customers and delivered to our Sanjiang Production Plants for processing into surfactants after undergoing the reaction with the ethylene oxide which we manufactured.

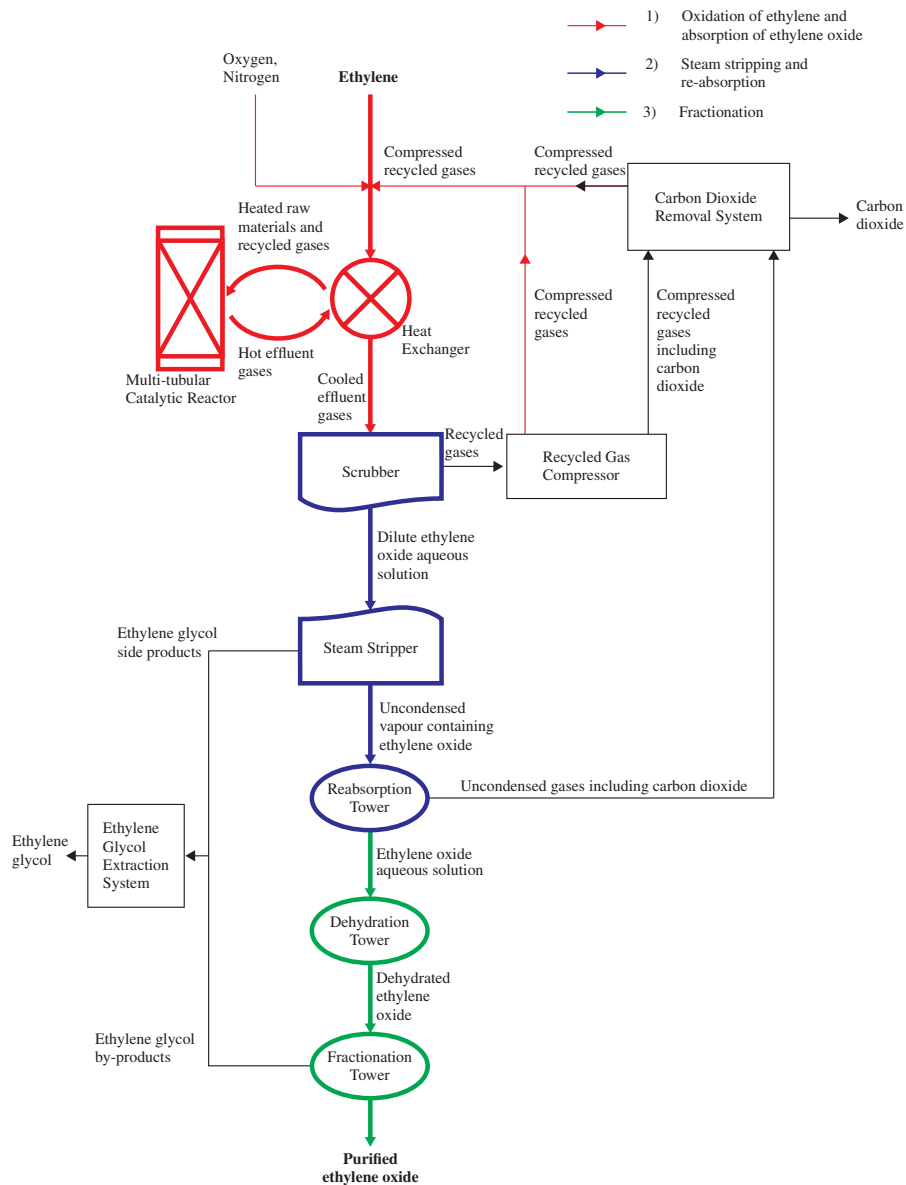
**OUR PRODUCTION**

Our sales, procurement and production departments work closely together to manage our production planning. We prepare production plans (in particular, at the beginning of each year for production of ethylene oxide), according to market demand and historical sales and production records, adjusted to take into account orders on hand at the time, production capacity and current inventory levels, as well as maintenance and repair needs from production facilities.

**Our production process**

**A. Ethylene oxide**

The production process of ethylene oxide is illustrated as follows:



Ethylene oxide is produced by the oxidation of ethylene when ethylene and oxygen react with a catalyst while in their respective vapour phases. The production process of ethylene oxide is primarily divided into three stages which are described below:

*(1) Oxidation of ethylene and absorption of ethylene oxide*

Pre-heated ethylene, oxygen and recycled gases are mixed and fed into a multi-tubular catalytic reactor. Nitrogen is added to maintain the balance of and stabilise the gas mixture. The reactor is then heated by high pressure steam to control the reaction temperature. Ethylene and oxygen will then undergo oxidation reaction in the reactor. A small amount of dichloroethane inhibitor is added to optimise the oxidation reaction and restrain side reactions. As a result of the oxidation reaction, low purity ethylene oxide and other side products, including carbon dioxide, water and a small amount of hydrocarbons are produced.

The resultant effluent gases from the reactor which contain, among others, ethylene oxide, are cooled and compressed. The cooling is accomplished by cross exchanging the reactor effluent with the recycled gases. The cooled reactor effluent is then passed to a scrubber where ethylene oxide is absorbed as a dilute aqueous solution. Recycled gases are compressed and returned to the reactor with a portion drawn off and diverted through a carbon dioxide removal system.

*(2) Steam stripping and re-absorption*

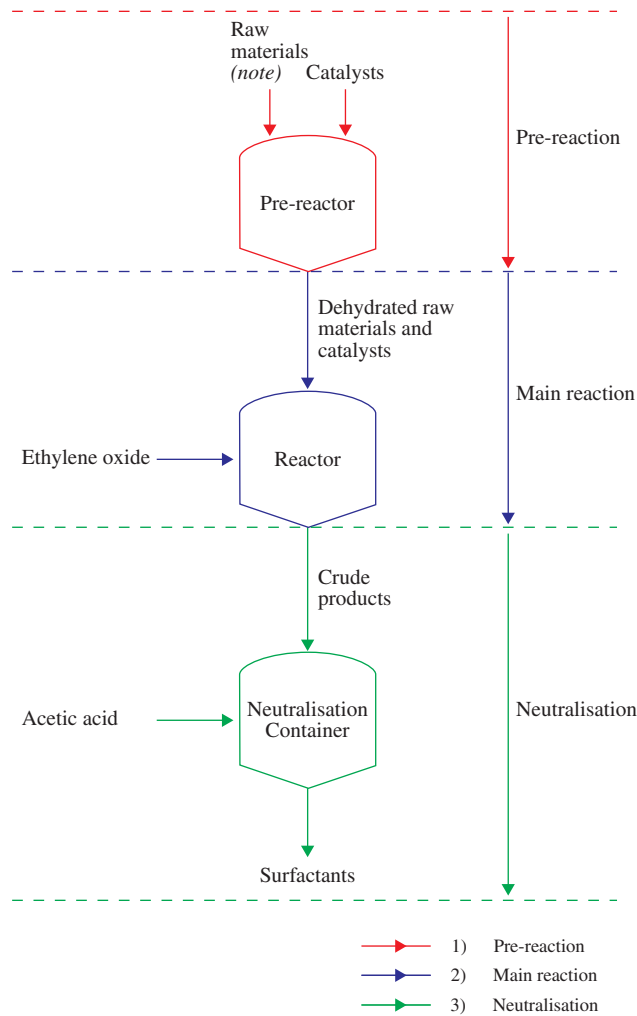
Ethylene oxide in aqueous form is decompressed and then steam stripped. The overhead vapour from the stripper is then cooled to condense out most of the water. The uncondensed vapour from the stripper is reabsorbed in recycled water at the re-absorption tower filled with polypropylene pall rings. Through this process, ethylene oxide of higher purity can be extracted. At the same time, impurities including carbon dioxide, oxygen, nitrogen and argon are also extracted. Further, ethylene glycol is produced as one of the side products.

*(3) Fractionation*

Ethylene oxide produced in the re-absorption tower as a result of the above step (2) is pre-heated and transmitted to the dehydration and fractionation tower, in which ethylene oxide is purified by fractionation until its purity reaches 99.99%. Ethylene oxide is then cooled and stored in spherical containers and transported through product pumps.

**B. Surfactants**

The production process of surfactants is illustrated below:



*Note:* Raw materials for production of surfactants vary depending on the type of surfactant to be manufactured.

The production process of surfactants is primarily divided into three stages which are described as follows:

*(1) Pre-reaction*

Raw materials, such as fatty alcohol, nonylphenol and catalysts, are added into the pre-reactor for vacuum dehydration.

*(2) Main reaction*

Dehydrated raw materials and catalysts are added into a nitrogen-filled reactor. Subsequently, ethylene oxide is added into the reactor to initiate chemical reaction.

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### (3) *Neutralisation*

The crude product from the above step (2) is added into a neutralisation container for mixing and stirring. Subsequently, nitrogen is added to the container and vacuum dehydration is initiated for the purpose of filtering any residual and unreacted ethylene oxide. Finally, acetic acid is added to begin the neutralisation process. Neutralised products are cooled and transported for storage by the discharging pump.

### C. *Our processing services*

Our ethylene oxide processing services in terms of production process are identical to that of our ethylene oxide production process.

Our surfactants processing services in terms of production process are identical to that of our surfactant production process.

## PRODUCTION CAPACITIES, PRODUCTION PLANT AND STORAGE FACILITY

### Production capacities

The following table sets forth our (i) pro-rated designed production capacity; (ii) production volume; and (iii) utilisation rate of ethylene oxide production capacity at our Sanjiang Production Plants for the three years ended 31 December 2009 and the four months ended 30 April 2010:

	<b>Pro-rated designed production capacity (MT)</b>	<b>Production volume (MT)</b>	<b>Utilisation rate (Approximate %)</b>
For the year ended 31 December 2007	60,000 <sup>(Note 1)</sup>	65,906 <sup>(Note 1)</sup>	110 <sup>(Note 4)</sup>
For the year ended 31 December 2008	65,000 <sup>(Note 2)</sup>	67,780 <sup>(Note 2)</sup>	104 <sup>(Note 4)</sup>
For the year ended 31 December 2009	120,000 <sup>(Note 3)</sup>	140,515 <sup>(Note 3)</sup>	117 <sup>(Note 4)</sup>
For the four months ended 30 April 2010	40,000 <sup>(Note 5)</sup>	49,006 <sup>(Note 5)</sup>	123 <sup>(Note 4)</sup>

As of the Latest Practicable Date, our designed annual production capacity of ethylene oxide at our Sanjiang Production Plants was approximately 120,000 MT<sup>(Note 3)</sup>.

#### *Notes:*

- (1) Representing the designed annual production capacity and production volume of our first production line in our Jiaxing Production Plant which commenced production in January 2006.
- (2) Representing and calculated based on the designed annual production capacity and production volume of our first production line in our Jiaxing Production Plant and the pro-rated production capacity of our second production line in our Jiaxing Production Plant which commenced production in December 2008. Such pro-rated production capacity of our second production line is calculated based on a designed annual production capacity of 60,000 MT and thus, an average designed monthly production capacity of 5,000 MT.
- (3) Representing the designed annual production capacity and production volume of our two production lines in our Jiaxing Production Plant.

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- (4) Representing the percentage of actual production volume as against the designed annual production capacity of our ethylene oxide production facilities. The high utilisation rate of our ethylene oxide production lines is due to (i) the various technology improvements made to our production facilities; and (ii) the extended operating hours of our production facilities beyond the operating hours assumed in the calculation of designed production capacity. According to the SAI Report, these measures are common practice amongst ethylene oxide producers in the PRC. As advised by our PRC Legal Advisers, the fact that our actual production volume of ethylene oxide exceeds our designed production capacity does not contravene the relevant PRC laws and regulations.
- (5) Representing and calculated based on the pro-rated production capacity and production volume of our two production lines in our Jiaxing Production Plant. Such pro-rated production capacity is calculated based on a designed annual production capacity of 120,000 MT and thus, an average designed monthly production capacity of 10,000 MT.

