OVERVIEW

Our business

We are one of the leading suppliers of HVAC systems for SUVs, pickup trucks and heavy trucks in terms of sales volume in 2011 in China. We principally engage in the development, production and sales of automotive HVAC systems and a range of automotive HVAC components. Our automotive HVAC systems represented approximately 94.5%, 95.7% and 90.4% respectively, of our total turnover for the Track Record Period. Our automotive HVAC systems are mainly used in SUVs, pickup trucks and heavy trucks. According to the Timer Auto Report, in terms of sales volume, we were the fifth largest supplier of automotive HVAC systems (with the market share of 9.9%) for SUVs and pickup trucks and the largest supplier of automotive HVAC systems (with the market share of 19.1%) for heavy trucks in China in 2011. According to the same report, we are the ninth largest automotive HVAC systems supplier in terms of sales volume in the overall automotive HVAC system market in the PRC with a market share of 2.8% in 2011. We also supply HVAC systems and HVAC components for construction machineries and other types of vehicles such as light trucks, sedans and buses.

Our production bases

Currently, we have two production bases. One is located at Jiangning District, Nanjing, Jiangsu, for the manufacture of HVAC systems and HVAC components (including evaporators, condensers, heater cores, HVAC hoses, HVAC housings, radiators, intercoolers and oil coolers). The other production base is located at Fushun Economic Development Zone, Fushun, Liaoning, for the manufacture of HVAC systems (without installing the compressors). We have an annual production capacity of 567,984 units of HVAC systems and 114,972 pieces of HVAC components in aggregate as at 31 December 2011. In order to further enhance our service to our customers and improve our competitive strengths, we have also acquired the land use right of a parcel of land at Daxing District, Beijing with a total site area of 45,178.23 sq.m. and plan to build our third production base.

Our products

According to the Timer Auto Report, driven by the growth of China's automotive market and rising penetrating rate of HVAC systems in automobile, the sales of automotive HVAC systems has grown rapidly over the past few years. As an integral part of an automotive, the primary function of a HVAC system is to maintain the temperature level of the vehicle for the comfort of its occupants. Automotive HVAC systems are assembled from different automotive HVAC components, such as, evaporators, condensers, heater cores, compressors, HVAC hoses, radiators, intercooler, oil cooler, receiver drier, expansion valve and HVAC control units. We primarily develop, manufacture and sell automotive HVAC systems and components (such as evaporators, condensers, heater cores and HVAC hoses). For manufacturing of our HVAC systems, we also source some other HVAC components from other suppliers (such as compressors, receiver driers, expansion valves and HVAC control units).

Our research and development

As the technical specifications and requirements of an automotive HVAC system differs depending on the model of vehicle which the HVAC system is to be used, automotive HVAC systems have to be designed, developed and manufactured based on the technical requirements and specifications of each different model of vehicles. In order to succeed in this industry, we place emphasis on strengthening our research and development capabilities. Our research and development team has a proven record of research and development capabilities and experience on automotive HVAC systems as well as related production techniques. We have 9 registered patents and have applied for registration of 6 other patents as at the Latest Practicable Date. In 2009, we have been accredited with the title 高新技術企業 (High and New Technology Enterprise*). To further strengthen our research and development capabilities, we are in the course of constructing a research and development building with a gross floor area of 15,631.00 sq.m. in the Jiangning Plant. We have purchased the environment simulation laboratory equipment, which is expected to put into use at the end of 2012. For information on our research and development capabilities, please refer to the paragraph titled "Our competitive strengths — Strong research and development capabilities and ability to offer customised products to customers" and "Our Strategies — Strengthening our research and development capabilities and developing HVAC system for electric vehicles" in this section of this prospectus.

Our customers

We offer automotive HVAC systems to automakers in China such as Foton, Hawtai Motor, Shuguang Automotive, Zhongxing Auto, Great Wall and Sinotruk. We also offer automotive HVAC components to automakers and other automotive HVAC system and component suppliers in China. Our products are mainly used in SUVs, pickup trucks and heavy trucks. The major customers of our HVAC systems for SUVs, pickup trucks and heavy trucks include, Foton, Shuguang Automotive, Hawtai Motor, and Sinotruk, which we have approximately 9 years, 9 years, 6 years and 9 years of business relationship, respectively. According to the Timer Auto Report, Foton and Sinotruk are two leading domestic heavy trucks manufacturers. In addition to strengthening our leading position in the automotive HVAC systems for SUVs, pickup trucks and heavy trucks market in China, we are also actively developing our presence in the automotive HVAC systems for construction machineries and other types of vehicles, such as sedans. One of our operating subsidiaries, Xiezhong Nanjing, has been recognised as an "Excellent Supplier" by certain customers, such as Foton, Hawtai Motor, Zhongxing Auto and SANY.

Our recognitions

Our HVAC systems and HVAC components are marketed under our own trademark "  " and this trademark has been recognised as a "Nanjing Municipal Well-known Trademark (南京市著名商標)" in 2010 and as a "Jiangsu Province Well-known Trademark (江蘇省著名商標)" in 2011. Our products have been recognised as "Nanjing Famous Brand (南京名牌產品)" by 南京市人民政府 (Nanjing Municipal People's Government*) in 2011.

Other information

For the Track Record Period, turnover attributable to our five largest customers represented approximately 82.5%, 66.5% and 65.2% of our total turnover, respectively. For the same periods, turnover attributable to our largest customer represented approximately 44.7%, 20.4% and 29.2%, respectively, of our total turnover.

For the Track Record Period, turnover attributable to sales of automotive HVAC systems accounted for approximately 94.5%, 95.7% and 90.4% of our total turnover respectively. For the same periods, turnover attributable to sales of automotive HVAC components accounted for approximately 5.5%, 4.3% and 9.6%, respectively, of our total turnover.

During the Track Record Period, all of our revenue was generated from our sales to the PRC domestic market.

OUR COMPETITIVE STRENGTHS

We believe our success to date and potential for future growth are attributable to our competitive strengths which include the following:

Leading position in automotive HVAC systems for SUVs, pickup trucks and heavy trucks market in China with strong brand recognition

We offer automotive HVAC systems mainly for SUVs, pickup trucks and heavy trucks. According to the Timer Auto Report, we are one of the leading suppliers of HVAC systems for SUVs, pickup trucks and heavy trucks in terms of sales volume in 2011 in China. According to the Timer Auto Report, in terms of sales volume, we were the fifth largest supplier (with market share of 9.9%) of automotive HVAC systems for SUVs and pickup trucks and the largest supplier (with market share of 19.1%) of automotive HVAC systems for heavy trucks in China in 2011. According to the same report, we are the ninth largest automotive HVAC systems supplier in terms of sales volume in the overall automotive HVAC system market in the PRC with a market share of 2.8% in 2011. In 2011, our products have been recognised as "Nanjing Famous Brand (南京名牌產品)" by the 南京市人民政府 ("Nanjing Municipal People's Government"). In 2010 and 2011, our trademark "  " have been recognised as "Nanjing Municipal Well-known Trademark" and as Jiangsu Province Well-known Trademark (江蘇省著名商標), respectively. With our leading market position and strong brand recognition established with our customers, we believe we are well-positioned to benefit from future growth in automotive HVAC systems industry in the PRC.

Long established and stable business relationship with our key customers in China

Our Directors believe due to our competitive strengths as set out in this section, we have succeeded in developing a stable and longstanding business relationship with our major customers, such as Foton, Shuguang Automotive, Hawtai Motor and

Sinotruk (amongst which, Foton and Sinotruk are two leading domestic heavy trucks manufacturers according to the Timer Auto Report) which we have approximately 9 years, 9 years, 6 years and 9 years of business relationship with, respectively. One of our operating subsidiary Xiezhong Nanjing has also been recognised as an "Excellent Supplier" by certain customers, such as Foton, Hawtai Motor, Zhongxing Auto and SANY. We believe our established and solid customer base provides us with a competitive advantage compared with other HVAC systems manufactures. For further information, please refer to the paragraph headed "Our Competitive Strengths — Strong research and development capabilities and ability to offer customised products to customers" in this section of this prospectus.

Strong research and development capabilities and ability to offer customised products to customers

We operate in an industry where the products require a high degree of customisation. The technical specifications and requirements of an automotive HVAC system differ depending on the model of vehicle which the HVAC system is to be used. The automotive HVAC systems have to be developed, customised and manufactured based on the technical requirements and specifications of each different model of vehicles. For this reason, we have emphasized the importance of strengthening our research and development capabilities. As at the Latest Practicable Date, our research and development team consists of approximately 117 staffs. Amongst which, 114 staffs have received tertiary education or above. Our research and development team has a proven record of research and development capability on automotive HVAC systems as well as related production techniques. We have 9 registered patents and have applied for registration of 6 other patents as at the Latest Practicable Date. Our research and development projects are mainly conducted in the laboratory at the Jiangning Plant. This laboratory has been recognised by Foton that it has met its capability requirement on key laboratory in July 2010. This laboratory has been accredited ISO/IEC 17025: 2005 which specifies the general requirements for the competence of testing and calibration laboratories by 中國合格評定國家認可委員會 (China National Accreditation Service for Conformity Assessment*) in February 2009 and again in March 2012. To further strength our research and development capabilities, we are in the course of constructing a research and development building with a gross floor area of 15,631.00 sq.m. in the Jiangning Plant. We estimate that the construction of the research and development building will be completed in the end of 2012. We have purchased the environment simulation laboratory equipment for RMB27.8 million, which is expected to put into use at the end of 2012. In 2009, we have been accredited with the title 高新技術企業 (High and New Technology Enterprise*).

We believe that our research and development capabilities have allowed us to timely respond to our customers' new product development requests and meet the specifications and technical requirements of our different customers.

In addition to cooperation with automakers, we have also established cooperating relationship in conducting research and development projects with certain academic institutions (such as Zhejiang University and Nanjing Agricultural University Institute of Technology) and other HVAC components suppliers. As an example, in October 2006, we entered into an agreement with Nanjing Agricultural University Institute of

Technology to improve the efficiency of evaporators used in our HVAC systems under an improvement program. We have subsequently applied the result of this project in our production process which has helped us to reduce the weight of our products.

Stringent quality control

We view product quality of critical importance to our business. Therefore, we place strong emphasis on the quality of our products through the implementation of quality control measures at our production process. We also believe that a good assurance system is a reliable mechanism to ensure the quality of our products, thus increasing our customers' confidence in our products. We conduct quality inspection during various key production processes to monitor the quality of our product. We carry out quality control process during the inspection and testing in accordance with the ISO/TS16949 requirements. We have proven our capability to meet product specifications and quality requirements of our customers. Our Group has been awarded certain quality system certifications. We have also earned numerous recognitions and honourable titles such as "Excellent Supplier" (優秀供應商) and "Top Ten Suppliers" (十佳供應商) from our customers such as Foton, Zhongxing Auto, Hawtai Motor and SANY. For further details of titles awarded to us or our products by customers, please see the paragraph titled "Awards and recognitions" in this section of this prospectus. These certifications, recognitions and titles are important indicators of our success and reflect our commitment to strict quality standards which help us to attract new customers.

Experienced, stable and dedicated key management personnel with significant industry expertise

Our key senior executives, including Mr. Chen Cunyou, our general manager and executive Director, Mr. Ge Hongbing, our executive deputy general manager and executive Director and Mr. Huang Yugang, our vice general manager, have extensive experience in the automotive HVAC systems industry. They have approximately ten years' experience working in our Group and have joined us since the establishment of our first operating subsidiary, Xiezhong Nanjing, in 2002. Our continued success in expanding our business and maintaining our growth is to a large extent attributable to the industry expertise and customer relationships of our management. We believe our experienced and dedicated management team will continue to lead our Group in capturing market opportunities and to develop and implement our business strategies.