The following table sets forth our (i) pro-rated designed production capacity; (ii) production volume; and (iii) utilisation rate of surfactant production capacity at our Sanjiang Production Plants for the three years ended 31 December 2009 and the four months ended 30 April 2010:

	<b>Pro-rated designed production capacity (MT)</b>	<b>Production volume (MT)</b>	<b>Utilisation rate (Approximate %)</b>
For the year ended 31 December 2007	18,000 <sup>(Note 6)</sup>	10,922 <sup>(Note 6)</sup>	61
For the year ended 31 December 2008	109,667 <sup>(Note 7)</sup>	19,815 <sup>(Note 7)</sup>	18
For the year ended 31 December 2009	118,000 <sup>(Note 8)</sup>	52,687 <sup>(Note 8)</sup>	45
For the four months ended 30 April 2010	39,333 <sup>(Note 9)</sup>	18,681 <sup>(Note 9)</sup>	47

As of the Latest Practicable Date, our designed annual production capacity of surfactants at our Sanjiang Production Plants was approximately 218,000 MT<sup>(Note 10)</sup>.

*Notes:*

- (6) Representing the designed annual production capacity and production volume of our production lines in our Xiaoshan Production Plant which commenced production in May 1998.
- (7) Representing and calculated based on the designed annual production capacity and production volume of our production lines in our Xiaoshan Production Plant and the pro-rated production capacity of our first production line in our Jiaxing Production Plant which commenced production in February 2008. Such pro-rated production capacity of our first production line in our Jiaxing Production Plant is calculated based on a designed annual production capacity of 100,000 MT and thus, an average designed monthly production capacity of approximately 8,333 MT.
- (8) Representing the designed annual production capacity and production volume of our production lines in our Xiaoshan Production Plant and our first production line in our Jiaxing Production Plant.
- (9) Representing and calculated based on the pro-rated production capacity and production volume of our production lines in our Xiaoshan Production Plant and our first production line in our Jiaxing Production Plant. Such pro-rated production capacity is calculated based on a designed annual production capacity of 118,000 MT and thus, an average designed monthly production capacity of approximately 9,833 MT.
- (10) Representing the designed annual production capacity of our production lines in our Xiaoshan Production Plant and our first and second production lines in our Jiaxing Production Plant.



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Our production facilities of ethylene oxide and surfactants operate independently and our products are sold separately. It is one of our competitive strengths to possess both ethylene oxide and surfactant production lines. This enables us to respond to the changes in market condition in terms of product pricing and customers' demand in a timely manner by resiliently switching between selling ethylene oxide to the customers and utilising the ethylene oxide manufactured by us to manufacture surfactants. It has been our long term strategy to expand our production capacities of both ethylene oxide and surfactants, as well as to diversify into other related products. Although the demand for ethylene oxide had been rising and the utilisation rate of our ethylene oxide production facilities had been over 100% during the Track Record Period, our Directors were of the view that it would not be a healthy and prudent strategy for us to rely on a single product in the long run. Our Directors are optimistic of the future demand for surfactants in the PRC and had decided to expand our surfactant production capacities so to have a better competitive advantage in the future when the surfactant market is expected to continue to grow. Therefore, despite the relatively low utilisation rate of the surfactant production facilities when compared with that of ethylene oxide, our Directors are of the view that the development of our surfactant business, whether by way of expanding our surfactant production capacities or through acquisition, is imperative for our sustainable growth in the long run.

The utilisation rate of the surfactant production facilities was low in 2008 because our production line with a designed annual production capacity of 100,000 MT in the Jiaying Production Plant commenced production in February 2008, we spent considerable time and efforts for the business development in light of such significant increase in annual production capacity of surfactants from 18,000 MT to 118,000 MT. This was further affected by the economic downturn resulting from the financial crisis in 2008. With our sales and marketing effort, in 2009, we had achieved a more developed surfactant customer base and thus the utilisation rate of surfactant production facilities increased to approximately 45%.

Also, the utilisation rate of surfactant production facilities during the Track Record Period was partially restricted by the in-house supply of ethylene oxide. The ethylene oxide used for the production of surfactant is entirely supplied in-house. Given the high market demand for ethylene oxide and its relatively higher profit margin during the Track Record Period, our Directors were of the view that it was commercially justifiable for us to allocate more ethylene oxide for sale than for further processing into surfactants. However, as the production capacity of ethylene oxide increased to 120,000 MT in December 2008, a larger portion of ethylene oxide manufactured was utilised to manufacture surfactants. Also, taking into account the third and fourth phase construction of ethylene oxide production lines and the anticipated rising demand for surfactants, our Directors expect that the utilisation rate will improve as more ethylene oxide produced in-house can be allocated for surfactant production as a result of ethylene oxide production capacity expansion.

We have two production plants, namely Jiaying Production Plant and Xiaoshan Production Plant.

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### Our Group's expansion plans

The following table sets forth information regarding our Group's planned production facilities, including those that are currently under development:

Production facility	Product type	Target date of commencement of operation	Expected capital expenditure and source of funding
Jiaying Production Plant – third phase ethylene oxide production facilities with a designed annual production capacity of 60,000 MT	Ethylene oxide	Early 2011	RMB300 million <sup>(Note)</sup> , to be funded by net proceeds of the Global Offering, internal resources and, if necessary, bank borrowings
Jiaying Production Plant – fourth phase ethylene oxide production facilities with a designed annual production capacity of 100,000 MT	Ethylene oxide	Early 2013	RMB600 million <sup>(Note)</sup> , to be funded by net proceeds of the Global Offering, internal resources and, if necessary, bank borrowings

Moreover, Sanjiang Honam was established in May 2010 in Jiaying of the Zhejiang Province with a registered capital of US\$12.0 million and a total investment amount of US\$29.2 million. We anticipate that Sanjiang Honam, the sino-foreign joint venture company jointly established and controlled by Honam Petrochemical Corp. and us, will commence the first phase construction of ethylene oxide production facilities with a designed annual production capacity of 100,000 MT at the end of 2010. We expect completion of the construction will take place by the end of 2011. We anticipate that the second phase construction of ethylene oxide production facilities with a designed annual production capacity of 100,000 MT will commence following the commencement of the first phase production of ethylene oxide. We intend to use approximately RMB98 million, to be funded by the net proceeds from the Global Offering, internal resources and, if necessary bank borrowings for capital contribution and investment in Sanjiang Honam. Pursuant to the joint venture agreement between Sanjiang Chemical and Honam Petrochemical Corp., among other things, each of Sanjiang Chemical and Honam Petrochemical Corp. has agreed to purchase 50% of the ethylene oxide produced by Sanjiang Honam at cost. Please refer to the subsection headed "Production capacities, production plant and storage facility – Joint venture arrangement with Honam Petrochemical Corp." in this section of this prospectus for further details on Sanjiang Honam.

*Note:* The expected licence and process design fees payable under new agreements with SD Company have been included.

### **Jiaying Production Plant**

We commenced our production of ethylene oxide in January 2006 and our production of surfactants in February 2008 at our Jiaying Production Plant.

Our Jiaying Production Plant is strategically located in Jiaying Port Economic Development Zone of Jiaying, Zhejiang Province, and is in close proximity to the Port of Zhapu (乍浦港) which is a national first class open port (國家一類開放口岸) for international trade. Our Directors believe that our Jiaying Production Plant has a definite geographical advantage in reducing cost of transportation of raw materials. Ethylene, our principal raw material for production of ethylene oxide, is generally transported by sea in tankers in large volume. We have installed an ethylene storage tank with capacity of 22,000 cubic metres, the largest ethylene storage tank in China according to the SAI Report on a parcel of land which we own with an aggregate site area of approximately 49,891 square metres near the Port of Zhapu (the “**Ethylene Storage Site**”). Ethylene imported by us is transported by sea to the Port of Zhapu and stored in our ethylene storage tank. Ethylene is then transported to our Jiaying Production Plant through our own pipelines which ensure safe transportation of ethylene.

Our Jiaying Production Plant is equipped with advanced equipment and machineries, some of which were purchased and imported from renowned overseas suppliers located in India, the United States and Japan. Such equipment and machineries include reactors and compressors in our ethylene oxide production device and other core equipment in our low temperature ethylene storage device, air separation plant, nitrogen liquefaction plant and carbon dioxide recollecting device. To the best of the knowledge and belief of our Directors, as the abovementioned equipment and machineries are technologically advanced and are largely essential to our operations, there are only very few entrusted alternative suppliers for the aforementioned equipment in the PRC.

As of the Latest Practicable Date, our designed annual production capacities of ethylene oxide and surfactants at our Jiaying Production Plant were approximately 120,000 MT and 200,000 MT respectively. Our Jiaying Production Plant has two production lines of ethylene oxide with a designed annual production capacity of 60,000 MT each. Our Jiaying Production Plant has two production lines of surfactants with a designed annual production capacity of 100,000 MT each.

Our Jiaying Site holds and occupies three parcels of land with an aggregate site area of approximately 306,764 square metres, over which our Jiaying Production Plant, office building, equipment room, main control room, warehouses, storage tanks and canteen were constructed. Three properties at our Jiaying Site with an aggregate gross floor area of approximately 4,779 square metres are under construction.

Among the aforesaid land and properties, two properties with an aggregate gross floor area of approximately 3,702 square metres owned by Sanjiang Chemical have been built on a parcel of land occupied by Yongming Petrochemical. As both Sanjiang Chemical and Yongming Petrochemical are companies within our Group, and Yongming Petrochemical has agreed in writing the aforementioned matters, our Directors believe that the discrepancies between the land user and the owner of the properties thereon will not lead to title disputes between the two companies. Our PRC Legal Advisers have advised that no penalties will be imposed on us due to the aforesaid discrepancies under PRC law. In addition, another two properties with an aggregate gross floor area of approximately 1,872 square metres have been constructed by Sanjiang Chemical on the aforesaid parcel of land occupied by Yongming Petrochemical. Yongming Petrochemical has applied for the building ownership certificates of such properties.

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We have not obtained building ownership certificates for four ancillary buildings, which are used for security guard rooms, rest lounges and weight room purposes, with a total gross floor area of approximately 580 square metres at our Jiaxing Site. We have not obtained the building ownership certificate for one building, which is used for rest lounge purpose, with a gross floor area of approximately 20 square metres at our Ethylene Storage Site.

As advised by our PRC Legal Advisers, the maximum penalty which the relevant authority may impose on us in respect of the aforesaid five properties would be the order of demolition of such properties within a prescribed time limit and a fine equivalent to less than one time of the construction costs, which, our Directors estimate, would not exceed RMB1.3 million.

Our Directors consider that the lack of building ownership certificates in respect of the aforesaid properties are not crucial to us and will not have a material impact on our operation for the reasons described below:

- (i) the aggregate area of the aforesaid properties represents approximately 1.85% of the total area of properties that we occupy; and
- (ii) these ancillary properties are used for security guard rooms, rest lounges and weight room purposes which are unrelated to our production activities and therefore would not have any material adverse effect on the business, financial condition and results of operation of our Group.

As the aforesaid properties are not production related, we will demolish the aforesaid properties if ordered by the relevant government authorities. The demolishing costs are estimated to be approximately RMB50,000, which, our Directors consider, would have insignificant impact on our financial position. It is not our current intention to relocate to other properties after the demolition.

Please refer to the section headed “Risk factors – Risks relating to our business – We have not obtained legal titles to some of the properties we own” in this prospectus for further details.

Details of the property valuation together with the summary of valuation and valuation certificates from the Independent Valuer are set out in Appendix IV to this prospectus.

### **Xiaoshan Production Plant**

Hangzhou Haoming commenced production of surfactants in May 1998 at the Xiaoshan Production Plant which is located in Xiaoshan, Hangzhou of the Zhejiang Province. We acquired, among other things, the ethylene oxide trading and manufacture and sale of surfactant business of Hangzhou Haoming in April 2010. As Hangzhou Haoming is under the common control and management of Mr. Guan and Ms. Han, the results of the business acquired from Hangzhou Haoming have been reflected in our Group’s results prior to 31 March 2010 by using merger accounting.

As of the Latest Practicable Date, our designed annual production capacity of surfactants at our Xiaoshan Production Plant was approximately 18,000 MT, with our first production line of designed annual production capacity of 8,000 MT and our second production line of designed annual production capacity of 10,000 MT.