OUR STRATEGIES

Our goal is to become a leader in the automotive HVAC systems market in China. We aim to achieve this objective by implementing the following strategies:

Reinforcing our leading market position in the automotive HVAC systems for SUVs, pickup trucks and heavy trucks markets in the PRC and expanding our production capacity to support future sales demand

According to the Timer Auto Report, China's automotive HVAC systems for SUVs, pickup trucks and heavy trucks markets are expected to grow at a CAGR of around 13% from 2011 to 2015. As one of the leading suppliers of automotive HVAC systems for SUVs, pickup trucks and heavy trucks, we believe we will benefit from such market growth. We intend to reinforce our current leading position in the PRC automotive HVAC systems for SUVs, pickup trucks and heavy trucks markets by i) exploring sales opportunities with other automakers which also manufacture SUVs, pickup trucks or heavy trucks and proactively participating in their new product development from the initial design stage; ii) enhancing our new product development capabilities; and iii) improving our product quality. In selecting other automakers which also manufacture SUVs, pickup trucks or heavy trucks which we intend to establish business relationship with, we will strive to look for automakers which have a good market reputation, a leading market position, with steady business growth and a strong financial background. Similar with our existing customers, we intend to proactively participate in product development with new customers from the initial design stage. To solidify our business relationship with these automakers, we may also establish production base close to these automakers. Currently, we are supplying HVAC systems for sedans and pickup trucks to certain sino-foreign joint ventures automakers such as Shenlong Motor and FAW-GM, respectively. We are exploring the market by seeking to sell HVAC systems for SUVs, pickup trucks and heavy trucks to such existing customers as well. We are also actively seeking business opportunities with other similar sino-foreign joint ventures automakers for sales of HVAC systems for SUVs, pick up trucks and heavy trucks.

In order to support our future sales demand, we intend to increase our production capacities. Our production facilities for HVAC systems achieved an average utilisation rate of 81.9%, 80.3% and 80.1% during the Track Record Period, calculated as described in this section under the paragraph titled "Production Facilities and Production Capacities — Production capacity and utilisation rate". For details of our expansion plans, please refer to the paragraph titled "Production Facilities and Production Capacities — Expansion of production plant" in this section of this prospectus.

Expanding our business in sedans and construction machineries HVAC system markets

To diversify our customer base and better leverage our already established presence in China automotive HVAC system and components markets, we are actively developing our business opportunities with sedans and construction machineries manufacturers. We have already supplied HVAC systems or HVAC components for

sedans to our existing customers, such as Foton, GAC Changfeng and Hawtai Motor. In addition to the existing customers, we have developed a number of new sedans manufacturers as our customers such as Shenlong Motor and BAIC Group from 2010. Amongst which, Shenlong Motor is a sino-foreign joint venture automaker. For the Track Record Period, our sales to customers who are construction machinery manufacturers has increased rapidly from approximately RMB10.3 million in 2009 to RMB32.8 million in 2010 and RMB58.0 million in 2011, representing approximately 3.0%, 6.0% and 9.3% of our total turnover, respectively. We have already been recognised as an "Excellent Supplier" by SANY. We will continue to further expand our business in sedan and construction machinery HVAC system markets.

Strengthening our research and development capabilities and developing HVAC system for electric vehicles

We believe our research and development capabilities are one of the key reasons for our success. We will strive to strengthen our research and development capabilities by recruiting more talents, increasing research and development expenditure and expanding our research and development facilities. We are in the course of constructing a research and development building with a gross floor area of 15,631.00 sq.m. in the Jiangning Plant. The construction of the research and development building is expected to be completed in the end of 2012. We have purchased the environment simulation laboratory equipment for RMB27.8 million, which is expected to put into use at the end of 2012. This equipment allows us to test our products under different simulated environmental conditions which can help us to develop the market of HVAC systems for sedans.

We believe that as a result of the growing environmental protection concerns, electric vehicles will become the future trend of the automotive industry. We have commenced research and development of HVAC systems for electric vehicles in 2008 and have started supplying HVAC systems for electric vehicles to Foton in 2010. We have also cooperated with other institutions to develop certain components of HVAC system for electric vehicles.

Maintaining our cost advantages

In order to maintain our long term competitiveness and stable profit margins, we will endeavour to maintain our cost advantages primarily through i) new product research and development; ii) optimising the manufacturing process and efficiency by upgrading our production lines and improving the level of automation; and iii) increasing economies of scale.

We believe that through the above measures, we will be able to efficiently manage our production cost and maintain our profitability.

Expanding our current network of production bases

To further improve our service to our customers, reduce the distribution cost and strengthen our strategic co-operation with our major customers, in addition to our presence in Jiangsu, we intend to strengthen our current presence in Liaoning, Beijing and Hubei. We are also considering establishing new manufacturing base in other regions of China by ourselves or through mergers and acquisitions or joint ventures. As at the Latest Practicable Date, we did not have any specific acquisition target in respect of which we have entered into any legally binding agreement.

PRODUCTS

Our principal products are automotive HVAC systems. We also manufacture HVAC components, including evaporators, condensers, heater cores, radiators, intercoolers, oil coolers, HVAC hoses and HVAC housings.

The following table sets forth the breakdown of our sales turnover by products during the Track Record Period:

Products	Year ended 31 December					
	2009		2010		2011	
	RMB'000	*% of total turnover*	*RMB'000*	*% of total turnover*	*RMB'000*	*% of total turnover*
HVAC systems	327,513	94.5	521,869	95.7	560,576	90.4
HVAC components[(1)]	19,026	5.5	23,633	4.3	59,328	9.6
Total turnover	346,539	100.0	545,502	100.0	619,904	100.0

Notes:

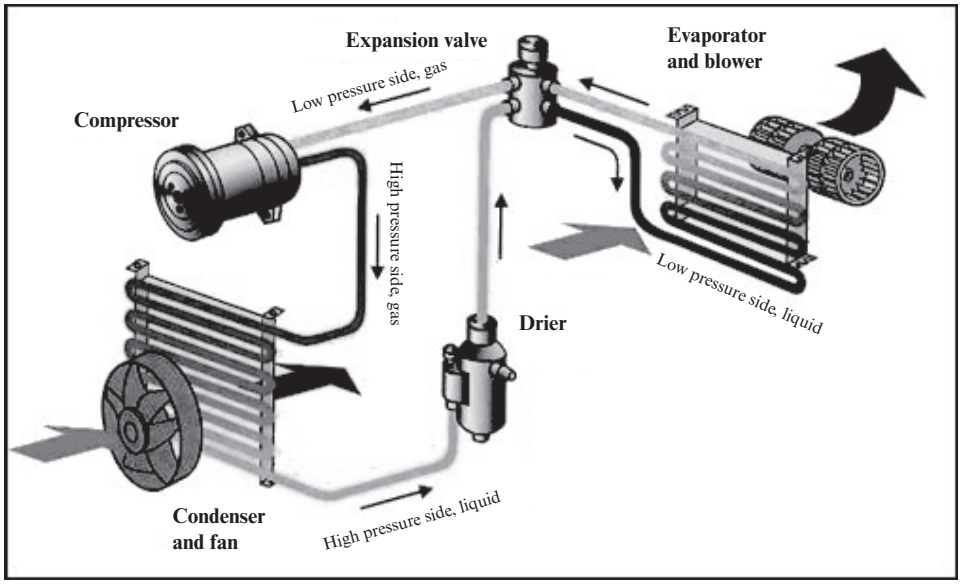
(1) HVAC component mainly comprises of evaporator, condenser and other HVAC components (such as heater core, radiator, intercooler, oil cooler, HVAC hoses and HVAC housing).

HVAC system

The technical specifications and requirements of an automotive HVAC system differ depending on the model of vehicle which the HVAC system is to be used. In order to be compatible and be able to adapt into different layouts of a vehicle's model, automotive HVAC systems have to be designed, developed and manufactured on a made-to-order basis.

Automotive HVAC systems are assembled from different automotive HVAC components, such as, evaporators, condensers, heater cores, compressors, HVAC hoses, HVAC housings, radiators, intercooler, oil cooler, receiver drier, expansion valve and HVAC control units.

The following diagram shows the schematic layout of an automotive HVAC system:



HVAC components

Evaporators

Evaporator is where the refrigerant evaporates from liquid form back into gaseous form. Its primary function is to cool down the interior of the vehicle.

The evaporators used in our HVAC systems are self-manufactured and we manufacture a diversified portfolio of evaporators. Our evaporators include laminated, tube-fin, tube-strip and parallel-flow type evaporators. Laminated and parallel-flow evaporators are currently the major types of our evaporator products used in our HVAC systems.

Condensers

Condenser is a heat exchanger that liquefies the high-pressure vapor discharged from compressor. Condenser consists of a series of tubes surrounded by thin fins which provide a large surface area for heat dissipation.

The condensers used in our HVAC systems are self-manufactured. Our condensers include parallel-flow, tube-fin and tube-strip type condensers with different specifications. Parallel-flow condenser is currently the major type of our condenser products used in our HVAC systems.

Other HVAC components

Heater Cores

Heater core provides warmth to the interior of the vehicle by circulating coolant from the engine, and then air blows through the heater core into the passenger compartment of the vehicle.

The heater cores used in our HVAC systems are self-manufactured. Our heater cores include laminated and parallel-flow type heater cores with different specifications. Parallel-flow heater core is currently the major type of our heater core products used in our HVAC systems.

Radiators, intercoolers and oil coolers

We also produce other automotive heat-exchange devices, such as radiator, intercoolers and oil cooler. Depending on the types of HVAC systems, different heat-exchange devices are used in the HVAC systems. Radiators are used for cooling the engine of a vehicle. Oil coolers and intercoolers are applied as an ancillary part to the vehicle engine to enhance its performance and reliability.

HVAC hoses

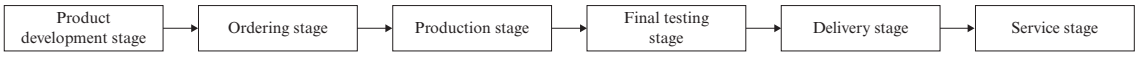
We also produce HVAC hoses. The function of the HVAC hoses is to link various HVAC components in an HVAC system in order to circulate refrigerant within the system.

HVAC housings

We also produce HVAC housings. The function of the HVAC housing is to house different HVAC components for fitting into the vehicle. It directs the air-flow with an HVAC system. Through various air-doors, it controls the direction of air to pass through the heater core or evaporator to achieve heated air or cold air, respectively, depending on the vehicle occupant's setting.

BUSINESS MODEL

The following diagram is a brief illustration of our business model:



Product development stage

As our products are customised for different types of vehicles, we work closely with our customers at the product development stage. Once the product development contract has been signed we will design our product with our customers. After that, we will produce samples of our products to our customers for testing and approval.

Ordering stage

Purchase orders setting out the actual quantity of purchase will be placed with us in accordance with the sales and production plan of our customers from time to time. Production of the products will commence according to the purchase orders placed by our customers.

Production stage

After we receive the purchase orders from our customers, our production planning team will prepare the overall production plan. We will then commence procurement of raw material and HVAC components and commence the production.

Final testing stage

We place great emphasis on the quality and standard of the HVAC systems and HVAC components we produce. We conduct quality inspection during various key production process to monitor the product is up to standard and major faults can be spotted and ratified as soon as possible during the production process. In addition, we conduct final quality control testing on all of our finished goods.

Delivery stage

Our finished products upon passing the quality inspection and testings will be packed and delivered to the location as specified by customers by logistics service providers engaged by us.

Service stage

We will provide technical and after-sales service to our customers during the warranty period.

PRODUCTION FACILITIES AND PRODUCTION CAPACITIES

We currently have two production bases. One of the production bases is located at Jiangning District in Nanjing, Jiangsu with a total site area of 60,133.90 sq.m., while the other is located at Fushun Economic Development Zone, Fushun, Liaoning, the PRC with a total site area of 30,893.00 sq.m.. We have an annual production capacity of 567,984 units of HVAC systems and 114,972 pieces of HVAC components in aggregate as at 31 December 2011. Some of the equipments of our assembly line and moulds of our products were imported from Japan and Korea.