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Our Xiaoshan Site occupies two parcels of land with an aggregate site area of approximately 16,733 square metres, over which our Xiaoshan Production Plant, office building, equipment room, main control room, warehouses and storage tanks were constructed. We have rented the properties with a total gross floor area of approximately 8,312 square metres on these two parcels of land from Hangzhou Haoming. Please refer to the section headed “Connected transactions” in this prospectus for details on the leases from Hangzhou Haoming.

Details of the property valuation together with the summary of valuation and valuation certificates from Independent Valuer are set out in Appendix IV to this prospectus.

### **Joint venture arrangement with Honam Petrochemical Corp.**

On 4 May 2010, Sanjiang Chemical entered into a joint venture agreement and a supplemental agreement with Honam Petrochemical Corp. (湖南石油化學株式會社) (“HPC”) which is a Korea-based petrochemical manufacturer, to establish Sanjiang Honam, a sino-foreign joint venture company in Jiaxing of the Zhejiang Province. Products manufactured by HPC include resins, ethylene oxide, ethylene glycol, benzene and other petrochemical and chemical products.

Pursuant to the joint venture agreement, Sanjiang Chemical and HPC agreed to establish Sanjiang Honam, a sino-foreign joint venture company jointly controlled by Sanjiang Chemical and HPC, with a registered capital of US\$12.0 million and a total investment amount of US\$29.2 million. Each of Sanjiang Chemical and HPC has an obligation to contribute a total of US\$6.0 million to the registered capital of Sanjiang Honam for a 50% shareholding interest. Moreover, Sanjiang Chemical and HPC have agreed that the net profit after tax derived in Sanjiang Honam, less any reserve funds, staff welfare funds and enterprise development fund, will be divided amongst them with reference to their respective percentage of capital contribution. Under the supplemental agreement, each of Sanjiang Chemical and HPC has agreed to purchase 50% of all ethylene oxide produced by Sanjiang Honam, the price of which shall be determined with reference to the actual cost of ethylene and other production costs incurred in the production process. Accordingly, ethylene oxide produced in Sanjiang Honam will only be sold to its shareholders. Pursuant to the supplemental agreement, in the event where HPC is unable to purchase the entire 50% of the ethylene oxide produced in a month, Sanjiang Chemical has agreed to take over and sell the remaining quantity and pay HPC 98.5% of the market value of the same. Alternatively, in the event where HPC’s demand for ethylene oxide exceeds the contracted quantity in a month, Sanjiang Chemical shall make, in favour of HPC, preferential adjustments to its share of ethylene oxide in exchange for HPC’s payment of 98.5% of the market value of the quantity transferred. HPC has agreed to supply ethylene to Sanjiang Chemical before Sanjiang Honam commences operations. Furthermore, Sanjiang Chemical has agreed to lease a piece of industrial land and to provide ancillary facilities and repair and maintenance services to Sanjiang Honam at agreed rates.

On 11 May 2010, Sanjiang Chemical and HPC established Sanjiang Honam in accordance with the terms and conditions of the joint venture agreement. Each of Sanjiang Chemical and HPC holds 50% shareholding interest and is entitled to appoint 50% of the members of the board of directors. As of Latest Practicable Date, each of Sanjiang Chemical and HPC has paid US\$1,199,858.30 and US\$1,200,000 respectively as its registered capital contribution. It is intended that Sanjiang Honam will principally engage in the manufacture and sale of ethylene oxide, ethylene glycol, oxygen, nitrogen and argon. The capital injected will be used for the construction of production facilities of Sanjiang Honam to produce ethylene oxide. We expect to commence the first phase construction of ethylene oxide production facilities with a designed annual production capacity of 100,000 MT at the end of 2010 and complete the

construction by the end of 2011. We anticipate that the second phase construction of ethylene oxide production facilities with a designed annual production capacity of 100,000 MT will commence following the commencement of the first phase production of ethylene oxide.

Under the prevailing PRC rules and regulations, ethylene oxide construction projects with an annual capacity of less than 200,000 MT are expressly banned. By forming a joint venture with HPC, we would be able to indirectly increase our ethylene oxide production capacity without a relatively large amount of initial capital outlay. Furthermore, by forming a non-controlling joint venture with HPC, we seek to strengthen the economical relationship and engage in technology exchanges with HPC, which our Directors believe would benefit both parties in terms of future business development. In addition, as HPC has agreed to supply ethylene to Sanjiang Chemical before Sanjiang Honam commences operations, our supply of ethylene can be further secured.

As we own a 50% shareholding interest in Sanjiang Honam and have the right to appoint 50% of the members of the board of directors, we do not control Sanjiang Honam. Therefore we do not account for Sanjiang Honam as our subsidiary.

### **Ethylene oxide production technology**

In January 2004, August 2006 and May 2009, we entered into licence, process design and technical assistance services agreements with Scientific Design Company, Inc. ("**SD Company**"). SD Company is a U.S. company established in 1946 that licenses petrochemical process technology, provides process engineering services and develops, manufactures and sells catalysts worldwide. According to the SAI Report, it is amongst a few dominant companies which possesses ethylene oxide production technologies and is one of the leading process technology companies that provide ethylene oxide production technologies to PRC ethylene oxide manufacturers. According to the SAI Report, there are at least two other companies that provide similar technologies.

The respective term of the agreements shall commence on the relevant effective date of the agreements and shall terminate on the fifth anniversary of the date of start-up, being the date on which feedstock is first introduced into the reactor system for the purpose of producing ethylene oxide. Under the agreements, we are granted with licences to use and practise a process, which is critical to our production of ethylene oxide. The licences granted are perpetual, non-exclusive and non-transferable. During the term of the agreements, SD Company shall disclose and make available to us the know-how and technical information relating to the production of ethylene oxide and engineering design of ethylene oxide production unit for our three production lines in our Jiaying Production Plant. SD Company also provides us with technical direction and technical assistance services in relation to the start-up, initial operation and performance tests of the three ethylene oxide production lines in our Jiaying Production Plant. We paid a one-off licence fee and process design fee for each of the agreements. The one-off licence fee and process design fee for our three ethylene oxide production lines totalled at approximately US\$6.8 million under the agreements. We have to pay a fee for technical assistance services provided by the technical personnel of SD Company at location away from the premises of SD Company and the expenses incurred by the said personnel only if such services are so requested by us. We have not requested for such services from SD Company during the Track Record Period and as of the Latest Practicable Date. No additional fee or royalty is required to be paid annually for the Group's use of the relevant know-how and technical information. Save for a sum of approximately US\$172,820 which is not yet due and payable under the terms of the agreement dated 7 May 2009, we have satisfied all our payment obligations under the agreements in a timely manner. During the Track Record Period and as at

the Latest Practicable Date, we had not defaulted on any provisions of the agreements with SD Company. The current agreements with SD Company only cover our two existing ethylene oxide production lines and our third ethylene oxide production line which will commence operation in early 2011. Accordingly, we have to enter into new agreements with SD Company for any other new production lines in the future. We expect that the fees payable under the new agreements with SD Company would be approximately US\$2 million for each of our fourth phase ethylene oxide production line and the new ethylene oxide production line of Sanjiang Honam.

Under the agreements, among other things, SD Company may, at its option, terminate the agreements and the licences granted forthwith by written notice to us if any payment required to be made by us under the agreements shall not be made when due and such default shall continue and remain unremedied for more than 90 days after written notice thereof is given by SD Company; or if we shall make any other material default thereunder and such default shall continue and remain unremedied for more than 90 days after written notice thereof is given to us by SD Company. We may at our option terminate the agreements forthwith by written notice to SD Company if SD Company shall make any material default under the provisions of the agreements and such default shall continue and remain unremedied for more than 90 days after written notice is given to SD Company by us.

#### **Engineering design of surfactant production facilities**

In February 2007, we contracted China BCEL International Engineering Co., Ltd.\* (中國中輕國際工程有限公司) (“**BCEL**”), a large-scale engineering consulting corporation in the PRC, for installation of the first phase of our surfactant production facilities with a designed annual production capacity of 100,000 MT at our Jiaxing Production Plant. In May 2009, we entered into an engineering design contract with BCEL for the engineering design of the second phase of our surfactant production facilities with a designed annual production capacity of 100,000 MT at our Jiaxing Production Plant. Under the aforesaid agreements entered into with BCEL, we are provided by BCEL with, among other things, know-how and technical information relating to the production of surfactant and engineering design of our first and second production lines of surfactants in our Jiaxing Production Plant. We paid a one-off contracting fee to BCEL under each of the aforesaid agreements in a timely manner.

#### **Technology advancement**

In addition to the technologies provided by the abovementioned technology and engineering companies, our technology team constantly seeks technology advancement to our production facilities with an aim to improve our production capacity and efficiency, as well as reduce costs. In 2007, we installed filler materials in the scrubber of our ethylene oxide production device, which enhanced ethylene oxide absorption, thereby increasing our production efficiency. Furthermore, in 2009, we made technology advancement in the cooling device for recycled water used in the production of ethylene oxide by replacing four electric cooling fans with hydro-turbine fans, which reduced our energy consumption in the production process.

### **Ethylene storage facility**

Our ethylene storage facility is located at the Port of Zhapu in Jiaxing, Zhejiang Province.

We own a parcel of land with an aggregate site area of approximately 49,891 square metres adjacent to the Port of Zhapu which is a national first class open port for external trade. We have installed an ethylene storage tank with a total storage capacity of approximately 22,000 cubic metres on such parcel of land for storage of ethylene which we imported. Such storage tank can effectively store 12,075 MT of ethylene which we imported. According to the SAI Report, our ethylene storage tank was the largest in China in terms of storage capacity as of 30 April 2010. Ethylene, our principal raw material for production of ethylene oxide, is transported by sea to the Port of Zhapu and stored in our ethylene storage tank. As ethylene is inflammable, our fully sealed ethylene storage tank provides suitable storage conditions by keeping ethylene in liquid state at or below the temperature of -104°C. Ethylene is then transported to our Jiaxing Production Plant which is in close proximity to the Port of Zhapu through our own pipelines to ensure safe transportation of ethylene.

Our ethylene storage tank can ensure a safe storage and stable supply of ethylene for our production. To ensure safe operating conditions of our ethylene storage tank, we conduct physical safety inspections every two hours on a daily basis. Our personnel who are responsible for monitoring the safety parameters of storage tank will report any irregularities and make any adjustments if necessary during the inspections. Further, our ethylene storage tank is equipped with automatic alarm and fire extinguishing systems and emergency stop mechanisms to allow our personnel to immediately control or attend to any emergency incidents and thus, prevent any damage done to our employees, ethylene stored and operation.

In order to accommodate our increasing ethylene oxide production capacity, we commenced the construction of our second ethylene storage tank having a total storage capacity of approximately 22,000 cubic metres on such parcel of land at Port of Zhapu in the second quarter of 2010. We anticipate the construction will be completed by the second quarter of 2011.

### **SUPPLIER AND PURCHASES**

Our principal raw material for our production of ethylene oxide is ethylene which we purchase from our suppliers. The principal raw material for our production of surfactants is ethylene oxide, which we manufacture ourselves. Other raw materials for production of surfactants vary depending on the type of surfactants to be manufactured. Fatty alcohol is a common type of raw material for production of surfactants.

We principally source and purchase ethylene from suppliers in Japan. According to SAI Report, approximately 98% of the domestic ethylene supplied is primarily for internal use of the suppliers and is not traded in the open market. To the best of the knowledge and belief of our Directors, domestic supplies of ethylene which can support our production capacity are not currently available in China. We generally maintain at least three suppliers so as to avoid reliance on any single source of supply. We regularly review and compare the pricing and terms offered by the suppliers. We also conduct routine sample tests of ethylene we purchase from our suppliers. These measures give assurance on the quality and reliability of ethylene for our production of ethylene oxide.

We enter into legally binding contracts with most of our suppliers on a yearly basis to fix the quantity of ethylene, ranging from approximately 100,000 MT to 240,000 MT, to be supplied to us in that year. We then place purchase orders from time to time according to our production needs. This ensures a steady supply of ethylene.



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The price of ethylene is agreed between our suppliers and us with reference to the CFR price quoted by ICIS at the time the purchase orders are placed. ICIS is an information provider for the chemical and oil industry. We believe that ICIS is trusted by many of the world's largest chemical companies, as well as manufacturers, analysts and traders of the relevant industry. Our purchases are mostly settled in USD and mainly through letters of credit. Our suppliers normally grant us approximately 90 days' credit period.

We source fatty alcohol, the main raw material for AEO surfactants, and other raw materials from local PRC suppliers. We place purchase orders from time to time according to our production needs. The prices of fatty alcohol and other raw materials are agreed between our suppliers and us with reference to the prevailing market prices of fatty alcohol and other raw materials respectively. Our payments for purchases are mostly settled in RMB by means of bank acceptances.

We have established good business relationship with most of our suppliers, among which, are reputable companies from Japan, with whom we have established business relationship since 2007. We believe that such relationship will continue to be good and stable. However, our Directors believe that alternative suppliers can easily be identified if so required. During the Track Record Period, we did not experience any difficulty in sourcing suppliers for raw materials or any production disruption due to shortage of supply of raw materials.

During the Track Record Period, our five largest raw material suppliers, who were Independent Third Parties, together accounted for approximately 79.3%, 68.0%, and 68.9% and 83.1% of our total purchases of raw materials respectively, and our largest raw material supplier accounted for 47.7%, 65.1%, 40.3% and 47.4% of our total purchases of raw materials respectively. None of our Directors or their respective associates or any Shareholder, who to the knowledge of our Directors, owns more than 5% of the issued Shares immediately after completion of the Global Offering, had any interest in any of our five largest raw material suppliers during the Track Record Period.

### **RAW MATERIALS, ENERGY AND UTILITIES**

#### **Raw materials**

The principal raw materials for our production of ethylene oxide are ethylene and oxygen. Oxygen is separated through our air separation plant from air. Ethylene is the key raw material purchased by our Group. During the Track Record Period, the cost of ethylene we consumed for sales amounted to approximately RMB525.9 million, RMB536.8 million, RMB577.4 million and RMB347.7 million respectively, representing approximately 78.8%, 73.7%, 62.1% and 76.4% of our total cost of sales.

One of the principal raw materials for our production of surfactants and surfactant processing services is ethylene oxide which we manufactured from ethylene. We do not have to source ethylene oxide from external suppliers. Other raw materials for production of surfactants vary depending on the type of surfactants to be manufactured.

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In providing surfactants processing services, raw materials other than ethylene oxide, such as fatty alcohol are provided by our customers and delivered to our Sanjiang Production Plants for processing into surfactants, whilst we also procure auxiliary raw materials for our surfactants processing customers.

During the Track Record Period, we did not experience any shortage of supply of raw materials and raw materials costs accounted for approximately 81.2%, 76.9%, 71.2% and 80.5% of our total cost of sales respectively.

### **Energy and utilities**

Electricity is the principal power source for our production. We have secured a double-circuit electricity power supply from 浙江嘉興電力局 (Zhejiang Jiaying Electric Power Bureau) to our Sanjiang Production Plants to maintain a stable electricity supply. During the Track Record Period, the cost of electricity supply for our production amounted to approximately RMB55.1 million, RMB75.2 million, RMB115.1 million and RMB37.6 million respectively, representing 8.3%, 10.3%, 12.4% and 8.3% of our cost of sales respectively. During the Track Record Period, we did not experience any electricity supply shortage.

Desalinated water is used for absorption of ethylene oxide in the production of ethylene oxide and cooling of reactants in the production of both ethylene oxide and surfactants. We purchase desalinated water from Jiahua Industrial Park Co, a company ultimately controlled by Mr. Guan and Ms. Han. Please refer to the section headed “Connected transactions – Continuing connected transactions subject to reporting, announcement and independent shareholders’ approval requirements – Supply agreements – Water and miscellaneous materials supply agreement” in this prospectus for further details on the transaction. In order to reduce water usage and waste water discharge, we have installed water treatment facilities in our Sanjiang Production Plants for water recycling purpose. During the Track Record Period, we did not experience any water shortage.

Steam is used for heating of reactants in the production of both ethylene oxide and surfactants. We purchase steam for heating of reactants from Jiahua Industrial Park Co, a company ultimately controlled by Mr. Guan and Ms. Han. Please refer to the sections headed “Connected transactions – Continuing connected transactions subject to reporting, announcement and independent shareholders’ approval requirements – Supply agreements – High pressure steam supply agreement” and “Connected transactions – Continuing connected transactions subject to reporting, announcement and independent shareholders’ approval requirements – Supply agreements – Low pressure steam supply agreement” in this prospectus for further details on the transactions. Steam is also used for vaporising the ethylene we imported. Ethylene in gaseous state is then transported to our Jiaying Production Plant through our own pipelines. We purchase steam for vaporisation of ethylene from Jiaying Rewang, a company which is owned as to 40% by Jiahua Industrial Park Co. Please refer to the section headed “Connected transactions – Continuing connected transactions exempt from reporting, annual review, announcement and independent shareholders’ approval requirements – Purchasing low pressure steam from Jiaying Rewang – Low pressure steam supply agreement with Jiaying Rewang” in this prospectus for further details on the transaction.

During the Track Record Period, the total utilities expenses amounted to approximately RMB69.3 million, RMB99.3 million, RMB165.1 million and RMB53.9 million respectively, representing approximately 10.4%, 13.6%, 17.8% and 11.8% of our total cost of sales respectively.

## **SALES AND MARKETING**

### **Marketing and promotion**

We market our products through our sales and marketing teams. The responsibilities of the sales and marketing teams include the promotion of our products to potential and existing customers, market research and analysis, implementation of marketing and sales strategies, customer visits and provision of after-sale services. As of the Latest Practicable Date, our sales and marketing teams comprised seven personnel. We provide training to our sales personnel including information on our products and their applications and customer service skills. We recognise the importance of marketing to our business growth and have adopted the following marketing strategies:

#### *Advertisements*

To enhance the awareness of our products, we regularly place advertisements in industry magazines to promote our brand and our products.

#### *Industry conferences*

We attend industry conferences to explore new potential customers and maintain relationships with existing customers. After identifying potential target customers during the industry conferences, our sales and marketing team will follow up by phone calls or visiting the potential customers in person to understand their needs and seek business opportunities.

#### *Customer nurturing*

We treasure the business relationship with our customers. Our sales and marketing team pays regular visits to our existing customers thus to maintain good relationships with our customers, keep abreast of their needs and obtain their feedbacks on the quality of our products.

We also keep abreast with the latest market development by subscribing to industry intelligence, conducting news searches and paying customers visits. Our sales and marketing team regularly updates our management with the latest market trend who in turn will adjust our sales and marketing plan or product mix if necessary.

### **Customers**

We have established years of good business relationship with most of our major customers since 2006 and are committed to providing high quality customer service. Our ethylene oxide customers include manufacturers of surfactants and other chemicals, as well as trading companies which sell our products to their customers in the PRC. For the two years ended 31 December 2008, our revenue derived from sales of ethylene oxide attributable to trading companies was over 80% and 50% respectively with the remaining attributable to manufacturers as we sought to, through the broad distribution network of trading companies, market our ethylene oxide when we were still relatively new to the ethylene oxide market. For the year ended 31 December 2009 and the four months ended 30 April 2010, over 60% of our ethylene oxide was sold to manufacturers of surfactants and other chemicals with the remaining attributable to trading companies. The shift in our focus from trading companies to manufacturers was part of our strategy to develop our own distribution channels and customer base in order to secure a steady

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and long term source of revenue through direct business relationships with end customers. Our top ten ethylene oxide customers included 嘉興金燕化工有限公司 (Jiaying Jinyan Chemical Co., Ltd.\*) and 江蘇銀燕化工股份有限公司 (Jiangsu Yinyan Speciality Chemicals Co., Ltd.\*) during the Track Record Period. 嘉興金燕化工有限公司 (Jiaying Jinyan Chemical Co., Ltd.\*) was one of our overall top ten customers for the two years ended 31 December 2009 and the four months ended 30 April 2010. 江蘇銀燕化工股份有限公司 (Jiangsu Yinyan Speciality Chemicals Co., Ltd.\*) was one of our overall top ten customers for the two years ended 31 December 2008. Our surfactants customers and our surfactant processing customers include manufacturers of household and industrial cleansing agent and trading companies which sell our products to their customers in the PRC. For the two years ended 31 December 2008, our revenue derived from sale of surfactants attributable to manufacturers was over 80% and 60% respectively with the remaining attributable to trading companies. For the year ended 31 December 2009 and the four months ended 30 April 2010, over 70% of the Group's surfactants were sold to trading companies with the remaining attributable to manufacturers. As the new surfactant production line of our Jiaying Production Plant commenced production in 2008 and a larger portion of our self-manufactured ethylene oxide was available for production of surfactants as a result of the expanded production capacity in December 2008, we were able to increase our surfactants output. As such, we shifted our focus from manufacturers to trading companies since 2009 in order to enhance the market penetration of our surfactants products through the broad distribution network of trading companies. Our top ten surfactants customers included 納愛斯集團有限公司 (Nice Group Co., Ltd.\*), 麗水市雕牌化工有限公司 (Lishui City Diao Brand Chemical Co., Ltd.\*) and 浙江傳化股份有限公司 (Zhejiang Transfar Co., Ltd.\*) during the Track Record Period. As of the Latest Practicable Date, all of our customers are PRC companies located in China.

The following table sets forth the breakdown of our customer composition (approximate %) for our ethylene oxide and surfactants products during the Track Record Period:

	For the year ended 31 December			For the four months ended 30 April
	2007	2008	2009	2010
Ethylene oxide				
Manufacturers	18%	45%	61%	64%
Trading companies	82%	55%	39%	36%
Surfactants				
Manufacturers	89%	61%	28%	20%
Trading companies	11%	39%	72%	80%

Since 2009 we have entered into contracts with a majority of our ethylene oxide customers on a yearly basis to fix the quantity of ethylene oxide to be supplied to them for the following year. They then place purchase orders with us from time to time. We do not enter into long term contracts with our surfactants customers and our surfactant processing customers.

The prices of ethylene oxide and surfactants are agreed between our customers and us with reference to the prevailing market prices of ethylene oxide and surfactants respectively. Our surfactant processing fees are agreed between our customers and us with reference to the market prices of ethylene oxide, our costs of auxiliary raw materials, energy, utilities and labour plus a profit margin.

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We generally deliver ethylene oxide to our customers after they have made full payment.

We generally grant to our surfactants customers and our surfactants processing customers credit period of less than 30 days after the date of delivery depending on the relevant customer's reputation and creditworthiness and size of purchase orders. Our management has delegated a cross-department team, headed by a general manager, comprising staff members from sales department, finance department and legal department to assess and monitor the credit risks of the customers. In order to manage the credit risks associated with trade receivables effectively, each customer has a maximum credit limit and the credit limits are evaluated periodically. The credit limits are assessed with reference to the sales contracts entered into by each customer and the corresponding repayment progress is closely followed up by the sales department in order to ensure prompt action is taken to recover overdue debts. The trade receivables of our Group amounted to approximately RMB34.0 million, RMB20.0 million, RMB17.8 million and RMB18.6 million as at 31 December 2007, 2008 and 2009 and 30 April 2010 respectively.

Our customers usually settle their payment in RMB through telegraphic transfers or by means of bank acceptances (銀行承兌匯票).

During the Track Record Period, our five largest customers, who were Independent Third Parties (save for 浙江贊宇科技股份有限公司 (Zhejiang Zanyu Technology Co. Ltd.\*) ("**Zhejiang Zanyu**") by virtue of Mr. Guan's indirect shareholding in Zhejiang Zanyu), together accounted for approximately 62.0%, 49.8%, 39.8% and 44.6% of our revenue respectively, and our largest customer accounted for 38.4%, 19.2%, 18.5% and 19.5% of our revenue respectively. Jiahua Industrial Park Co, a company ultimately controlled by Mr. Guan and Ms. Han, holds approximately 4.87% shareholding interest in Zhejiang Zanyu which is one of our five largest customers. Zhejiang Zanyu holds the entire shareholding interest in 嘉興贊宇科技有限公司 (Jiaying Zanyu Technology Development Co, Ltd.\*) ("**Jiaying Zanyu**", together with Zhejiang Zanyu, the "**Zanyu Group**"). During the Track Record Period, the revenue attributable to Zanyu Group were approximately RMB0, RMB48.4 million, RMB59.9 million and RMB32.3 million respectively, representing approximately 0%, 5.1%, 6.5% and 5.7% of our revenue, respectively. Zanyu Group is principally engaged in the businesses of the manufacture of leather chemicals, surfactants and daily chemical products. To the best of the knowledge and belief of our Directors, the surfactants products manufactured by Zanyu Group are different from those products manufactured by us. We mainly manufacture non-ionic surfactants products, whereas, to the best of the knowledge and belief of our Directors, Zanyu Group mainly manufactures anionic surfactants products, which are different types of surfactants with different chemical properties. Our surfactants products, namely AEO surfactants, are generally used as raw materials for the production of Zanyu Group's surfactants products, namely AES and AESA and hence, Zanyu Group's products are the downstream products of our AEO surfactants. As such, Zanyu Group is not engaged in any business in direct competition with our Group. The transactions entered into between our Group and Zanyu Group were carried out on normal commercial terms and did not have the effect of distorting our results in the Track Record Period.