Production capacity and utilisation rate

The following table sets forth the production capacity, the production volume and the average utilisation rate of our production lines for each of our product types during the Track Record Period:

	Year ended 31 December								
	2009			2010			2011		
Products	Production capacity	Actual production volume	Utilisation rate[4]	Production capacity	Actual production volume	Utilisation rate[4]	Production capacity	Actual production volume	Utilisation rate[4]
HVAC system[1]	399,828	327,648	81.9%	507,492[2]	407,738	80.3%	567,984	454,988	80.1%
HVAC components[3]	83,844	51,576	61.5%[5]	84,924	72,011	84.8%	114,972	98,952	86.1%

Notes:

(1) As HVAC system is our primary product, most of our HVAC components produced by us are assembled to produce HVAC system rather than sold as separate HVAC components. Hence, our production capacity and production volume of HVAC components is lower than HVAC systems. Our annual production capacity for HVAC systems as at 31 December 2009, 2010 and 2011 are calculated by multiplying the actual production volume of the highest output month in the relevant year by twelve. The production capacity as set out in the above table is an estimation calculated on the aforesaid basis and hence may not reflect the capacity of our production facilities in reality.

(2) The Fushun Plant commenced operation in April 2010, hence our production capacity contributed by this production base is calculated by multiplying the actual production volume of the highest output month during 2010 by nine (being the nine months period of operation from April 2010 to December 2010).

(3) The production capacity and the production volume of our HVAC components excludes those HVAC components manufactured by us and used to manufacture HVAC systems rather than sold to third parties as HVAC components products. Our annual production capacity for HVAC components as at 31 December 2010 and 2011 are calculated by multiplying the actual production volume of the highest output month in the relevant year by twelve. In 2009, due to exceptional overtime operations, there was an exceptionally high output in one particular month. To avoid distorting the calculation of production capacity by this outlying output record of a particular month, production capacity in 2009 is calculated by multiplying the actual production volume of the second highest monthly output by twelve. The production capacity as set out in the above table is an estimation calculated on the aforesaid basis and hence may not truly reflect the capacity of our production facilities in reality.

(4) The average utilisation rate is derived on the basis of the actual production volume divided by the production capacity during the same period of time.

(5) The utilisation rate of capacity for production of HVAC components for the year ended 31 December 2009 was relatively lower as compared to 2010 and 2011 because there had been a smaller demand for our components products in 2009 as compared to 2010 and 2011.

Expansion of production plant

We intend to leverage our leading position in the automotive HVAC systems for SUV, pickup truck and heavy truck market in China and our product research and development capability to capture further business opportunities. We plan to expand our production capacity to cater for the growing demand from our customers and to realize potential economies of scale.

Nanjing

In order to increase our production capacity in the Jiangning Plant, we plan to upgrade and purchase additional machinery, equipments, moulds and toolings for the Jiangning Plant. With upgraded machinery and additional toolings and moulds, we expect that our production capacity in the Jiangning Plant would increase from about 499,000 units in 2011 to about 700,000 units in 2013. The increase in production capacity in the Jiangning Plant would facilitate us to strengthen capacity for production of HVAC systems for SUVs, pickup trucks and heavy trucks, and to expand the market for HVAC systems for sedans. We estimate that capital expenditure for expansion in the Jiangning Plant would be about RMB90 million. We plan to fund the capital expenditure of RMB90 million partly by the net proceeds of the Share Offer and partly by our internal resources.

We also plan to build a new production plant in Nanjing to manufacture HVAC systems mainly for construction machinery and buses and HVAC components. We intend to acquire land and to commence construction by mid-2013 and complete the whole construction work in 2015. As at the Latest Practicable Date, we have not entered into any legally binding agreement for the acquisition of land. We expect that the New Nanjing Plant would have a designed production capacity of about 150,000 units of HVAC system. We plan to have the New Nanjing Plant to commence operation partially in 2014 and to commence full operation in 2015. We estimate that total capital expenditure for the New Nanjing Plant would be approximately RMB80 million, of which about RMB60 million would be the cost of land and construction; and about RMB20 million would be the cost of machinery and equipment. We plan to fund the capital expenditure of RMB80 million partly by the net proceeds of the Share Offer and partly by our internal resources. When the New Nanjing Plant commence full operation in 2015, we estimate that our total production capacity for production of HVAC system in Nanjing would reach about 850,000 units in 2015.

The New Nanjing Plant is planned with a view to further exploring the market of HVAC systems for construction machineries and buses. During the Track Record Period, our turnover attributable to HVAC systems for construction machineries, buses and other vehicles increased substantially by 4 times in 2010. Our Directors believe that the growth in demand for construction machineries has been driven by infrastructure and construction work being carried out in China in recent years. According to the Timer Auto Report, the PRC Government invested heavily in infrastructure in the past few years, especially in roads

and other related infrastructure. For further details, please refer to the paragraph titled "Key growth drivers — 3. Improving infrastructure" in the "Industry Overview" section of this prospectus. Our Directors also believe that demand for HVAC systems for buses would be steady and stable as bus of various kinds are one of the major transportation used by the general public in the PRC. According to the Timer Auto Report, China's bus market has achieved a CAGR of 11.2% from 2005 to 2011 in terms of sales volume with sales volume reaching approximately 490,000 units in 2011. For further details, please refer to the paragraph titled "China's automotive industry segments — 2. Commercial vehicle market" in the "Industry Overview" section of this prospectus. Currently, a number of our automakers customers also manufacture construction machineries and buses. Riding on our established business relationship with them, we intend to further explore business opportunities with our customers in respect of HVAC systems for construction machineries and buses. Since our existing facilities in Nanjing are mainly used in producing HVAC system for SUVs, pickup trucks, heavy trucks and sedans, and that utilisation rate of our capacity already reached over 80% during the Track Record Period, in light of the increasing demand for HVAC systems for construction machineries, buses and other vehicles, we plan to build the New Nanjing Plant in order to further explore market opportunities in this respect. Based on the historical growth of the construction machineries and bus markets in China, the increase of China's automotive HVAC system penetration rate, and growth of our turnover attributable to HVAC systems for construction machineries, our Directors believe that there will be sufficient customer demand on the Group's products to utilise the New Nanjing Plant.

Currently, we are also in the course of constructing a research and development building with a gross floor area of 15,631.00 sq.m. in the Jiangning Plant. We estimate that the construction of the research and development building will be completed by the end of 2012.

Liaoning

The Fushun Plant was located at a leased property with an aggregated gross floor area of 1,200 sq.m. until September 2012. In June 2011, we completed the acquisition of the land use right of a parcel of land with a total site area of 30,893.00 sq.m. located in Fushun Economic Development Zone, Fushun Liaoning and have constructed the Fushun Plant with an aggregate gross floor area of 5,656.56 sq.m. We commenced production in the Fushun Plant in October 2011. We estimate that capital expenditure for Fushun Plant for the purchase of additional machinery, equipments, moulds, toolings and other fixed assets would be about RMB10 million. We plan to fund the capital expenditure of RMB10 million partly by the net proceeds of the Share Offer and partly by our internal resources. Along with our normal business growth and as we further tap into the northern China market, we expect that the annual production capacity for production of HVAC systems (without installing compressors) of Xiezhong Liaoning will be increased gradually from approximately 68,000 units of HVAC systems in 2011 to approximately 80,000 units of HVAC systems in 2013.

Beijing

We have acquired a parcel of land at Daxing District in Beijing with an aggregated site area of 45,178.23 sq.m. on which we plan to construct the Beijing Plant for the manufacture of HVAC systems. We intend to commence construction of the Beijing Plant in the second half of 2012 and to complete the whole construction work in 2015. We expect that the Beijing Plant would have a designed production capacity of 200,000 units of HVAC systems, and would commence operation partially in 2014 and full operation in 2015. We estimate that total capital expenditure for the Beijing Plant would be approximately RMB90 million and we, as a 50% equity owner of Xiezhong Beijing, would be responsible of about RMB45 million of the capital expenditure, being mainly the cost of machinery and equipments. We plan to fund the capital expenditure partly by net proceeds from the Share Offer and partly by our internal resources.

The Beijing Plant is being built with a view to exploring market for HVAC systems for sedans especially in Hebei, Beijing and cities nearby. According to the Timer Auto Report, China's sedan market has achieved a CAGR of 22.8% from 2005 to 2011 in terms of sales volume with sales volume reaching approximately 10 million units in 2011. For further details, please refer to the paragraph titled "China's automotive industry segments — Passenger vehicle market" in the "Industry Overview" section of this prospectus. We have been supplying HVAC systems to automakers located in Beijing and Hebei for a number of years, and in 2012, we have also started supplying HVAC systems for sedan to certain automakers in northern China. Steady demand from automakers in the area is observed. By establishing the Beijing Plant, we will be able to save delivery cost and sell HVAC systems to automakers in the proximity at a more competitive price. Our Directors also believe that the establishment of the Beijing Plant would facilitate us to strengthen communication with our existing customers in the area and to establish contacts and potential business opportunities with other automakers in the area. Based on the historical growth of the sedans market in China, and couple with our plan to expand our business in sedan HVAC system market as further detailed in the paragraph titled "Our Strategies — Expanding our business in sedans and construction machineries HVAC system markets" in this section our Directors believe that there will be sufficient customers demand on the Group's products to utilise the Beijing Plant. We have entered into technical agreements of products development with BAIC Group for development of HVAC systems for their electric vehicles. We expect that our Beijing Plant will be able to utilise its capacity and handle the orders from BAIC Group when it commences operation.

In addition, we will seek to acquire, invest in, or form joint ventures or strategic alliances with companies which we believe can facilitate our expansion strategy. As at the Latest Practicable Date, we did not have any specific acquisition target in respect of which we have entered into any legally binding agreement.

A summary of capital expenditure/breakdown of application of the net proceeds for the Share Offer for the above expansion plan is set out below:

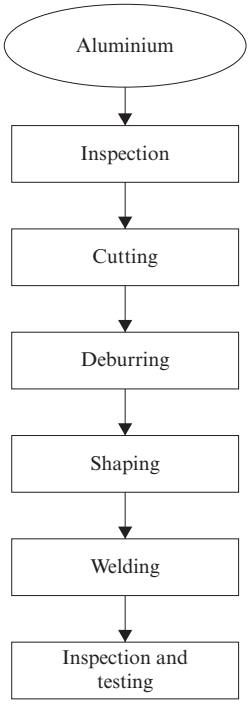
Expansion plan	Expected completion date of the expansion plan	Expected addition in production capacity	Forecast capital expenditure	Source of funding
Upgrading facilities in Jiangning Plant	By the end of 2013	201,000 units of HVAC systems	RMB90 million	As to about RMB52 million from the net proceeds of the Share Offer (or about 32% of the net proceeds) and the balance of about RMB38 million by our internal resources
Building the New Nanjing Plant	By the end of 2015	150,000 units of HVAC systems	RMB80 million	As to about RMB44 million from the net proceeds of the Share Offer (or about 27% of the net proceeds) and the balance of about RMB36 million by our internal resources
Construction and acquiring production facilities for Beijing Plant	By the end of 2015	200,000 units of HVAC systems	RMB45 million	As to about RMB11 million from the net proceeds of the Share Offer (representing about 6.7% of the net proceeds) and the balance of about RMB34 million by our internal resources
Acquiring production facilities for Fushun Plant	By the end of 2013	12,000 units of HVAC systems	RMB10 million	As to about RMB5 million from the net proceeds of the Share Offer (or about 3.3% of the net proceeds) and the balance of about RMB5 million by our internal resources

PRODUCTION PROCESS

Set forth below are the major steps of the production process of our major products:

HVAC components

Our principal HVAC components products are evaporators, condensers and heater cores which undergo similar production process. The followings are the principal production process of evaporators, condensers and heater cores.



1 Inspection — Incoming aluminium raw materials are subject to on-site inspection on a sampling basis and substandard materials will be returned to suppliers.

2 Cutting — Aluminium raw materials are cut and processed to form different production components such as heat dissipation plates, water tanks and pipes. Aluminium wastes are generated as a by-product in the course of cutting of the raw materials.

3 Deburring — In the process of cutting, burrs are created on the aluminium parts which has to be deburred. Additionally, the processed parts are cleaned to remove oil and dirt from their surface before passing to assembly.

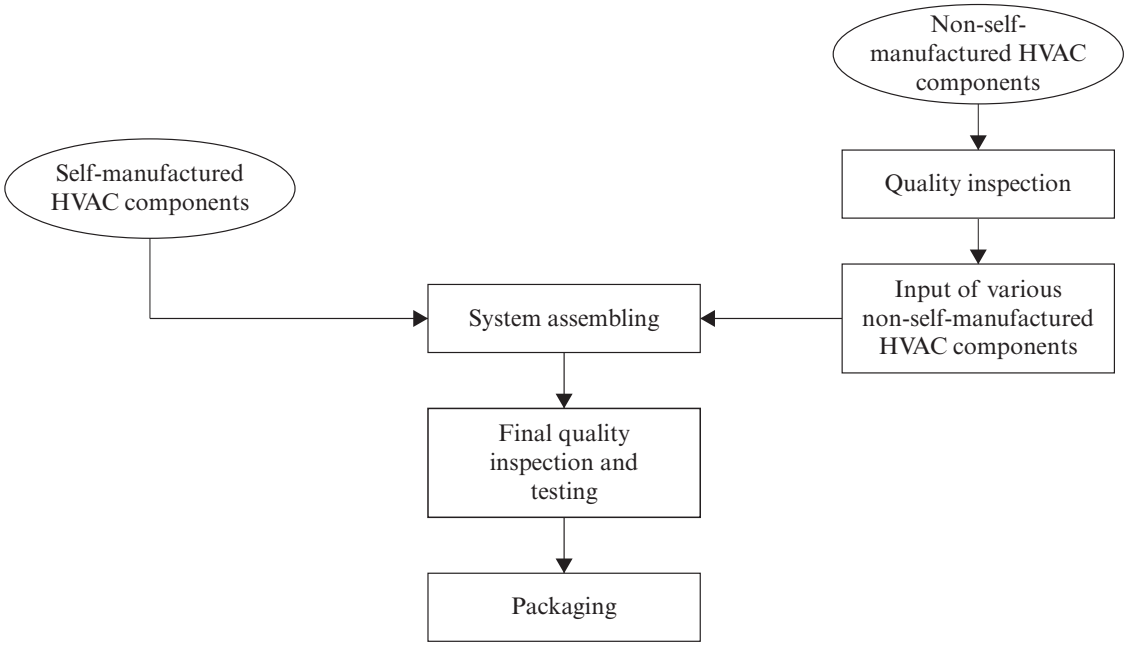
4 Shaping — The processed parts are shaped with our mould in the stamping presses to form the assemble parts. We also carry out inspection at this stage of our production process.

5 Welding — The assembled parts undergo the welding process.

6 Inspection and testing — The finished products are inspected and tested with relevant quality control criteria (e.g. product size, gas-tightness and performance) before sending to our warehouses. The condensers and evaporators are tested for any leakage. Substandard products will be removed and sold as aluminium wastes.

HVAC systems

HVAC system is manufactured by assembling various HVAC components together, which include those HVAC components which are manufactured by us, such as evaporators, condensers, heater cores and HVAC hoses and other HVAC components which are sourced from other HVAC components manufacturers, such as compressors, receiver driers, expansion valves and HVAC control units. The followings are the principal production process of HVAC systems.



1 Inspection of non-self-manufactured HVAC components — HVAC components which are not manufactured by us are inspected before they are used in various steps of the production process of our HVAC systems below.

2 System assembling — HVAC components, which are manufactured by us and other HVAC components which are sourced from other HVAC components manufacturers are assembled together to become a HVAC system.

3 Quality inspection and testing — Quality inspection will take place for the HVAC systems we produce at different key production process so as to spot any defects and conduct ratification as soon as possible. As our final quality control testing, the HVAC systems are tested and inspected for any defects on various aspects, including the performance of the HVAC systems. At the same time, we will carry out process controls during testing in accordance with the ISO/TS16949 requirements.

4 Packaging — If no defects are found, the HVAC systems are packaged.

RAW MATERIALS AND SUPPLIERS

Raw materials

The primary raw materials for our production are aluminium and HVAC components. During the Track Record Period, the total cost of raw materials accounted for approximately 87.9%, 89.7% and 88.5%, respectively, of our total cost of sales.

We mainly purchase our aluminium from suppliers in China and most of our purchases are settled in Renminbi. Instead of having long-term fixed price supply contracts, we place orders with our suppliers according to our monthly procurement plan on a monthly basis pursuant to the framework supply agreements entered into with our suppliers (which normally have a one-year term) according to our annual procurement plan (which is set according to our annual sales plan). As advised by our PRC Legal Advisers, the framework supply agreements between the Group and its major suppliers which are currently being performed and have not expired or been terminated are legally binding and enforceable under the relevant laws and regulations of the PRC. Under certain framework supply agreements for purchase of aluminium, our purchase cost of aluminium raw materials is based on the market price of aluminium at the time of purchase with reference to the Shanghai Futures Exchange (上海期貨交易所) plus a per-unit processing fee which was fixed when the framework supply agreements were entered into. Under the framework supply agreements for purchase of HVAC components, the unit price, warranty period, payment and delivery terms are usually fixed when such agreements were entered into. Generally, we have no obligations to meet any minimum purchases quantity under such framework supply agreements. The quantity of our purchase is usually set when we place the purchase order with our suppliers. Our suppliers bear the transportation costs for delivery to our production facilities. Credit terms generally offered by our major suppliers are around 90 days. Staffs of our procurement department inspect the level of storage of raw material on a weekly basis to ensure that there is no excessive storage of any type of raw material and compile a raw material control list. Orders for raw material will be made with reference to such control list. Once an order for raw material has been placed, staffs of our procurement department will monitor and keep track of the ordered raw materials until they are arrived at our production site.

The price of aluminium is primarily determined by supply and demand of aluminium in the domestic PRC commodity market. During the Track Record Period, the daily weighted average aluminium price as quoted on the Shanghai Futures Exchange (上海期貨交易所) was RMB13,608 per tonne, RMB16,416 per tonne and RMB17,195 per tonne, respectively. We have not adopted any policy to hedge against the fluctuation in aluminium price. We closely monitor movements in the market price of aluminium and will adjust our stock level should we anticipate any significant fluctuation in price or supply. During the Track Record Period, we have not experienced any material disruption in the supply of any of the raw materials required for our production.

To maintain our relationship with our customers, we have not been raising the price of our products due to increase of raw material price during the Track Record Period. To minimise our exposure to fluctuation of raw material price and maintain a stable profit margin, we have implemented the following measures:

1. develop new products with higher profit margins and develop new customers;

2. improve the design of our product to achieve maximum performance at the least cost;

3. improve our production technique to streamline our production process;

4. negotiate with our suppliers and request for discounts on the raw material to be used for older vehicle models;

5. it is our inventory procurement policy to maintain at least two suppliers for each of the raw material to prevent overreliance on any particular supplier and that we are able to source the raw material from the supplier which can offer the lowest price; and

6. our logistic team reviews and monitors our inventory level on a periodical basis to maintain an appropriate level of inventory. We formulate monthly procurement plans to determine the quantity of raw material we purchase in a particular month with reference to our sales plan. This allows us to determine the quantity of raw material we should procure taking into account our sales plan in the forthcoming month, our inventory level, the current price and estimated price trend of such raw material.

For our production of HVAC systems, we also purchase compressors and other automotive HVAC components which we do not manufacture. Amongst which, compressor is the major HVAC component we procure. During the Track Record Period, our costs of sales of compressors were RMB70.7 million, RMB96.4 million and RMB86.5 million, respectively, representing approximately 28.3%, 24.4% and 19.3% of our total cost of sales. Compressors and the HVAC components which we produce are distinct products. The technology requirements and equipment requirements for production of compressors are different from the HVAC components which we produce. In order to manufacture compressors, we would have to recruit new personnel with expertise in the area of compressors manufacturing and acquire new production equipments. This would impose additional capital requirement on us. In addition, as we currently do not possess the experience in sales and manufacturing of compressors, we would be exposed to certain risks if we embark on sales and manufacturing of compressors. As a result, the Group currently does not have any plan to acquire or develop its capability in manufacturing its own compressors in the foreseeable future. According to Timer Auto Consulting, it is the industry practice that the production of compressors and other HVAC components are carried out separately by different manufacturers given that these products are distinct from one and other, and some automakers may also require the HVAC system providers to source the compressors from its designated compressor manufacturers. In this light, the Sponsor is of the view that it is in line with industry practice for the Group to source

compressors from third parties for assembling of its automotive HVAC systems and that it represents a complete business model. During the Track Record Period, we did not encounter any material disruption in the supply of compressors and other automotive HVAC components required for our production.

Pursuant to the framework supply agreements we entered into with our suppliers, our suppliers generally provide a warranty period equal to or more than the warranty period we provide to our customers. It is generally stipulated in the framework supply agreement that if any incident has arisen in the market due to the quality of the product supplied by our suppliers, the suppliers shall send personnel to attend the scene to resolve the matter at our request and be responsible to indemnify our loss. It is also generally stipulated in the framework supply agreements that our suppliers shall be responsible for all economic loss and legal liabilities as a result of products recall due to regulatory non-compliance including potential issue on product safety caused by our suppliers.

Utilities

Electricity, water and nitrogen gas are the principal utilities used in our production process. Our electricity and water are supplied by state-run organisations at market price. Our nitrogen gas is purchased at market price. No long-term supply contract has been entered in respect of utility supply. During the Track Record Period, our utility cost amounted to approximately RMB3.9 million, RMB5.1 million and RMB5.9 million, respectively, representing approximately 1.5%, 1.3% and 1.3% of our total cost of sales. During the Track Record Period, we did not encounter any material disruption in the supply of utilities to our production facilities.

Suppliers

Our suppliers have to go through certain selection process prescribed by us before it can become our supplier of a particular raw material. We take into account factors such as the quality and technology level of the suppliers, the purchase price and the historical dealings with the suppliers in selecting our suppliers. We also conduct evaluation of our suppliers from time to time and eliminate suppliers who fail to meet our standard from our suppliers' list and add in new qualified suppliers. Once they become our suppliers, we conduct regular assessments on our suppliers to ensure that they fulfill our requirements on quality control. In particular, our procurement team would carry out on site evaluations at the premises of our main suppliers, and assess their production capacity, so as to ensure that the production capacity of the respective suppliers are sufficient to meet our Group's production and future development needs, and at the same time maintain the quality of the products and materials from the source of supply.

For the Track Record Period, our five largest suppliers together accounted for approximately 33.4%, 30.4% and 25.6%, respectively, and our largest supplier accounted for approximately 11.0%, 9.7% and 8.0%, respectively, of our total purchase.

The following tables set forth certain information in relation to our five largest suppliers during the Track Record Period.

Five largest suppliers for the year ended 31 December 2011	**Purchase amount** *(RMB'000)*	**Years of relationship**
Supplier A	33,871	7
Supplier B	26,721	7
Supplier C	17,368	9
Supplier D	16,305	1
Supplier E	14,117	8

Five largest suppliers for the year ended 31 December 2010	**Purchase amount** *(RMB'000)*	**Years of relationship**
Supplier A	38,579	7
Supplier B	37,948	9
Supplier E	17,386	8
Supplier C	14,861	9
Supplier F	12,227	5

Five largest suppliers for the year ended 31 December 2009	**Purchase amount** *(RMB'000)*	**Years of relationship**
Supplier A	31,869	7
Supplier B	30,167	9
Supplier C	12,784	9
Supplier E	12,318	8
Supplier F	9,621	5

The number of years of business relationship with our five largest suppliers during the Track Record Period ranged from approximately 1 to 9 years.

As our purchase mainly comprises aluminium and automotive HVAC components, mainly compressors, receiver driers and expansion valves that are not customised products and are readily available in the market, we believe that it would not be difficult for us to find alternative suppliers should existing suppliers cease business relationships with us in the future with no significant impact to our production process. To avoid any disruptions in production, we maintain at least two suppliers for each of the raw materials.

In some cases, our customers would have preference on the type or supplier of the automotive HVAC components to be used in the HVAC systems we supply to these customers. Unless specifically requested by our customers, generally we would recommend to our customers and discuss with our customers which type or supplier of automotive HVAC components we use in our HVAC systems.