In 2009, we ceased trading with a major customer which accounted for approximately 45% and 22% of our revenue in 2007 and 2008 respectively. In 2007 and 2008, the early stage of our Group's ethylene oxide business, our Group supplied large quantities of ethylene oxide to such customer which was a dominant player in the PRC oil-refined products and petrochemical products market. In order to maintain business relationship, we provided concessions to such customer in the form of lower selling price for the ethylene oxide and credit period which deviated from our normal commercial terms. As our business gradually developed and also in order to reduce our reliance on a single major customer, we

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sought better business opportunities with many other ethylene oxide customers, who were willing to provide better prices and business terms for our ethylene oxide. As such, sales to such customer gradually decreased to the extent that it ceased to be one of our top five customers from 2009 onwards.

Save for the aforesaid, none of our Directors or their respective associates or any Shareholder, who to the knowledge of our Directors, owns more than 5% of the issued Shares immediately after completion of the Global Offering, had any interest in any of our five largest customers during the Track Record Period.

### **Customer service**

We are dedicated to providing customer service of the highest quality. We demonstrate flexibility and innovation in our endeavour to develop customised solutions to meet our customers' needs. We also endeavour to supply our products to our customers in a timely manner even if purchase orders are made under short notice. We run an around the clock operation throughout the year so that our customers can take delivery of our products at any time.

In addition, we regularly visit our customers and conduct customer surveys in order to understand their evolving needs and resolve their concerns proactively. These regular visits also enable us to gain an insight into the latest market trends and capture potential business opportunities.

### **LOGISTICS AND TRANSPORTATION**

Our products are delivered to our customers through our own pipelines or by land or sea transportation. We generally deliver ethylene oxide, surfactants, oxygen, nitrogen and argon in liquid state to our customers by road tankers. We also deliver ethylene oxide in liquid state and nitrogen in gaseous state through our own pipelines to customers which are in close proximity to our Jiaying Production Plant to reduce transportation cost. Surfactants are also delivered to our customers by trucks and vessels.

We generally do not provide free delivery services to our customers. Some of our customers take delivery of our products at our production facilities or make their own transportation arrangements. We also assist our customers in arranging for transportation services from Independent Third Party transportation services providers.

### **INVENTORY CONTROL**

Our inventories mainly consist of raw materials, which are mostly chemicals including ethylene, fatty alcohol and other auxiliary materials, and our finished products. We conduct our production planning in conjunction with our purchasing and sales planning on a regular basis and maintain records of our inventory levels. This enables our production, procurement and sales departments to effectively monitor changes and levels of inventory on a timely basis. We adjust our production plan, raw materials purchase plan and sales plan accordingly based on such information.

Some of our customers enter into contracts with us on a yearly basis to fix the quantity of ethylene oxide to be purchased from us for the following year. This enables us to conduct production planning and inventory planning in advance without the need of maintaining a higher buffer inventory level. During the Track Record Period, the sales of ethylene oxide to these customers accounted for approximately

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0%, 1%, 54% and 91% of our total revenue derived from sales of ethylene oxide respectively. In the early stage of our Group's business, our Group supplied large quantities of ethylene oxide to a customer which was a dominant player in the PRC oil-refined products and petrochemical products market, who did not enter into contracts with us on a yearly basis. As our business gradually developed, we sought better business opportunities with many other ethylene oxide customers, who were more willing to enter into contracts with us on a yearly basis. As a result, we have been able to improve our production and inventory planning since 2009.

In addition, given our ability to manufacture ethylene oxide and over 100 types of surfactants, we are able to respond to the changes in market condition in terms of product pricing and customers' demand in a timely manner by resiliently switching between selling ethylene oxide to our customers and utilising the ethylene oxide manufactured by us to manufacture surfactants, with an aim to increase our overall profitability.

Our Directors believe that, by implementing the above measures, we can effectively control our inventory level in order to better control our cost and thereby increase our profitability.

Our inventories as at 31 December 2007, 2008 and 2009 and 30 April 2010 amounted to approximately RMB94.8 million, RMB77.1 million, RMB67.7 million and RMB115.2 million respectively.

### QUALITY AND SAFETY CONTROL

We place substantial emphasis on quality control of our products. We were accredited the certificate of "ISO9001 Quality Management System" in June 2008 for our good quality management practices in Sanjiang Chemical.

As of the Latest Practicable Date, our Group had a quality control team comprising 29 personnel who were qualified technicians and staff members. Some of our Group's quality control staff possess (i) vocational certificates and/or (ii) diplomas from technical institutes in the PRC. Most of the personnel have vast experience in the chemical industry.

We provide regular internal and external training programmes to our quality control personnel in order to standardise the quality control procedures. Such training programmes include quality control in the production process. Attendees are usually required to sit for a test after the training.

We have implemented a series of internal policies to ensure thorough and strict quality control during the various stages of production, from raw material purchase, production process to inventory storage. Sample testing of raw materials is conducted to ensure that the quality of raw materials meets our required standard. We have set up multiple inspection points at different production stages to test our products during the production process as well as random sample testing. Each of our Sanjiang Production Plants has a team of personnel who are responsible for monitoring the parameters of equipment, stability of materials, reporting any irregularities and making adjustments accordingly during the production process. We maintain records of storage levels of our raw materials and products to ensure that the storage level is in strict compliance with the relevant safety standards and the PRC laws and regulations.

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We follow up with our customers by regular visits or customer surveys on product quality after delivery to ensure a high level of client satisfaction and sustained long term quality relationship.

We are committed to achieving a high standard of industrial health and safety. We have implemented a series of internal policies to ensure health and safety of our employees and have taken measures to comply with all relevant PRC laws and regulations applicable to health and safety. In particular, we have 15 designated personnel for our production plants who are responsible for, among others, overseeing and monitoring our labour, hygiene and safety conditions. Most of these personnel received internal and/or external trainings on production safety. Three of them possess the qualifications for production safety management issued by the Administration of Work Safety of Jiaxing Port Economic Development Zone and/or the Administration of Work Safety of Xiaoshan District, Hangzhou. Furthermore, four factory managers and/or deputy managers who are in charge of our production have also obtained such qualifications. Mr. Niu Yingshan, our executive Director, is responsible for the management of production safety of our Group. Mr. Niu also possesses the aforesaid qualification for production safety management. From September 2007 to August 2008, Mr. Niu was appointed by Jiaxing Port Economic Development Zone Management Committee of Development and Construction (嘉興港區開發建設管理委員會) as a technical consultant on production safety of Jiaxing Port Economic Development Zone. Since April 2010, Mr. Niu has been appointed by Haiyan Administration of Work Safety (海鹽縣安全生產監督管理局) as a member of the Expert Committee on Production Safety of Chemical Industry in Haiyan, Jiaxing for a term of two years. With an aim to ensure adequate safety knowledge amongst all personnel in the workplace, we provide induction and safety education programmes to our employees through the provision of safety instruction manuals, training seminars and safety knowledge and response testing. Moreover, as our personnel control and monitor the daily operation of our production facilities from computerised operation control rooms, as well as conduct periodic physical safety inspections of our production equipment and facilities, we have the ability to attend to any safety and health issues without delay and thus, provide a healthy and safe workplace for our personnel.

During the Track Record Period, our annual expenditure in respect of safety matters were approximately RMB2.3 million, RMB4.9 million, RMB0.9 million and RMB1.9 million respectively. We incurred relatively high safety-related expenses in 2008 as we conducted a comprehensive repair and maintenance work on our production facilities. We estimate that approximately RMB6.8 million will be expended as safety costs for the full maintenance of our production facilities in 2010 and approximately RMB8.4 million will be expended for our third phase of the ethylene oxide production project to be completed in 2011.

Our chemical production business involves the handling, storage and use of hazardous, flammable and explosive materials, including ethylene, ethylene oxide and ethylene glycol. Improper handling of these hazardous materials can cause serious health and safety issues. We have not experienced any major incidents of improper handling of hazardous materials or products since the establishment of each of the members of our Group. We have been subject to the inspections by the local governmental authority from time to time. During the Track Record Period, we had complied with all relevant PRC health and safety laws and regulations and had not been subject to any fine, penalty or citation for our health and safety measures. During the Track Record Period, there had not been any major work accidents causing material health or safety issues. As advised by our PRC Legal Advisers, all the relevant licences and permits in relation to the safety control of our Group are valid and so far as our PRC Legal Advisers are aware, there is no legal impediment for renewal of such licences and permits.



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### RESEARCH AND DEVELOPMENT

We have a research and development centre at our headquarters in Jiaxing, which employed 19 engineers and technicians in our operation and production departments as of the Latest Practicable Date. These engineers and technicians, apart from performing production and other operational functions, engage in research and development projects organised and decided by our research and development centre. With our research and development team, we strive to enhance our manufacturing technologies, improve the quality of our existing products and develop new types of surfactants.

We plan to explore opportunities to form collaboration and/or cooperation with universities in the PRC to upgrade our production technologies and reduce our production costs.

### EMPLOYEES

As of the Latest Practicable Date, we had a total of 462 full-time employees. The following sets out the number of employees by function as of the Latest Practicable Date:

	<b>Number of employees</b>
Senior management	6
Technical	6
Finance and accounting	10
General administration	19
Operation and production	378
Sales and marketing	7
Quality control	29
Procurement	7
	<hr/>
Total	<u>462</u>

Our Directors believe that our success is attributable in part to our ability to attract, recruit and retain quality employees.

In order to maintain the quality, knowledge and skill levels of our employees, we place strong emphasis on training. We provide training to our employees periodically, including introductory training for new employees, technical training, professional and management training and health and safety training.

We provide employee benefits, including housing subsidies, shift subsidies, bonuses, allowances, medical check-up, staff quarters, social insurance contributions (including unemployment insurance, medical insurance, work-related injury insurance, pension insurance and maternity insurance) and housing fund contributions. During the Track Record Period, our aggregate staff costs (including Directors' remuneration) amounted to approximately RMB13.5 million, RMB14.7 million, RMB22.9 million and RMB7.4 million respectively, representing approximately 1.5%, 1.5%, 1.8% and 1.3% of our total revenue.

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We enter into individual employment/ labour contracts with our employees with terms ranging from one year to five years. Housing subsidies are provided to some of our employees who have entered into long term employment contracts with us.

We have not experienced any significant difficulty in recruiting employees. We have not experienced any strikes, work interruptions or labour disputes. Our Directors consider that we have good relationships with our employees.

Under the relevant PRC laws and regulations, we are required to contribute to a number of employee social welfare schemes in respect of our employees. Such schemes include social insurance contributions and housing fund contributions. During the Track Record Period, we did not fully comply with the social insurance and housing fund requirements for our employees because (i) a number of employees declined our Group's payment of social insurance contributions on their behalf as such payment might reduce their direct disposable income; and (ii) a number of employees declined our Group's payment of housing fund contributions on their behalf as they did not foresee that they would purchase properties in the near future and given that the contributions made would not be returned to them in cash, they preferred not to make such contributions. We estimate that the aggregate unpaid amount by our Group to the social insurance authority for the years ended 31 December 2007, 2008 and 2009 and the four months ended 30 April 2010 would be approximately RMB1.03 million, RMB1.40 million, RMB1.86 million and RMB0.69 million respectively, and the aggregate unpaid amount by our Group to the housing fund authority for the years ended 31 December 2007, 2008 and 2009 and the four months ended 30 April 2010 would be approximately RMB0.69 million, RMB1.00 million, RMB1.14 million and RMB0.31 million respectively. We have made the relevant provisions in our Group's consolidated accounts.