When we engage a HVAC components supplier to supply a new HVAC component, we will enter into a technical agreement of products development with our supplier to set out, amongst others, 1) the technical requirements of the HVAC component to be developed; 2) the respective responsibility of our supplier during the development stage of the HVAC component; 3) the ownership of the intellectual properties created during the development of the HVAC component; and 4) the timetable of the development of the HVAC component. Under the technical agreement of products development, we are responsible for providing the technical requirements of the component to be developed, conducting functionality testing and trail assembly on the sample according to the technical requirement and providing feedback to our suppliers. Our suppliers are responsible for compiling the product development timetable for our approval, developing the component according to the technical drawing, sample and other technical information we provided, submitting the sample product and testing report to us and commence trial production upon our notification. Generally, the ownership of intellectual properties created during the products development would belong to us and we do not provide any funding to our suppliers while the product is being developed. Generally, we will pay a certain portion of the cost of the mould of the product to our supplier for its development while the remaining cost of the mould will either be (i) amortised in the subsequent sales of the HVAC components by our supplier to us; or (ii) be payable by us once production volume of such product has reached a certain level; or (iii) be payable by us when the products produced using the mould have passed the relevant quality inspection tests.

During the Track Record Period, 45.1%, 38.0% and 45.7% of the compressors we used in our HVAC systems were sourced from Aotecar Nanjing, a connected person of our Company under the Listing Rules upon Listing. For further details, please refer to the section titled "Connected Transactions" of this prospectus. During the Track Record Period, our purchase from Aotecar Nanjing amounted to RMB31.9 million, RMB38.6 million and RMB33.9 million respectively, which represents 12.8%, 9.8% and 7.6% of the cost of sales for the corresponding year and was our largest supplier during the Track Record Period. Aotecar Nanjing is an indirect wholly-owned subsidiary of China Auto System Technologies Limited (中國汽車系統技術有限公司) which is engaged in investment holding and with its subsidiaries principally engaged in the manufacture and sale of automobile air-conditioning compressors in the PRC.

Save as disclosed above, none of our Directors or their associates or any person who, to the best knowledge of our Directors, owned 5% or more of our issued share capital as at the Latest Practicable Date had any interest in any of our five largest suppliers for the Track Record Period.

SALES AND MARKETING

Our products can be principally divided into two product segments: (1) sales of automotive HVAC systems and (2) sales of automotive HVAC components. For the Track Record Period, we generated 94.5%, 95.7% and 90.4%, respectively, of our turnover from sales of HVAC systems and 5.5%, 4.3% and 9.6%, respectively, of our turnover from sales of HVAC components.

The following table sets out an analysis of our turnover by segments for the Track Record Period:

Products	**Year ended 31 December**					
	2009		**2010**		**2011**	
	RMB'000	*% of total turnover*	*RMB'000*	*% of total turnover*	*RMB'000*	*% of total turnover*
HVAC systems	327,513	94.5	521,869	95.7	560,576	90.4
HVAC components[(1)]	19,026	5.5	23,633	4.3	59,328	9.6
Total turnover	346,539	100.0	545,502	100.0	619,904	100.0

Notes:

(1) HVAC component mainly comprises of evaporator, condensers and other HVAC components (such as heater core, radiator, intercooler, oil cooler, HVAC hoses and HVAC housing).

Our HVAC systems are mainly used by our customers in SUVs, pickup trucks and heavy trucks.

The following table sets out a breakdown of our sales turnover by different types of vehicles for the Track Record Period:

	Year ended 31 December					
	2009		2010		2011	
Types of vehicles	*RMB'000*	*% of total turnover*	*RMB'000*	*% of total turnover*	*RMB'000*	*% of total turnover*
HVAC systems						
SUVs and pickup trucks	181,082	52.2	254,570	46.7	286,572	46.2
Heavy trucks	120,285	34.7	150,222	27.6	126,946	20.5
Construction machineries	10,271	3.0	32,841	6.0	57,959	9.3
Other vehicles[(1)]	15,875	4.6	84,236	15.4	89,099	14.4
HVAC components[(2)]	19,026	5.5	23,633	4.3	59,328	9.6
Total turnover	346,539	100.0	545,502	100.0	619,904	100.0

Notes:

(1) Other vehicles mainly comprised of light trucks, buses, MPVs and sedans.

(2) HVAC components mainly comprise of evaporator, condensers and other HVAC components (such as heater core, radiator, intercooler, oil cooler, HVAC hoses and HVAC housing) for all types of vehicles.

Our automotive HVAC systems are primarily sold to the automakers and construction machinery manufacturers in China such as, Foton, Hawtai Motor, Shuguang Automotive, Zhongxin Auto, Sinotruk and SANY. Our operating subsidiary, Xiezhong Nanjing, has been recognised as an "Excellent Supplier" by certain customers, including Foton, Hawtai Motor, Zhongxin Auto and SANY. Our HVAC systems and HVAC components are marketed under our own trademark "  ". We also sell our automotive HVAC components to automakers and other automotive HVAC systems and components suppliers.

As the technical specifications and requirements of an automotive HVAC system differ depending on the model of vehicle which the HVAC system is to be used, we primarily sell our products according to the specification requirements of our customers. We have been working closely with our customers in developing and producing a wide variety of automotive HVAC systems which are used in different vehicle models. We will continue to develop our products according to our customers' specifications to solidify our position in the HVAC systems market. Meanwhile, we are also exploring potential business opportunities with other automakers. For further details please refer to the paragraph titled "Our strategies" in this section of the prospectus.

We generally obtain sales of our products to our existing customers by way of invitation for product development for new products or direct purchase orders for the existing products; and from new customers by way of tender.

Sales contracts with new customers are usually secured through tender. Our marketing team identifies tenders through market research, invitation by automakers or through referrals. Once we have identified a tender, we will engage in discussion with the automaker

on the preliminary commercial terms and technical requirements of the potential sales. The automaker will send us a "technical package" of the product it wishes to source which will contain information such as, the product requirements (such as the type of vehicles which the product will be used in), the technical requirements of the product, the timetable of the product development, estimated production volume of the product and the product's expected lifespan. Based on the information in the technical package, we will conduct a market analysis and prepare a product design and development proposal which contains the development timetable of the product, the technical and development requirements of the product, the size of the potential market and estimated sales volume for our management to consider whether the potential sales will be beneficial for us. If our analysis suggests that the potential sales will be beneficial for us, we will prepare the tender documents and submit a bid for such sales with our bidding price based on the aforementioned analysis. If we are shortlisted amongst other bidders, representatives of the automaker will carry out onsite assessment on our production facilities. If the automaker is satisfied with the result of the onsite assessment and our bid has been accepted by such automaker, we will sign a technical agreement of products development with the automaker.

In respect of sales of a new products to existing customers, we will obtain information from our customers of the proposed new products and the required product specifications, and prepare the price quotation and the relevant documents for our customers' consideration. If our price quotations are accepted by our customers, we will sign a technical agreement with our customers.

Generally, the purpose of the technical agreement on products development is to set out, amongst others, 1) the technical requirement of the product to be developed; 2) the responsibility of our customer and us during the development stage and production stage of the product; 3) the ownership of the intellectual properties created during products development; and 4) the timetable of the product development. Generally, the ownership of intellectual properties created during products development by us with our customers would belong to our customers. In the development of our products, our customers would usually set out the technical requirements and we would conduct the design and development of the product according to such requirements. During the development of our products, our customers are responsible for providing information of the compartment layout of the vehicle, closely cooperate with us and coordinate resolving any issue during the course of development of the product, ensure the accuracy of the data provided to us, assessing the design proposal and technical data we provided, assessing the functionality and quality of the sample product we provided. Our customers would also participate in the quality assurance and functionality testing process and would assess whether to commence mass production of the product based on our production preparation status. During the approval process before small scale production commences, samples of our product will be produced using the mound of the product developed. The samples functionality will be tested and its appearance and its dimension will be tested against the products technical requirements. Before mass production commences, further assessment will be conducted on the stability of our product's quality and consistency during large scale production and whether our production capacity can satisfy large scale production. During the Track Record Period, approximately 4.4%, 3.5% and 2.4% of our total turnover were from sales to new

customers. These new customers generally required us to go through the above approval processes. During the Track Record Period and up to the Latest Practicable Date, none of our HVAC systems or HVAC components has ever failed to pass the approval process prescribed by automaker. Generally, our customers do not provide any funding to us while the product is being developed. The cost of developing the product incurred by us is generally amortised in the subsequent sales of the product to our customer.

In addition to the product development contract, we will also enter into an annual framework sales agreement with our customer for a term of one year which is renewable on a yearly basis, pursuant to which our customers will normally place monthly orders with us. As advised by our PRC Legal Advisers, the annual framework sales agreements between the Group and its major customers which are currently being performed and have not expired or been terminated are legally binding and enforceable under the relevant laws and regulations of the PRC. The annual framework sales agreements generally set out the planned specification, model, name and unit price of our products and other terms including packing, delivery and payment. For sales under subsequent annual framework sales agreement of such product, the price of our product may change depending on the negotiation between our customers and us while the other terms of the annual framework sales agreements remain mostly unchanged. In some of our annual framework sales agreements, it is a condition that we have obtained ISO/TS 16949:2009 certification. Generally, our customers have no obligations to meet any minimum sales quantity under the annual framework sales agreements. The quantity of our products ordered by our customers will be determined according to the purchase orders placed by our customers.

We have focused on developing customer relationships through direct marketing activities including maintaining regular management visits, providing customer care through our sales representatives and offering after-sales technical support. As part of our after-sales service, during the Track Record Period, we have seconded certain staff members to our major customers' production base to offer onsite technical support.

Customers

We primarily sell automotive HVAC systems and components to automakers and construction machinery manufacturers in China such as Foton, Hawtai Motor, Shuguang Automotive, Zhongxin Auto, Sinotruk and SANY. During the Track Record Period, we had 80, 91 and 113 customers respectively and they were mainly PRC automakers of SUVs, pickup trucks and heavy trucks, as well as other automotive HVAC systems and components suppliers.

During the Track Record Period, we have not entered into any long-term sales agreement with our customers, which we believe is consistent with the market practice.

For the Track Record Period, turnover attributable to our five largest customers represented approximately 82.5%, 66.5% and 65.2% of our total turnover, respectively. For the same periods, turnover attributable to our largest customer represented approximately 44.7%, 20.4% and 29.2%, respectively, of our total turnover.

The following tables set forth certain information in relation to our five largest customers during the Track Record Period:

Five largest customers for the year ended 31 December 2011	**Sales amount** *(RMB'000)*	**Years of relationship**
Customer A	180,910	9
Customer B	73,776	9
Customer C	63,603	4
Customer D	43,118	3
Customer E	42,557	5

Five largest customers for the year ended 31 December 2010	**Sales amount** *(RMB'000)*	**Years of relationship**
Customer A	111,380	9
Customer B	76,561	9
Customer F	60,838	2
Customer C	60,626	4
Customer G	53,285	5

Five largest customers for the year ended 31 December 2009	**Sales amount** *(RMB'000)*	**Years of relationship**
Customer A	154,846	9
Customer G	47,422	5
Customer B	44,419	9
Customer H	20,959	9
Customer I	18,217	9

The number of years of business relationship with our five largest customers during the Track Record Period ranged from approximately 2 to 9 years.

The BAIC Group has become our connected persons under the Listing Rules since January 2011. Foton, being our largest customer, is an associate of BAIC. A breakdown of sales to the BAIC Group during the Track Record Period is set out below:

	For the year ended 31 December		
	2009	**2010**	**2011**
	RMB' million	*RMB' million*	*RMB' million*
Sales to Foton by our Group	154.8	111.4	180.9
Sales to Foton by Xiezhong Beijing before it became our subsidiary in January 2011	—	64.0	12.3
Sales to other associates (as defined under the Listing Rules) of BAIC by our Group	—	—	7.3
Total	154.8	175.4	200.5

Please refer to the section headed "Connected Transactions" in this prospectus for details of our transactions with the BAIC Group.

Save as disclosed above, none of our Directors or their associates or any person who to the knowledge of our Directors owned 5% or more of our issued share capital as at the Latest Practicable Date had any interest in any of our five largest customers for the Track Record Period.