In hope to settle the outstanding social insurance and housing fund contributions, we and our PRC Legal Advisers have consulted Pinghu Social Insurance Management Centre (平湖市社會保險管理中心) and Jiaxing Housing Fund Management Centre Pinghu branch (嘉興市住房公積金管理中心平湖市分中心), being the competent social insurance and housing fund authorities which supervise us in relation to our Group's social insurance and housing fund contributions in Jiaxing, Zhejiang Province of the PRC respectively. Our PRC Legal Advisers have advised, based on the consultation with the social insurance authority, the social insurance authority would not accept our payments for the outstanding social insurance contributions for our former employees. As to our current employees, the social insurance authority would only allow us to settle the relevant outstanding amounts since their commencement of employment or since the employees have payment records on social insurance contributions at Pinghu Social Insurance Management Centre, whichever is later. As the aforementioned conditions do not apply to any of our current employees, the social insurance authority would not accept our payments for the outstanding social insurance contributions. Our PRC Legal Advisers have further advised, based on the consultation with the housing fund authority, the housing fund authority would only accept our payments for the outstanding housing fund contributions for our current employees after we first opened our housing fund account with the authority in November 2009. As the aforementioned conditions apply to four employees of our Group, the housing fund authority would only accept our payments for these four employees. The relevant outstanding amounts for their housing fund contributions were RMB6,433 in aggregate. We have paid the sum of RMB6,433 in full to the housing fund authority in July 2010.

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As advised by our PRC Legal Advisers, under the relevant laws and regulations of the PRC, we may be ordered by the relevant social insurance authority to pay the outstanding social insurance contributions within a prescribed time limit, and a late charge at a daily rate of 0.2% on the outstanding contributions may be imposed if such payment is not made within the prescribed time limit. In respect of the housing fund, we may be ordered by the relevant housing fund authority to pay the outstanding housing fund contributions and a late charge at a daily rate of 0.1% on the outstanding contribution may be imposed on us. However, as the social insurance and housing fund authorities do not allow us to make full payments for the outstanding social insurance and housing fund contributions and we have paid the aforesaid housing fund contributions acceptable by the authority, our PRC Legal Advisers are of the view that the risk of the relevant authority imposing any penalty on our Group is very remote. Our PRC Legal Advisers have however advised that in case an employee of our Group succeeds in labour dispute against us with respect to the outstanding social insurance and housing fund contributions, we may still be required to make such outstanding contributions to such employee, the maximum amount of which was estimated to be RMB8.1 million in aggregate as of 30 April 2010.

Pursuant to a deed of indemnity dated 2 September, 2010 executed by Mr. Guan and Sure Capital in favour of our Group, Mr. Guan and Sure Capital, being our controlling shareholders, have agreed to indemnify our Group, among others, against any payment obligations or penalties imposed by any relevant authorities in relation to such non-compliance with the employee welfare contribution regulations.

Save as disclosed in the prospectus, our PRC legal advisers have advised that we have complied with all the laws and regulations in respect of the payment of employee benefits for all our employees.

### LICENCES AND PERMITS

We are principally engaged in the manufacture and supply of ethylene oxide and surfactants, as well as other chemical products such as ethylene glycol and industrial gases, namely oxygen, nitrogen and argon. We are required to obtain the Certificate of Approval for Production and Storage of Hazardous Chemicals (危險化學品生產、存儲批准證書) issued by Jiaying Administration of Work Safety (嘉興市安全生產監督管理局), the Safety Production Permit (安全生產許可證) issued by Zhejiang Administration of Work Safety (浙江省安全生產監督管理局), the National Production Licence for Industrial Products (全國工業產品生產許可證) issued by the Zhejiang Administration of Quality Supervision, Inspection and Quarantine (浙江省質量監督檢驗檢疫總局), and the Hazardous Chemical Operation Licence (危險化學品經營許可證) issued by Jiaying Administration of Work Safety for our business operation. We are also required to obtain approval from the competent governmental authorities in the PRC for our production projects of ethylene oxide, liquefied industrial gases and surfactants.

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The following table sets forth the details of the licences and permits obtained by the Group and Sanjiang Honam:

Certificate/Licence	Grantee/licensee	Content of Permission	Grant Date	Expiry Date	Granting Authority
The Certificate of Approval for Production and Storage of Hazardous Chemicals (No. JXAP – F – 0055)	Sanjiang Chemical	Annual production of 60,000 MT of ethylene oxide, 4,440 MT of ethylene glycol, 1,100 MT of liquid oxygen, 500 MT of liquid nitrogen, 2,500 MT of liquid argon, recycling of 50,000 MT of liquid carbon dioxide, storage of 20,000 m <sup>3</sup> of ethylene and 10,000 m <sup>3</sup> of propylene	3 February 2010	Open-end permit	Jiaxing Administration of Work Safety
The Safety Production Permit (No. (ZJ) WH An Xu Zheng Zi [2009] – F – 1340)	Sanjiang Chemical	Annual production of 60,000 MT of ethylene oxide, 4,440 MT of ethylene glycol, 1,100 MT of liquid oxygen, 500 MT of liquid nitrogen, 2,500 MT of liquid argon, recycling 50,000 MT of carbon dioxide (including 5,000 MT for food and beverage uses), storage of 20,000 m <sup>3</sup> of ethylene	20 April 2010	23 December 2012	Zhejiang Administration of Work Safety
The National Production Licence for Industrial Products (No. (Zhe) XK13 – 010 – 00026)	Sanjiang Chemical	Production of industrial oxygen, industrial nitrogen, pure nitrogen, pure argon, industrial liquid carbon dioxide	8 April 2010	14 February 2013	Zhejiang Administration of Quality Supervision, Inspection and Quarantine
The National Production Licence for Industrial Products (No. (Zhe) XK13 – 014 – 00005)	Sanjiang Chemical	Production of ethylene oxide	8 April 2010	5 June 2013	Zhejiang Administration of Quality Supervision, Inspection and Quarantine

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Certificate/Licence	Grantee/licensee	Content of Permission	Grant Date	Expiry Date	Granting Authority
The Certificate of Approval for Production and Storage of Hazardous Chemicals (No. ZJAP – F – 001610)	Yongming Petrochemical	Production of 60,000 MT of ethylene oxide, 4,400 MT of ethylene glycol (by-product), 1,100 MT of liquid oxygen, 500 MT of liquid nitrogen, 2,500 MT of liquid argon	13 November 2007	Open-end permit	Zhejiang Administration of Work Safety
The Safety Production Permit (No. (ZJ) WH An Xu Zheng Zi [2009] – F – 0937)	Yongming Petrochemical	Annual production of 60,000 MT of ethylene oxide, 1,100 MT of liquid oxygen, 500 MT of liquid nitrogen, 2,500 MT of liquid argon	30 July 2009	29 July 2012	Zhejiang Administration of Work Safety
The National Production Licence for Industrial Products (No. (Zhe) XK13 – 010 – 00031)	Yongming Petrochemical	Production of industrial oxygen, industrial nitrogen, pure nitrogen, pure argon	21 April 2010	20 April 2015	Zhejiang Administration of Quality Supervision, Inspection and Quarantine
The National Production Licence for Industrial Products (No. (Zhe) XK13-014-00009)	Yongming Petrochemical	Production of ethylene oxide	21 April 2010	20 April 2015	Zhejiang Administration of Quality Supervision, Inspection and Quarantine
The Hazardous Chemical Operation Licence (No. Jia An Jian Jing (Yi) Zi [2007] A91005)	Sanjiang Trading	Wholesale (direct selling) of ethylene oxide and ethylene	31 October 2007	17 October 2010 (Note)	Jiaxing Administration of Work Safety
The Certificate of Approval for Production and Storage of Hazardous Chemicals (No. JXAP – F – 0064)	Sanjiang Honam	Annual production of 200,000 MT of ethylene oxide	11 May 2010	Open-end permit	Jiaxing Administration of Work Safety

*Note:* As of the Latest Practicable Date, Sanjiang Trading had applied to Jiaxing Administration of Work Safety for the renewal of its Hazardous Chemical Operation Licence. We expect to obtain the renewed licence in September 2010.

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Upon obtaining the consent from the Economic Development Bureau of Jiaying Port Economic Development Zone (嘉興港區經濟發展局) and the Administration of Work Safety of Jiaying Port Economic Development Zone (嘉興港區安全生產監督管理局) in December 2005, Sanjiang Chemical commenced its trial production of ethylene oxide and industrial gases in January 2006 and obtained the Safety Production Permit in December 2006. Sanjiang Chemical however had not applied for the National Production Licence for Industrial Products after obtaining the Safety Production Permit in a timely manner due to its inadvertence in updating itself of the latest development of the laws and regulations applicable to our Group. Sanjiang Chemical subsequently obtained the said production licences for the production of industrial gases and ethylene oxide in February 2008 and June 2008 respectively. According to the written confirmation issued by Zhejiang Quality and Technical Supervision Bureau (浙江省質量技術監督局) in September 2008, the aforesaid production prior to the issuance of National Production Licence for Industrial Products would not be regarded as production without proper licences. As advised by our PRC Legal Advisers, Zhejiang Quality and Technical Supervision Bureau is the proper authority to issue the aforesaid confirmation and such confirmation is legal and valid. As such, our PRC Legal Advisers are of the view that no penalty will be imposed on our Group by the relevant authorities for the aforesaid production prior to the issuance of such production licences.

Upon obtaining the consent from Jiaying Administration of Work Safety in December 2008, Yongming Petrochemical commenced its trial production of ethylene oxide and industrial gases in December 2008 and obtained the Safety Production Permit in July 2009. Yongming Petrochemical first applied for the National Production Licence for Industrial Products in August 2009 but was informed by the relevant authority that its application could not be processed due to its misunderstanding of some application requirements. Yongming Petrochemical therefore amended and resubmitted its application which was acknowledged by the relevant authority in March 2010. Yongming Petrochemical obtained the said production licences for the production of ethylene oxide and industrial gases in April 2010. Jiaying Quality and Technical Supervision Bureau (嘉興市質量技術監督局) issued a written confirmation on 30 April 2010 confirming that Yongming Petrochemical was entitled to commence production after submission of the application for National Production Licence for Industrial Products. The Quality and Technical Supervision Bureau of Jiaying Port Economic Development Zone (嘉興市質量技術監督局港區分局) further confirmed on 5 May 2010 that Yongming Petrochemical has been complying with the laws and regulations concerning the quality and technical supervision and no illegal action in regard thereof has been found since its establishment. As advised by our PRC Legal Advisers, Jiaying Quality and Technical Supervision Bureau and the Quality and Technical Supervision Bureau of Jiaying Port Economic Development Zone are the proper authorities to issue the aforesaid confirmations and such confirmations are legal and valid. As such, our PRC Legal Advisers are of the view that no penalty will be imposed on our Group by the relevant authorities for the aforesaid production prior to the issuance of such production licences.

Yongming Petrochemical constructed its ethylene oxide production facilities with a designed annual production capacity of 120,000 MT (being one 60,000 MT project completed in December 2008 and one 60,000 MT project which is currently under construction and expected to complete by early 2011) as such ethylene oxide production facilities were considered by us as supplementary to Yongming Petrochemical's surfactant production projects. However, our PRC Legal Advisers have advised that such construction did not comply with the then applicable laws and regulations of the PRC because Yongming Petrochemical did not seek separate approval for the construction of the ethylene oxide facilities. In February 2010, Yongming Petrochemical obtained an approval from Jiaying Economic and Trade Commission (嘉興市經濟貿易委員會) pursuant to which the authority approved Yongming Petrochemical's application for increasing its designed annual production capacity of ethylene oxide

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from 120,000 MT to 220,000 MT. As advised by our PRC Legal Advisers, Jiaxing Economic and Trade Commission is the proper authority to approve such application, such approval is legal and valid and ratifies the construction of Yongming Petrochemical's ethylene oxide production facilities prior to the issuance of such approval. As such, our PRC Legal Advisers are of the view that Yongming Petrochemical has complied with all statutory approval procedures for its ethylene oxide project with a designed annual production capacity of 220,000 MT.