Pricing and credit policy

Our products are not subject to any price control by the PRC Government. We set prices for each type of our products by taking into account the costs of raw materials and other HVAC components, level of complexity of products, market competition and demand and with reference to a reasonable profit margin.

We offer credit to our customers on a case-by-case basis, depending on our relationship with, and the location, credibility and volume of purchases of, each customer and the industry practices and market conditions. We generally offer a credit period of around 90 days to our customers. Most of our sales are denominated in Renminbi and payments are settled by prepayment, notes receivables, or through bank transfers or by bank bills.

Transportation

We generally bear the cost of transporting products to our customers. Except for cases where we need to deliver our products to our customers by our own transportation on an urgent basis, we generally outsource the delivery of our products to third-party logistics providers. These outsourcing arrangements allow us to reduce our capital investment and eliminate the risk of liability to transportation accidents, delivery delays and losses, as our logistics providers will bear these risks. In addition, we also re-evaluate the credentials and

performance of our logistics providers on a periodic basis and terminate those providers with unsatisfactory service. We have established an average of approximately 6 years of business relationships with 2 logistics providers, in order to lower the risk of losses arising from performance failure of these logistics providers.

Branding and recognition

We consider brand awareness and customer loyalty as the key to our future success. Our HVAC systems and HVAC components products are marketed under our own trademark "  " which has be recognised as a "Nanjing Municipal Well-known Trademark (南京市著名商標) in 2010 and as a "Jiangsu Province Well-known Trademark (江蘇省著名商標)" in 2011. Our products have been recognised as "Nanjing Famous Brand (南京市名牌產品)" by the 南京市人民政府 (Nanjing Municipal People's Government*) in 2011. To introduce our products to a broader group of customers and further expand our customer base, we participate in trade shows and exhibitions, including heavy trucks or commercial vehicles related exhibitions and other automobile-related exhibitions in major cities of China. We also organize visits to our production facilities by automakers to market our new products and enhance our brand recognition.

Seasonality

Based on our experience in the automotive HVAC industry, our sales are subject to seasonal fluctuation. As our sales are affected by the sales in the automotive market, our seasonal fluctuation period is similar to the automotive industry's period. Generally, our sales are higher during the months of March to May and October to December of each year while our sales are lower during the months of June to September of each year.

AWARDS AND RECOGNITIONS

Awards/Certification	Time of Granting/ Awarding (validity period, if any)	Granted/Awarded by	Awarded Entity
文明企業 (Civilized Unit*)	2004–2005	南京市江寧區精神文明建設指導委員會 (Jiangning District of Nanjing Spiritual Civilization Development Steering Commission*)	Xiezhong Nanjing
南京市江寧區十佳和諧勞動關係企業 (Top ten harmonious labour relation in Jiangning District of Nanjing*)	2006	江寧區總工會 (Labour Union of Jiangning District*) 江寧區勞動和社會保障局 (Social and Labor Insurance Administration of Jiangning District*) 江寧區中小企業局 (Small and Medium Enterprise Bureau of Jiangning District*) 江寧區企業聯合會、企業家協會 (Joint Association of Enterprises and Entrepreneur Association of Jiangning*)	Xiezhong Nanjing
安全生產先進單位 (Safety production advanced enterprise*)	February 2006, January 2008	南京市江寧區人民政府 (Jiangning District of Nanjing Municipal People's Government*)	Xiezhong Nanjing
先進單位 (Advanced unit)	January 2007	南京市江寧區勞動和社會保障局 (Social and Labor Insurance Administration of Jiangning District, Nanjing)	Xiezhong Nanjing
重合同守信用企業 (Contract trustworthy enterprise of Nanjing*)	2008, 2009, 2010	南京市江寧區人民政府 (Jiangning District of Nanjing Municipal People's Government*)	Xiezhong Nanjing
高新技術企業 (High and new technology enterprise*)	December 2009	江蘇省科學技術廳 (Jiangsu Province Science and Technology Department*) 江蘇省財政廳 (Jiangsu Province Finance Department*) 江蘇省國家稅務局 (Jiangsu State Administration of Taxation*) 江蘇省地方稅務局 (Jiangsu Local Taxation Bureau*)	Xiezhong Nanjing

Awards/Certification	Time of Granting/ Awarding (validity period, if any)	Granted/Awarded by	Awarded Entity
福田汽車重點試驗室分包方能力認可証書 (Subcontractors Capability Certificate of Key Laboratory of Foton*)	28 July 2010 (valid until 27 July 2013)	recognised by 福田汽車節能減排重點試驗室 (Foton's Key Laboratory of Energy Saving*); Examined by 天津華城認証中心 (Tianjin Huacheng Certification Centre*)	Laboratory of Xiezhong Nanjing
南京市著名商標 (Nanjing Municipal Well-known Trademark*)	December 2010 (valid until 2013)	南京市工商行政管理局 (Nanjing Administration for Industry and Commerce*)	Xiezhong Nanjing for the trademark of " "
GB/T24001-2004 idt ISO14001:2004 for production of XZ series automobile air conditioners and its relative environment management activity	5 January 2011 (valid for three years)	北京中潤興認證有限公司 (Beijing ZhongRunXing Certification Co., Ltd.*)	Xiezhong Nanjing
GB/T 28001-2001 for production of XZ series automobile air conditioners and its relative established occupation health and safety management activity	5 January 2011 (valid for three years)	北京中潤興認證有限公司 (Beijing ZhongRunXing Certification Co., Ltd.*)	Xiezhong Nanjing
南京市名牌產品 (Nanjing Famous Brand*)	April 2011 (valid for three years)	南京市人民政府 (Nanjing Municipal People's Government*)	Xiezhong Nanjing
ISO/TS16949:2009 for quality management system applicable to the design and manufacture of air-conditioners	11 July 2011 (valid for three years)	BSI Management Systems (China)	Xiezhong Nanjing
江蘇省著名商標 (Jiangsu Province Well-known Trademark*)	31 December 2011	江蘇省工商行政管理局 (Jiangsu Province Administration for Industry and Commerce*)	Xiezhong Nanjing for the trademark of " "
ISO/IEC 17025: 2005	27 March 2012 (valid for three years)	中國合格評定國家認可委員會 (China National Accreditation Service for Conformity Assessment*)	Xiezhong Nanjing

In addition, our customers have granted us the following honourable titles.

Customers	Honours
Foton	Excellent Supplier in 2007, 2008, 2009 Technology Innovation Awards in 2008, 2009 Concurrent Development Alliance (同步開發聯合體) in 2005
Zhongxing Auto	Excellent Supplier in 2008, 2009, 2011
Changfeng Motor	Excellent Supplier in 2009 Excellent Components Supplier in 2008, 2011
Hawtai Motor	Excellent Supplier in 2010 Top Ten Excellent Supplier in 2009
Hengte Heavy Industry	Excellent Supplier in 2010
GAC Gonow	Top Ten Excellent Supplier in 2009, 2011
Sinotruk	Qualified Supplier in 2009
SANY	Excellent Supplier in 2009, 2010
Shantui	Excellent Supplier in 2011
FAW-GM	Excellent Supplier in 2011
Foday	The Best Supplier for Development for 2008
Mianyang Huarui Auto	Excellent Quality Performance Award (優秀質量表現獎) in 2011

RESEARCH AND DEVELOPMENT

Our research and development team consists of approximately 117 staffs as at the Latest Practicable Date. Amongst which, 114 staffs have received tertiary education or above (with 53 of them are university graduates and 61 of them have received tertiary education). Our research and development team is headed by our executive deputy general manager and executive Director, Mr. Ge Hongbing, who is the executive deputy general manager and chief engineer of Xiezhong Nanjing, and Mr. Huang Yugang who is one of the members of our senior management. Mr. Huang is the deputy general manager and research and development department head of Xiezhong Nanjing and is responsible for overseeing the technical aspect of the research and development of our products. Mr. Ge Hongbing has approximately 17 years of experience in automobile air conditioner industry. Mr. Huang has approximately 21 years of experience in the production technique and production quality control of electrical appliance and automobile air conditioning systems. Our research and development projects are mainly conducted in the laboratory at the Jiangning Plant. This laboratory has been recognised by Foton that it has met its capability requirement on key laboratory in July 2010. This laboratory has been accredited ISO/IEC 17025: 2005 which specifies the general requirements for the competence of testing and calibration laboratories by 中國合格評定國家認可委員會 (China National Accreditation Service for Conformity Assessment*) in February 2009 and again in March 2012. We have purchased the environment simulation laboratory equipment, which is expected to put into use at the end of 2012. Such environment simulation laboratory equipment enables us to evaluate the performance of our HVAC system products when they are installed in different model of vehicles by simulating different environmental conditions, including different temperature and humidity. We have invested RMB27.8 million to purchase such environment simulation laboratory equipment.

We have adopted the following research and development strategies:

(i) to develop our own proprietary technologies by our own research and development team

Our research and development team has a proven record of independent research and development experience on automotive HVAC systems as well as related production techniques. As at the Latest Practicable Date, we had 9 registered patents, 8 of which were developed by our own research and development team and had applied for registration of 6 other patents.

Our registered patents had mainly been applied to improve the functionality, quality and reliability of our products and the efficiency of our production process.

Examples of our registered patents include, amongst others, the followings:

1. one utility model of parallel-flow condenser and one invention of parallel-flow evaporator, both involves fitting plates with holes in the header tube of the condenser and evaporator. These have allowed the refrigerant to flow evenly in the condenser and evaporator which have improved the cooling efficiency of the condenser and heat dissipation ability of the evaporator;

2. an invention of a device which continuously defrost the evaporator so that the compressor do not have to switch on frequently thereby reducing energy consumption and improving reliability of the HVAC system;

3. a utility model of header tube of our parallel-flow evaporator. This utility model involves shaping the header tube of the parallel-flow evaporator from one single piece of raw material which has reduced the risk of leakage and improve the functionality of the evaporator. As the production of such tube is relatively simplier, this utility model has also the benefit of reducing production cost;

4. a utility model of laminated evaporator involves fully utilising the heater exchange's surface area to improve cooling ability of the evaporator; and

5. two designs of the outlook of HVAC control units.

The patents which we have applied for registration include utility models of improvement of design of HVAC system and various components of our products (such as blower unit, electric circuit of HVAC system, heater water tank and HVAC housing). These utility models are designed to improve the functionality and production process of our products. For example, one of the utility models replaces screws with locking clips in assembling the blower units thereby reducing cost of raw material and making the assembly easier so as to reduce the production cost. Other patents which we have applied for registration include design of the outlook of HVAC control unit.

Please refer to "B. Further Information about the Business — 2. Intellectual Property Rights" in Appendix VI in this prospectus for further details on our patents and other intellectual property rights.

(ii) to strengthen research and development cooperation with universities, automakers and our HVAC components suppliers

While we perform most of our research and development activities independently to develop our own products and technologies, we also leverage our research and development capability to undertake research projects with certain automakers, HVAC components suppliers and academic institutions (such as Zhejiang University and Nanjing Agricultural University Institute of Technology).

Our technical team will work closely with the technical department of our customers to ascertain their technical requirements. We further cooperate with the customer during the products development process. In addition, we will enter into components and parts development agreement with our suppliers, pursuant to which we develop some HVAC components we do not manufacture.

In October 2006, we entered into an agreement with Nanjing Agricultural University Institute of Technology to improve the efficiency of evaporators used in our HVAC systems under an improvement program. Pursuant to the agreement, we allocated RMB200,000 to this project, of which RMB50,000 was used for research, labour, administration and sample production fee and the remaining RMB150,000 was used for revising the mould of the evaporators. Nanjing Agricultural University

Institution of Technology's role in this project included analyzing the functionality of the original evaporators, building the mathematical model and preparing the proposal for revising the mould of the evaporators while our role in this project included providing the two-dimension drawing, information on the experiments carried out to the original sample of the evaporators, and providing technical guidance to Nanjing Agricultural University Institution of Technology, assessing the feasibility of revising the mould of the evaporators based on the proposal prepared by Nanjing Agricultural University Institution of Technology and if determined to be feasible, revised the mould accordingly. This project ended in May 2007. We have subsequently applied the result of this project in our production process which has helped us to reduce the weight of our products. Pursuant to the agreement we entered into with Nanjing Agricultural University Institution of Technology, we retained ownership of the revised mould and the technical know-how developed as a result of this project.