Among our current designed annual production capacity of 120,000 MT of ethylene oxide, the annual capacity of Sanjiang Chemical is 60,000 MT while the annual capacity of Yongming Petrochemical is 60,000 MT.

Sanjiang Chemical was granted an approval for its ethylene oxide production project with an annual capacity of 60,000 MT in 2003. The Industrial Restructuring Catalogue, the Production Licence Notice and the Land Catalogue came into effect on 2 December 2005, 9 November 2006 and 12 December 2006 respectively, and have no retrospective effect to the said project which was in conformity with the then effective laws and regulations of the PRC. As mentioned above, Sanjiang Chemical subsequently obtained the National Production Licence for Industrial Products and a certificate issued by Zhejiang Quality and Technical Supervision Bureau confirming the validity of its production prior to the issuance of National Production Licence for Industrial Products in 2008.

Yongming Petrochemical's ethylene oxide production project with an annual capacity of 60,000 MT is the first phase of its ethylene oxide production project with a total annual capacity of 220,000 MT which was approved by the local government in 2010. The ethylene oxide production expansion project with respect to the increase of Yongming Petrochemical's annual production capacity by 160,000 MT (being 60,000 MT and 100,000 MT respectively) are the second and third phases of the aforementioned project with a total annual capacity of 220,000 MT. As such, our PRC Legal Advisers have advised that Yongming Petrochemical's production expansion plan to increase its annual production capacity of ethylene oxide by 160,000 MT will not be banned by the PRC government. Since the said 220,000 MT project meets the requirements of the current laws and regulations of the PRC, as mentioned above, Yongming Petrochemical obtained the National Production Licence for Industrial Products and two certificates issued by Jiaxing Quality and Technical Supervision Bureau and the Quality and Technical Supervision Bureau of Jiaxing Port Economic Development Zone confirming the validity of its production prior to the issuance of National Production Licence for Industrial Products in 2010.

Currently, only Sanjiang Chemical and Yongming Petrochemical of our Group are engaged in the manufacture of ethylene oxide. Our PRC Legal Advisers have further advised that, assuming Sanjiang Chemical and Yongming Petrochemical would like to expand the annual production capacity of ethylene oxide in the future, Sanjiang Chemical would need to increase its annual production capacity by a minimum of 140,000 MT to 200,000 MT in order to comply with the current laws and regulations applicable to us, while Yongming Petrochemical would be permitted to expand beyond its currently approved annual production capacity of 220,000 MT. However, if Sanjiang Chemical and Yongming Petrochemical would like to construct new ethylene oxide production facilities in other new locations, such expansion must reach a minimum annual production capacity of 200,000 MT in order to obtain the relevant approval from the government authorities.

Save as disclosed above and in other paragraphs of this prospectus, our PRC Legal Advisers have advised that we are in compliance with all applicable laws and regulations of the PRC in all material respects, and have obtained all relevant and necessary licences, permits, certificates and approvals required for our business operation from the proper issuing authorities.

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We have adopted relevant procedures to ensure the compliance with the applicable laws and regulations of the PRC. Mr. Zhang Gui, the head of the administration department of our Company has been appointed as head of legal and compliance for a term of one year since July 2010 to handle all legal and compliance matters of our Group. Such appointment will be renewed automatically upon expiry. In addition, we have appointed PRC legal advisers to advise us on legal and compliance matters in relation to our Group's operation. We have adopted a compliance procedure manual to standardise all the legal and compliance internal control procedures. Mr. Zhang will be responsible for timely updating the manual when there is any change in laws and regulations applicable to our Group.

### CERTIFICATES AND AWARDS

As of the Latest Practicable Date, we had obtained a number of certificates and awards including the following which our Directors consider are the more important ones.

Awards	Awarded by	Award month and year
十強企業 (Top Ten Enterprises)	中共嘉興市委 (The Communist Party of China Jiaxing Municipal Party Committee) and 嘉興市人民政府 (Jiaxing Municipal People's Government)	February 2008
ISO9001 Quality Management System Certification Certificate	Beijing United Intelligence Certification Co., Ltd.	June 2008
ISO14001:24 Environmental Management Systems Certification Certificate	Beijing United Intelligence Certification Co., Ltd.	July 2008
嘉興市高新技術企業 (Jiaxing City High and New Technology Enterprise)	嘉興市人民政府 (Jiaxing Municipal People's Government)	November 2008
十佳工業企業 (Top Ten Industrial Enterprises)	中共嘉興市委嘉興港區開發建設管理委員會 (The Communist Party of China Jiaxing Municipal Party Committee Jiaxing Port Economic Development Zone Working Committee of Development and Construction) and 嘉興港區開發建設管理委員會 (Jiaxing Port Economic Development Zone Management Committee of Development and Construction)	February 2009



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Awards	Awarded by	Award month and year
安全生產先進集體 (Advanced Production Safety Group)	嘉興港區安全生產工作委員會 (Jiaxing Port Economic Development Zone Working Committee of Production Safety)	February 2009
十強納稅企業 (Top Ten Tax Paying Enterprises)	中共嘉興市委嘉興港區開發建設管理委員會 (The Communist Party of China Jiaxing Municipal Party Committee Jiaxing Port Economic Development Zone Working Committee of Development and Construction) and 嘉興港區開發建設管理委員會 (Jiaxing Port Economic Development Zone Management Committee of Development and Construction)	February 2009
十強生產性投入企業 (Top Ten Production Input Enterprises)	中共嘉興市委嘉興港區開發建設管理委員會 (The Communist Party of China Jiaxing Municipal Party Committee Jiaxing Port Economic Development Zone Working Committee of Development and Construction) and 嘉興港區開發建設管理委員會 (Jiaxing Port Economic Development Zone Management Committee of Development and Construction)	February 2009
浙江省科技型中小企業證書 (Zhejiang Province Technology Medium/Small Sized Enterprise)	浙江省科學技術廳 (Science and Technology Department of Zhejiang Province)	October 2009
十強納稅企業 (Top Ten Tax Paying Enterprise)	中共嘉興市委嘉興港區開發建設管理委員會 (The Communist Party of China Jiaxing Municipal Party Committee Jiaxing Port Economic Development Zone Working Committee of Development and Construction) and 嘉興港區開發建設管理委員會 (Jiaxing Port Economic Development Zone Management Committee of Development and Construction)	March 2010

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Awards	Awarded by	Award month and year
十佳工業企業 (Top Ten Industrial Enterprise)	中共嘉興市委嘉興港區開發建設管理委員會 (The Communist Party of China Jiaxing Municipal Party Committee Jiaxing Port Economic Development Zone Working Committee of Development and Construction) and 嘉興港區開發建設管理委員會 (Jiaxing Port Economic Development Zone Management Committee of Development and Construction)	March 2010

### COMPETITION

According to the SAI Report, the domestic ethylene oxide supply market currently consists of several state-owned and privately-owned corporations, including China Petroleum and Chemical Corporation (also known as Sinopec) and China National Petroleum Corporation (also known as CNPC). As at 30 April 2010, the domestic ethylene oxide supply market was largely dominated by the two aforementioned state-owned suppliers. Our Directors consider that with respect to our production of ethylene oxide, we face competition from these two large-scale state-owned petrochemical companies in terms of cost effectiveness, product pricing and production scale. However, due to the flammable and explosive nature of ethylene oxide in both its gaseous and liquid forms and hence a relatively high cost of transportation, delivery of ethylene oxide has its geographical limitation. Our Directors consider that there is limited competition from the two large-scale state-owned petrochemical companies as, so far as the Directors are aware, a majority part of the ethylene oxide produced by these two state-owned petrochemical companies is utilised in-house for further processing in downstream products such as ethylene glycol. The Directors also consider that privately-owned ethylene oxide or surfactant manufacturing petrochemical companies do not pose significant threat to our business as we have significant size advantage over these privately-owned competitors.

With respect to the minimum production capacity requirement of 200,000 MT per annum for ethylene oxide set out in the Industrial Restructuring Catalogue, the Production Licence Notice and the Land Catalogue (the “**Ethylene Oxide Rules**”), such requirement only applies to newly established production facilities after the implementation of the Ethylene Oxide Rules between 2005 and 2006 without any retrospective effect. Therefore, ethylene oxide production facilities which existed before the implementation of the Ethylene Oxide Rules are not affected by such requirement. As such, the implementation of the Ethylene Oxide Rules should not lead to any consolidation among existing small-scale manufacturers that will change the competitive landscape of the industry. Besides, according to the SAI Report, save for Sinopec, CNPC and us, there are currently only two other ethylene oxide manufacturers in the PRC with a designed annual production capacity of 20,000 MT and 10,000 MT respectively. Given the small scale production capacity of these manufacturers, even if there is consolidation between them or a buyout by larger scale manufacturers, either voluntarily or by way of future governmental directives to phase out small-scale manufacturers, the competition amongst the existing competitors in the market will not be intensified. In view of the aforesaid, our Directors believe that the risk of potential consolidation and future significant change in competitive landscape in the short term is very remote.

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According to the SAI Report, in 2009, the domestic AEO surfactant supply market in China was dominated by 20 domestic suppliers, with their products accounting for an aggregate of 78% of the total domestic supply. The remaining 22% was mainly supplied by small surfactants producers that manufacture AEO surfactants in very low quantities. Our Directors consider that with respect to our production of surfactants, we compete with our competitors in terms of product and service quality, production efficiency, cost effectiveness, responsiveness to customers' requirements and market trends.

Our Directors believe that we have competitive strengths as set forth in the paragraph headed "Competitive strengths" above that enable us to compete with our industry participants and to continue our business expansion.

## ENVIRONMENT

### **Relevant environmental laws and regulations governing our business and operation**

As advised by our PRC Legal Advisers, our business and operation are governed by the following relevant environmental laws and regulations over the past years:

The Environmental Protection Law of the PRC (《中華人民共和國環境保護法》) (the "**Environmental Protection Law**"), which was promulgated by the SCNPC and came into effect on 26 December 1989, sets forth the legal framework for environmental protection in China. The Ministry of Environmental Protection (環境保護部) is responsible for overall supervision and administration of nationwide environmental protection work, while local environmental protection authorities at the county level and above are responsible for environmental protection work within their respective jurisdictions.

According to the Environmental Protection Law, an environmental impact report for a construction project assessing the pollution and environmental impact of the construction project, setting forth prevention and treatment measures and having been approved by the relevant environmental protection authorities prior to construction is required. Environmental protection facilities must be simultaneously designed, built and put into operation with the major facilities of those construction projects. Construction projects are not permitted to be put into use until the environmental protection facilities have passed inspections by the environmental protection authorities. Environmental protection facilities installed may not be dismantled or idled without authorisation. Where it is necessary to dismantle or idle such installations, prior approval must be obtained from the environmental protection authorities where such installations are located.

Enterprises engaging in operations that affect environmental conditions are required to adopt certain measures and systems in their operations to effectively prevent and control pollution caused by waste gas, water and solids as well as noise. Enterprises that discharge pollutants must report to and register with the Ministry of Environmental Protection or their local counterparts. Enterprises discharging pollutants shall pay discharge fees in accordance with the applicable regulations.

A person or an enterprise failing to comply with the Environmental Protection Law may be subject to various penalties imposed by the relevant environmental protection authorities, depending on the circumstances of each case and the extent of contamination. Penalties may include warnings, fines, imposition of deadlines for remedying the contamination, orders to suspend production or use, orders to re-install contamination prevention and treatment facilities that have been removed without permission or left unused, orders to close down the enterprises, or orders to compensate any parties affected by the contamination. In case of serious violations, the responsible persons may also be subject to criminal liabilities.

The Regulations on the Administration of Environmental Protection for Construction Project (《建設項目環境保護管理條例》) were promulgated by the State Council and came into effect on 29 November 1998. These regulations are formulated specifically to govern the environmental protection issues that may arise in connection with construction projects that may cause pollution and damage the ecological environment.