In July 2009, we have engaged Zhejiang University to assist us in the development of the HVAC control unit for electric vehicles. Pursuant to the agreement entered into between Xiezhong Nanjing and Zhejiang University, Zhejiang University was responsible for developing the HVAC control unit for electric vehicles according to the technical requirements provided by us. Zhejiang University was responsible for preparing the research and development proposal which mainly contained information of the research to be carried out, the technical road-map, coordination of the research process and the product approval process. The agreement also stipulated a development timetable which spanned from July 2009 to December 2010. Under the agreement, both Zhejiang University and us have equal share of the ownership of the intellectual properties and are entitled to apply for patent of the intellectual properties developed in this project. Once patented, the ownership of the relevant patent and any income arising from such patent will be shared equally between Zhejiang University and us. This project was completed in December 2010 and a HVAC control unit for electric vehicles has been developed. As at the Latest Practicable Date, no intellectual properties developed in this project has been patented. Xiezhong Nanjing paid a fee of RMB100,000 to Zhejiang University for funding the research. To capture the emerging electric vehicle market opportunities, we intend to allocate more resources for the research and development of HVAC systems for electric vehicles.

Since we operate in an industry where the products require customisation, we believe that our research and development activities have allowed us to respond to our customers' new product development requests and meet the specifications and technical requirements of its different customers. To successfully secure sales, we have to demonstrate to automakers that we have the research and development capability to conduct concurrent product development with the automakers while the vehicle is being developed and that our products will be compatible with the vehicle. In order to better satisfy our customers' requirement, we have participated in new product research and development with customers from the initial design stage. We believe such collaborative research and development efforts with automakers have enhanced our research and development capabilities and customer loyalty. Benefited from our research and development efforts, we are able to develop new products and thereby maintain our competitiveness and pricing power. We have successfully registered 9 patents of invention or utility models, and we are in the process of applying 6 patents of design or utility models as at the Latest Practicable Date.

We had also been benefited from our research and development efforts in reducing the size and weight of our products, enhancing the efficiency of our products and enabling us to use common parts for various products.

Going forward, we intend to strengthen our research and development of existing products through recruiting additional expertise and increase our annual budget on research and development. For further details, please refer to the paragraph titled "Our Strategies — Strengthening our research and development capabilities and developing HVAC system for electric vehicles" in this section of the prospectus

We place strong emphasis on our research and development capabilities, as our Directors believe it is one of the key factors to our success. Our research and development expenses during the Track Record Period amounted to approximately RMB4.1 million, RMB6.6 million and RMB9.9 million, respectively. Expenditure on research activities is recognised as an expense in the period in which it is incurred. According to IFRS, expenditure on development activities is capitalised only if all the criteria for capitalisation under IFRS are met. The criteria include, among others, technical feasibility of completing the intangible asset so that it will be available for use or sale; and whether the expenditure attributable to the intangible asset during its development can be reliably measured. As our research and development costs may not be easily quantified and allocated to specific items to be developed, our research and development expense were not capitalized, but were expensed when they were incurred.

INTELLECTUAL PROPERTY

Our intellectual property rights are important to our businesses since we have developed a number of patents over the years and have applied them in our HVAC systems to enhance our competitiveness, product quality and operation efficiency. We take steps to protect our intellectual property rights and implement a set of internal intellectual property management rules. We also enter into confidentiality agreements and non-competition agreements with certain of our staff (who have access to our technical know-hows) as measures to protect, amongst others, our technical know-hows. Under the confidentiality agreements with our staff, our staff would be responsible to pay the damages caused to us as a result of their breaches of the confidentiality agreement. During the Track Record Period and as at the Latest Practicable Date, there has not been any breach of the confidentiality requirement under the relevant agreement by our staff where our staff was required to pay damages to us as a result.

Pursuant to the agreements with our customers, our customers require us and our staffs to keep confidential and ensure the safekeeping of the confidential information they have provided to us. Generally, we are restricted from divulging any confidential technical and commercial information to any third party without the written consent of our customers. Under the agreements with our customers, we would be responsible to pay damages to our customers if we breach the confidentiality requirement imposed on us. During the Track Record Period and as at the Latest Practicable Date, there has not been any breach of the confidentiality requirement under the relevant agreement by us where we were required to pay damages to our customers as a result.

To ensure that our staff also fulfill their duty of confidentiality, we also require our staff who are involved in the relevant project to sign confidentiality undertakings in relation to the technical drawings, products and other technical information provided by our

customers, designs belonging to our customers and other information as specified by our customers as confidential. As products of different customers are produced in the same production facilities, to prevent leakage of confidential information and to protect technological know-how, we have formulated relevant confidentiality policies and have requested our staffs to adhere to such policies. For example, our confidentiality policies stipulate that for representatives of our customers visiting our production bases, they will be allowed to enter our production facilities only if they are guided by our staffs who will accompany representatives of our customers throughout their visit. Our confidentiality policies also prohibit our staffs from making copies of confidentiality information without the approval of managerial staffs and from discussing in open area of our premises in relation to our customers' confidential information.

In some cases, we engage automotive HAVC components suppliers to develop a new automotive HVAC component. Generally, we would have the ownership of the intellectual property rights in respect of such new automotive HVAC components. In such cases, we enter into technical agreements of product development with the automotive HAVC components suppliers, pursuant to which, the suppliers have a duty of confidentiality on all of the design drawings, technical documents provided by us and so developed under the relevant agreements. Such duty of confidentiality shall survive on termination of the relevant agreement. Under the agreements with our suppliers, our suppliers shall be responsible for all loss and damages arising out of breaches of their duty of confidentiality. Under the relevant agreements with automotive HVAC components suppliers, the automotive HVAC components suppliers are restricted from (i) selling, distributing, importing, exporting or allowing other parties to manufacture, use, sell, distribute or transfer the innovation created under the relevant agreement; (ii) assembling, supplying or otherwise transferring the products or similar products to any third parties; and (iii) selling or otherwise transferring the mould, specialized production tool and facilities containing the information of the products. During the Track Record Period and as at the Latest Practicable Date, there has not been any breach of confidentiality requirement under the relevant agreement by our suppliers, where our supplier was required to pay damages to us as a result.

As at the Latest Practicable Date, we had registered 1 trademark, 9 patents and 1 domain name and had applied for registration of 6 other patents and another 2 trademarks of "协众 XIEZHONG" in two different classes in China. We had applied for the registration of 3 trademarks and had registered 3 domain names in Hong Kong. Details of our registered intellectual property portfolio are provided in the section headed "B. Further Information about the Business — 2. Intellectual Property Rights" in Appendix VI to this prospectus. There was no infringement or disputes in respect of our intellectual property rights against or by any third parties during the Track Record Period.

QUALITY CONTROL

We adopt a quality control system throughout our operation, extending from raw materials procurement, production and processing, to sales and distribution of our products to customers. Raw material which are used in our production are subject to quality control. We conduct sample testing on batch of HVAC components which are not manufactured by us. In the event we detect any substandard parts from the number of samples we have drawn, according the terms of our contract with our suppliers, we will return the whole batch of such parts to the relevant suppliers and may claim compensation in accordance with the terms of the supply agreements. We provide technical support services to give

guidance to our customers on how to install our products in their vehicles to prevent product damage caused by improper installation. We cooperate with customers so that our HVAC systems can better suit our customers' vehicles. In July 2011, our operating subsidiary, Xiezhong Nanjing, obtained ISO/TS16949:2009 certification for its quality management system applicable to the design and manufacturing of air-conditioner, which will remain valid until 10 July 2014. ISO/TS16949:2009 is a particular set of standards for the application in the automobile industry. We have not received any material complaint on our product quality during the Track Record Period.

It is our policy that our customers are not entitled to return our products except for deficiency of quality reason. Some of our sales contracts with customers stipulate that our products may be returned if there is serious deficiency of the quality of our products. Upon receipt of feedback from our customers on the defective products, we shall discuss with our customers to resolve the matters according to the terms of the sales contract. We shall also conduct investigation and take remedial measures (such as price adjustment or return of those specific defective goods) if appropriate. During the Track Record Period, goods return was less than 2% of our sales.

We generally provide warranty coverage for our products. Generally, the warranty period we provide ranges from 60,000 kilometres to 100,000 kilometres of mileage of the relevant vehicle or 1 year to 3 years. In other contracts for sales of HVAC systems or HVAC components for construction machineries, we provide a warranty period of 1 year or 2,000 hours of operation of the machinery of which the HVAC systems are used, whichever is sooner. During the warranty period, we will be responsible for repairing, exchanging and returning our defective products free-of-charge for our customers. During the Track Record Period, provision for product warranties utilised amounted to approximately RMB2.3 million, RMB1.6 million and RMB3.6 million respectively and additional provision made for products warranties amounted to approximately RMB2.3 million, RMB4.9 million and RMB2.4 million, respectively. Our Directors have confirmed that we had not received any significant product recall, warranty claims or product liability claims for defective products during the Track Record Period.

INVENTORY MANAGEMENT

Our inventories mainly consist of raw materials, work-in-progress and finished products. Our logistics team reviews and monitors our inventory level on a periodical basis. This involves the maintenance of an appropriate level of inventory as well as any write-down or provision for any obsolete and slow-moving inventory items. During the Track Record Period, there was a write-down of inventories of approximately RMB0.1 million, RMB1.4 million, and RMB1.3 million, respectively.

COMPETITION

Our products are sold in the domestic market in China. We face increasing competition from various competitors including foreign and domestic automotive HVAC system manufacturers. For further details of the competitive landscape of the automotive HVAC system market, please refer to the paragraph titled "China's SUV, pickup truck and heavy truck HVAC system market overview" in the "Industry Overview" section of this prospectus.

Given our competitive strengths as set out in the paragraph titled "Our competitive strengths" in this section of the prospectus, our Directors believe our leading position in the HVAC systems for SUVs, pickup trucks and heavy trucks markets will not be easily overtaken.

ENVIRONMENTAL AND OCCUPATIONAL HEALTH AND SAFETY

Environmental Protection

Our Group's manufacturing operations are subject to PRC environmental laws and regulations on air emission, solid waste emission, sewage and waste water, discharge of waste and pollutants, and noise pollution. These laws and regulations include the Law on Environmental Protection, the Law on Prevention and Control of Water Pollution, the Law on Prevention and Control of Atmospheric Pollution, the Law on Prevention and Control of Noise Pollution and the Law on Prevention and Control of Environmental Pollution Caused by Solid Waste. These laws and regulations govern a broad range of environmental matters, including air pollution, noise emissions and water and waste discharge. Our Group is also subject to Administrative Regulations on Environmental Protection for Construction Project and the Law on Appraising of Environmental Impacts.

The pollutants generated from our operation mainly include exhaust fume emitted from our canteen, sewage and waste water from our production process, solid waste such as scrap aluminium and noise generated in the course of our production. We mainly deal with the above pollutants with the measures listed below:

1. Exhaust fume — exhaust fume passes through the oil fume separator before it is emitted through the chimney.

2. Sewage and waste water — sewage and waste water are treated in septic tank and oil separator respectively before they undergo water treatment.

3. Solid waste — solid waste, mainly scrap aluminium, is collected by scrap metal recyclers.

4. Noise — we have fitted noise insulation to suppress the noise generated in the course of our production.

In January 2011, our operating subsidiary, Xiezhong Nanjing, was accredited GB/T24001-2004 idt ISO14001:2004 certification in relation to its environmental management systems, which will remain valid until 4 January 2014.

Neither Xiezhong Nanjing, Xiezhong Beijing, Xiezhong Liaoning nor Xiezhong Hubei produces, uses or sells refrigerants except that: (i) Xiezhong Nanjing may use a very small amount of R134a for the purpose of experiment; (2) Xiezhong Nanjing would purchase R134a for certain customers according to their specific requirements. For each of the three years ended 31 December 2011, the cost of refrigerants represents approximately 0.05%, 0.03% and 0.15%, respectively, of our total cost of sales. As confirmed by our PRC Legal Advisers, it is not necessary for Xiezhong Nanjing to get any permission from any

government authorities to use or purchase R134a and that we are in compliance with the relevant PRC environmental laws and regulations in relation to our use of R134a in the course of our business.