The Law of the PRC on the Prevention and Control of Air Pollution (《中華人民共和國大氣污染防治法》) promulgated by the SCNPC on 5 September 1987 with the latest amendment which came into effect on 1 September 2000, the Law of the PRC on the Prevention and Control of Water Pollution (《中華人民共和國水污染防治法》) promulgated by the SCNPC on 11 May 1984 with the latest amendment which came into effect on 1 June 2008, the Law of the PRC on the Prevention and Control of Environmental Pollution by Noise (《中華人民共和國環境噪聲污染防治法》) promulgated by the SCNPC on 29 October 1996 and which came into effect on 1 March 1997 and the Law of the PRC on the Prevention and Control of Environmental Pollution by Solid Wastes (《中華人民共和國固體廢物污染環境防治法》) promulgated on 30 October 1995 with the latest amendment which came into effect on 1 April 2005 set out, respectively, the regulations governing the prevention and control of air, water, noise and solid waste pollution in order to protect and improve the environment, safeguard public health and promote economic and social development. In particular, these laws stipulate concrete requirements for prevention and control of air, water, noise and solid waste pollution for a variety of activities, including residential, production and operation activities.

Enterprises failing to comply with the provisions of the laws on the prevention and control of air, water, noise or solid waste pollution may be subject to warnings, fines, suspension of operations and cessation of business, as determined by the relevant environmental protection authorities. Enterprises that cause air, water, noise or solid waste pollution are obligated to eliminate the pollution and are required to compensate the parties directly affected by the pollution for their losses. Criminal liabilities may also be imposed on the responsible persons for serious violations.

### **Environmental protection measures and pollution controls**

Our Directors have recognised the global trend of growing awareness of environmental protection in terms of both government regulations and customer preference. We consider ourselves a “green” manufacturing company and place strong emphasis on environmental protection. We have made substantial investments to adopt environmental protection measures and pollution controls against carbon dioxide, waste water and solid waste produced in the course of our production process. We have maintained production technologies and process-integrated environmental protection measures by adopting an environmental management system to reduce the impact of pollutant emissions on the environment. We have attained the ISO14001:2004 Environment Management Systems Certification Certificate issued by Beijing United Intelligence Certification Co., Ltd. We have 14 designated personnel

for our production plants who are responsible for, among others, formulating and implementing our environmental measures. Mr. Niu Yingshan, one of our executive Directors, is responsible for the management of environmental protection of our Group. From February 2009 to January 2010, Mr. Niu was appointed by Jiaying Environmental Protection Bureau (嘉興市環境保護局) as an expert of Jiaying Environmental Protection Expert Service Group. We believe that we are equipped with the necessary experience and resources to comply with the increasingly stringent environmental protection requirements. Our Directors believe that such environmental protection measures and controls have by far exceeded the requirements of the relevant PRC environmental protection laws and regulations. Brief details of our environmental protection measures and controls are set forth below:

**A. Carbon dioxide**

Carbon dioxide is generated during the production process of ethylene oxide. We have installed two sets of carbon dioxide recollecting device which have the capacity to absorb approximately 30,000 MT and 20,000 MT of carbon dioxide per year respectively in our Jiaying Production Plant. The carbon dioxide absorbed is then sold for recycling purpose.

**B. Waste water**

We have installed water treatment facilities at our Jiaying Production Plant and Xiaoshan Production Plant respectively which have the respective capacities of treating 2,000 MT and 1,300 MT of waste water per day to treat all waste water generated during the production process of our products. Such treated waste water is recycled and used for cooling of reactants in the production of both ethylene oxide and surfactants.

**C. Solid waste**

Solid catalyst waste produced during our production process is collected by us and sold for recycling purpose.

In light of the aforesaid environmental protection measures and controls taken by our Group, our Directors believe that the environment is not adversely affected as a result of our operation. During the Track Record Period, our annual expenditure in respect of environmental matters were approximately RMB1.6 million, RMB0.6 million, RMB8.7 million and RMB0.1 million respectively. The significant increase in environmental costs in 2009 as compared with those in 2008 was mainly attributable to our investment in the installation of the abovementioned water treatment facilities of approximately RMB7.6 million at our Jiaying Production Plant and other auxiliary facilities and related staff trainings. We estimate that RMB1.3 million will be expended as environmental costs for the full maintenance of our production facilities in 2010 and RMB3.2 million will be expended for our third phase of the ethylene oxide production project to be completed in 2011.

Our PRC Legal Advisers have advised that the only licence or permit in relation to the environmental matters applicable to us is the Pollutant Discharge Licence (排污許可證). At our Jiaying Production Plant, as the relevant local authority in Jiaying, Zhejiang Province of the PRC is in the process of establishing the system for the issuance of the Pollutant Discharge Licences to the companies located in the Jiaying Port Economic Development Zone, Sanjiang Chemical and Yongming Petrochemical have not obtained the Pollutant Discharge Licences as of the Latest Practicable Date. However, Sanjiang Chemical and Yongming Petrochemical can still discharge the waste water into the governmental water

## **BUSINESS**

treatment centre as previously agreed. As advised by our PRC Legal Advisers, there is no legal impediment for Sanjiang Chemical and Yongming Petrochemical to obtain the Pollutant Discharge Licence. At our Xiaoshan Production Plant, Hangzhou Haoming ceased its production of surfactants and other products which were in direct competition with us, after Hangzhou Sanjiang acquired Hangzhou Haoming's ethylene oxide trading and surfactant manufacture and sale businesses in April 2010. Upon completion of the acquisition, Hangzhou Sanjiang prepared for the transfer of the Pollutant Discharge Licence from Hangzhou Haoming and obtained the licence in July 2010. As advised by our PRC Legal Advisers, such licence is legal and valid and so far as our PRC Legal Advisers are aware, there is no legal impediment for renewal of such licence.

Save as disclosed above, we have fully complied with the relevant PRC environmental protection laws and regulations since our commencement of operation. We have been subject to the inspections by the local governmental authority from time to time. Up to the Latest Practicable Date, we were not subject to any material fine or claim arising from non-compliance with environmental laws and regulations or any citation for our environmental measures. We are committed to the continued compliance with the relevant PRC environmental protection laws and regulations.

### **INSURANCE**

We maintain insurance policies for all of our properties, manufacturing facilities, plant and machinery, equipment and inventories against damage caused by accidents. We also maintain insurance policies for our employees, including pension insurance, medical insurance, unemployment insurance, work-related injury insurance and maternity insurance.

Taking into account (i) we have adopted stringent safety precaution measures and has fully complied with the relevant rules and regulations in the PRC; and (ii) there had not been any major work accidents causing material health or safety issues since the establishment of each of the members of our Group, our Directors are of the view that we have maintained sufficient insurance coverage for our current operations based on their knowledge of the industry practice and experience.

During the Track Record Period and up to the Latest Practicable Date, we had not received any product liability claims.

### **INTELLECTUAL PROPERTY**

As of the Latest Practicable Date, we had not applied for any patent in respect of our production know-how.

We have applied for registration of a number of trademarks in the PRC and Hong Kong. Please refer to the section headed "Further information about the business of the Company – Intellectual property rights of the Group" in Appendix VII to this prospectus.

## **LEGAL COMPLIANCE AND PROCEEDINGS**

We have established and maintained a legal compliance procedure for the purpose of ensuring that, among other things, our activities are in compliance with the applicable PRC laws and regulations promulgated by the State, Provincial, Municipal governments and our employees are aware of their legal responsibilities.

We set out below the non-compliances and irregularities relating to our operations during the Track Record Period:

- (1) We failed to fully contribute the social insurance and housing fund for our employees during the Track Record Period. We estimate that the aggregate unpaid amounts by our Group to the social insurance and housing fund authorities were approximately RMB1.7 million, RMB2.4 million, RMB3.0 million and RMB1.0 million, respectively during the Track Record Period and relevant provisions have been made in our Group's consolidated accounts. In hope to settle the outstanding social insurance and housing fund contributions, we and our PRC Legal Advisers have consulted the local social insurance and housing fund authorities in Jiaxing, Zhejiang Province of the PRC respectively. Our PRC Legal Advisers have advised, based on such consultation, that the social insurance authority would not accept our payments for the outstanding social insurance contributions, and the housing fund authority would only accept our payments of RMB6,433 for the outstanding housing fund contributions. We have therefore paid the sum of RMB6,433 in full to the housing fund authority in July 2010. Based on the above, our PRC Legal Advisers are of the view that the risk of the relevant authorities imposing any penalty on our Group is very remote. Our PRC Legal Advisers have however advised that in case an employee of our Group succeeds in labour dispute against us with respect to the outstanding social insurance and housing fund contributions, we may still be required to make such outstanding contributions to such employee, the maximum amount of which was estimated to be RMB8.1 million in aggregate as of 30 April 2010. Nonetheless, our controlling shareholders have agreed to indemnify our Group against any payment obligations or penalties imposed by any relevant authorities in relation to the non-compliance with the employee welfare contribution regulations.

Please refer to the subsection headed "Employees" in this section of the prospectus for further details.

- (2) As of the Latest Practicable Date, we did not possess the building ownership certificates for five properties with a total gross floor area of approximately 600 square metres. As the aggregate area of the five properties represents approximately 1.85% of the total area of properties our Group occupies and these five ancillary properties are not production related, our Directors consider that the lack of building ownership certificates in respect of the aforesaid properties are not crucial to us and will not have a material impact on our operation. We will demolish the five properties if ordered by the relevant government authorities. The demolishing costs are estimated to be approximately RMB50,000, which, our Directors consider, would have insignificant impact on our financial position. It is not our current intention to relocate to other properties after the demolition.

Please refer to the subsection headed "Production capacities, production plant and storage facility – Jiaxing production plant" in this section of the prospectus for further details.

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- (3) Sanjiang Chemical and Yongming Petrochemical commenced their production of ethylene oxide prior to obtaining the National Production Licence for Industrial Products, and obtained the said production licences in June 2008 and April 2010 respectively. According to the certificates subsequently issued by the relevant government authorities, the authorities confirmed the validity of production of Sanjiang Chemical and Yongming Petrochemical prior to the issuance of the National Production Licence for Industrial Products. As such, our PRC Legal Advisers have advised that no penalty will be imposed on our Group by the relevant authorities.

Please refer to the subsection headed “Licences and permits” in this section of the prospectus for further details.

- (4) During the Track Record Period, Yongming Petrochemical leased some of its office premises to Sanjiang Trading, Guanlang and Sanjiang Honam for office use respectively. Hangzhou Haoming leased some of its production premises to Hangzhou Sanjiang for production use. The lease agreements for the aforesaid leases have not been registered with the relevant authorities. Our PRC Legal Advisers have advised that the non-registration of the lease agreements does not affect the validity of the lease agreements. However, Yongming Petrochemical and Hangzhou Haoming, as the lessors, may be subject to a fine for non-registration of the lease agreements.
- (5) During the Track Record Period, we made advances to some Independent Third Parties out of our commercial considerations having regard to the risks of non-recoverability and interest earned. Some advances were interest-bearing whereas some were interest-free. Our PRC Legal Advisers have advised that the advances to Independent Third Parties did not comply with the relevant PRC laws and regulations. As a result, the principal amount of the advances should be returned to the lender and the interest earned (if any) could be confiscated by the relevant authority. In addition, a fine equivalent to one to five times of the interest earned (if any) may be imposed on the lender. Based on the interest earned from the advances made to Independent Third Parties, the maximum penalty for our Group would be approximately RMB24 million. Our controlling shareholders have agreed to indemnify our Group against any payment obligations or penalties imposed by any relevant authorities in relation to such advances made to Independent Third Parties. As the advances to Independent Third Parties have been fully settled as at 30 April 2010 and our Group will not make advances to Independent Third Parties in the future, our PRC Legal Advisers have advised that the risk of the relevant authority imposing penalty on our Group will be very remote.

Please refer to the section headed “Financial information – Analysis of financial positions – Prepayments, deposits and other receivables” in this prospectus for further details.



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We have adopted relevant procedures to ensure the compliance with the applicable laws and regulations of the PRC. Mr. Zhang Gui, the head of the administration department of our Company has been appointed as head of legal and compliance for a term of one year since July 2010 to handle all legal and compliance matters of our Group. Such appointment will be renewed automatically upon expiry. In addition, we have appointed PRC legal advisers to advise us on legal and compliance matters in relation to our Group's operation. We have adopted a compliance procedure manual to standardise all the legal and compliance internal control procedures. Mr. Zhang will be responsible for timely updating the manual when there is any change in laws and regulations applicable to our Group.

As of the Latest Practicable Date, we were not involved in any material litigation, arbitration or administrative proceedings that could have a material adverse effect on our financial condition or results of operations.