As confirmed by our PRC Legal Advisers, we have complied in all material respects with the relevant PRC environmental protection laws and regulations. We have been subject to the inspections by the local governmental authorities 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.

During the Track Record Period, our annual cost of compliance with the applicable environmental protection laws and regulations was approximately RMB6,000, RMB6,000 and RMB6,000, respectively. The cost of compliance going forward is expected to be approximately RMB8,000, RMB10,000 and RMB12,000 for each of the three years ending 31 December 2014.

We have taken necessary measures to protect our employees' health and safety at work, including providing our employees with protective clothing and accessories, such as gloves, goggles and masks, and providing occupational safety training for all of our employees and special training for operators of certain equipment. In January 2011, our operating subsidiary, Xiezhong Nanjing, was accredited GB/T 28001-2001 certification for its established occupational health and safety management systems, which will remain valid until 4 January 2014.

During the Track Record Period, we have not encountered any material claims or incidents in relation to occupational health and safety issues or been involved in any accident causing death or serious injury in the course of our business operations.

EMPLOYEES

As at 31 December 2009, 2010 and 2011 and as at the Latest Practicable Date, we had approximately 612, 747, 893 and 882 staff, respectively. The following table sets forth, for the periods indicated, the breakdown of number of our employees employed by function:

Department	As of 31 December 2011		As at the Latest Practicable Date	
	Number of employees	*Percentage of total employees (%)*	*Number of employees*	*Percentage of total employees (%)*
Management	6	0.7	8	0.9
Research and development	113	12.7	117	13.3
Sales and marketing	69	7.7	78	8.8
Production	491	55.0	484	54.9
Procurement	16	1.8	17	1.9
Quality control	71	8.0	62	7.0
Office Support	39	4.3	37	4.2
Finance	17	1.9	16	1.8
Human resources	5	0.5	5	0.6
Logistic	66	7.4	58	6.6
Total	893	100.0	882	100.0

Our total staff costs for the Track Record Period were RMB33.8 million, RMB42.7 million and RMB50.7 million, respectively, which accounted for 9.7%, 7.8% and 8.2% of our total turnover, respectively. We provide training to our staff on a regular basis. We adopt a performance-based incentive scheme for all our employees. We adhere strictly to both statutory employment standards and those requested by our customers, such as wages and working hours, and maintain internal standards and workplace practices that exceed both.

Social insurance and housing provident funds contributions

Pursuant to applicable PRC laws and regulations, we are required to contribute to social insurance (which includes contribution for various funds in the PRC, including pension insurance, medical insurance, unemployment insurance, occupation injuries and maternity insurance) and housing provident funds for our staff.

Xiezhong Nanjing, Xiezhong Liaoning, Xiezhong Hubei and Xiezhong Beijing, as PRC entities, are required by the PRC laws and regulations to make contributions to the social insurance and housing provident funds. Due to the differences in local regulations, inconsistent implementation by local authorities in the PRC and different levels of acceptance of the social insurance and housing provident funds systems by employees,

during the Track Record Period, Xiezhong Nanjing, Xiezhong Liaoning and Xiezhong Hubei did not fully comply with the relevant PRC laws and regulations in relation to social insurance contributions.

As advised by our PRC Legal Advisers, the amount of social insurance contributions made by the Group for the employees of Xiezhong Liaoning and Xiezhong Hubei and some of the employees of Xiezhong Nanjing were lower than the amount required under the PRC laws and regulations as they had adopted an amount less than the average monthly salary received by each employee in the preceding year as the basis for calculation. We have consulted with the competent social insurance administration bureau, and were informed that according to the general practice of these social insurance administration bureau, the unpaid social insurance contributions cannot be fully paid since such social insurance administration bureau will not accept repayment of the unpaid social insurance contributions and that the contribution basis can only be adjusted in July of each year. We estimate that the aggregated amount of unpaid social insurance contributions will be approximately RMB7.9 million until 30 June 2012. We will make full social insurance contributions for all of employees of Xiezhong Nanjing, Xiezhong Liaoning and Xiezhong Hubei from July 2012 onward for all of our PRC employees in according with the relevant PRC laws and regulations.

As advised by our PRC Legal Advisers, Xiezhong Nanjing, Xiezhong Liaoning and Xiezhong Hubei may be required by the relevant authorities to contribute all the unpaid social insurance contributions in the prescribed period plus a daily overdue fine calculated at 0.05% of any unpaid social insurance contributions will be imposed. If we fail to make contribution in such prescribed period, the amount of maximum fine/penalty that may be imposed on our Group for the non-compliance with social insurance regulations is three times the amount equivalent of the amount of all the unpaid social insurance contributions, which, as we estimate, amounts to approximately RMB23.7 million until 30 June 2012.

Each of Xiezhong Nanjing, Xiezhong Liaoning and Xiezhong Hubei had communicated with the relevant authorities regarding the contributions of social insurance. Xiezhong Nanjing has obtained a written confirmation from 南京市江寧區社會勞動保險所 (the Social and Labor Insurance Administration of Nanjing Municipal Jiangning District*), the competent social insurance authority, on 5 December 2011, which confirmed that Xiezhong Nanjing had duly contributed social insurance for its employees since its incorporation in compliance with the PRC law without any record of being sanctioned for any non-compliance. Xiezhong Liaoning has obtained a written confirmation from 撫順市社會保險事業管理局經濟開發區分局 (the Social Insurance Matter Administration Bureau of Fushun Municipal Branch of Economic Development Zone*), the competent social insurance authority, on 2 November 2011, which confirmed that Xiezhong Liaoning had duly contributed social insurance for its employees since its incorporation in compliance with the PRC law without any record of being sanctioned for any non-compliance. Xiezhong Hubei has obtained a written confirmation from 武漢經濟技術開發區社保處登記科 (the Registration Unit of Social Insurance Bureau of Wuhan Economic Technology Development Zone*), the competent social insurance authority, on 26 October 2011, which confirmed that payment of social insurance contributions by

Xiezhong Hubei is normal. Such written confirmation only confirmed that Xiezhong Hubei has made contributions for its employees, and no unusual incidence has occurred in the payment of social insurance contributions by Xiezhong Hubei.

Xiezhong Nanjing has obtained a written confirmation from 南京住房公積金管理中心江寧管理部 (the Housing Provident Funds Administration Centre of Nanjing, Jiangning Administration Department), the competent housing provident funds authority on 9 December 2011, which confirmed that Xiezhong Nanjing had fully paid all previously unpaid housing provident funds during the Track Record Period and has since contributed housing provident funds for its employees without any non-compliance with laws, regulations or local rules related to housing provident funds. Xiezhong Liaoning has obtained a written confirmation from 撫順市住房公積金管理中心望花區辦事處 (the Office of Housing Provident Funds Administration Centre of Wanghua District of Fushun*), the competent housing provident funds authority, on 16 December 2011, which confirmed that Xiezhong Liaoning had duly contributed housing provident fund for its employees, without any record of being sanctioned for any non-compliance since its incorporation. Xiezhong Hubei further obtained a written confirmation from 武漢住房公積金管理中心 (the Housing Provident Funds Administration Centre of Wuhan*), the competent housing provident funds authority on 12 January 2012, which confirmed that Xiezhong Hubei had paid the housing provident funds from April 2010 to December 2011 and that it has not received any complaint from the relevant government authorities and employees.

There is no assurance that the relevant government authorities will not levy administrative penalties as mentioned above against the Group in the future. Nevertheless, based on the above confirmations from the relevant government authorities, our PRC Legal Advisers are of the view that the risk of Xiezhong Nanjing, Xiezhong Liaoning and Xiezhong Hubei being imposed of any fines by the relevant authorities is relatively remote. Taking into account the advice from our PRC Legal Advisers above, the Directors consider that the financial impact on the Group is minimal and no provision has been made in this regard, which would not affect the true and fair view of the financial information in Appendix I to this prospectus.

The previously unpaid housing provident funds amounted to RMB4.0 million and such amount has been subsequently fully paid. The Group has already made due contributions to housing provident funds as at the Latest Practicable Date.

As at the Latest Practicable Date, none of Xiezhong Nanjing, Xiezhong Liaoning and Xiezhong Hubei had received any complaint from our employees in relation to the social insurance and housing provident funds contributions, or any notice or legal documents from the regulatory authorities of social insurance and housing provident funds requesting contributions for the relevant social insurance or housing provident funds.

Save for the above, as advised by our PRC Legal Advisers, the Group has complied with the relevant labour and social welfare laws and regulations in PRC in all material aspects.

During the Track Record Period, we have not experienced any significant problems with our employees or disruption to our operations due to labor disputes, nor have we experienced any difficulties in the recruitment and retention of experienced staff. We believe that we have a good working relationship with our employees.

INSURANCE

We maintain insurance policies covering certain properties and motor vehicles. In line with our understanding of the usual industry practice, we do not maintain product liability insurance as it is not compulsorily required under the PRC laws and regulations. We consider that our insurance coverage is in line with the industry practice in the PRC.

PROPERTIES

As at the Latest Practicable Date, we had interest in the following properties in the PRC.

At Jiangning District, Nanjing, Jiangsu, we have our Jiangning Plant, which are five single to three-storey workshop, office buildings and warehouse with a total gross floor area of approximately 34,689.10 sq.m. and various structures erected upon a parcel of land with a site area of 60,133.90 sq.m. On the same parcel of land, we are constructing a research centre building with a gross floor area of 15,631.00 sq.m.

At Fushun Economic Development Zone, Fushun, Liaoning, a three-storey workshop and office building with a gross floor area of approximately 5,656.56 sq.m. erected upon a parcel of land with a site area of 30,893.00 sq.m.

At Caiyu Town, Daxing District, Beijing, a parcel of land with a site area of approximately 45,178.23 sq.m. This parcel of land was acquired for construction of the Beijing Plant.

At Caiyu Town, Daxing District, Beijing, a leased property of a room with a gross floor area of approximately 33.39 sq.m. which is occupied by us for office use.

At Yujia Town, Tongzhou District Beijing, a leased property of a single-storey warehouse building with a gross floor area of approximately 674.2 sq.m. which is occupied by us for storage use.

At Wuhan Economic Technology Development District, Wuhan, Hubei Province, a leased property of an office unit with a gross floor area of approximately 140 sq.m. which is occupied by us for office use.

The following sets out the material irregularities in respect of our properties.

Lack of planning and construction permits, completion acceptance report and building ownership certificates for some of the properties in the Jiangning Plant

As at the Latest Practicable Date, we have not obtained the Four Documents for the Canopy and the Electricity Distribution Room. We did not obtain the Four Documents because we have mistakenly believed that since these structures are simple temporary structures and we can demolish them if required by the relevant governmental authorities, it was not necessary to obtain the Four Documents. We have consulted with the relevant governmental authorities, and was informed that Xiezhong Nanjing cannot make up the formalities for applying for the Planning Permit on Construction Works (which is the prerequisite for applying for the other three documents) for both the Canopy and the Electricity Distribution Room because Xiezhong Nanjing had failed to satisfy the requirements of planning pursuant to the relevant PRC laws and regulations. Without the Planning Permit on Construction Works, Xiezhong Nanjing is not able to apply for the other three documents.

As advised by our PRC Legal Advisers, the penalty which the relevant authority may impose on us in respect of the Canopy and the Electricity Distribution Room would be as follows:

(a) for failing to obtain the Planning Permit on Construction Works, order of demolition of such properties within a prescribed time limit, forfeiture of any realty or unlawful gains if cannot be demolished and a fine equivalent to not more than 10% of the construction costs of such properties, which we estimate would not exceed RMB80,000;

(b) for failing to obtain the Construction Permit on Construction Works, a fine of not less than RMB5,000 and not more than RMB30,000 in the event that Xiezhong Nanjing has made any unlawful gains, or a fine of not less than RMB5,000 and not more than RMB10,000 in the event that Xiezhong Nanjing has not made any unlawful gains; and

(c) for failing to obtain the Completion Acceptance Report, order to the rectify non-compliance and a fine of not less than 2% and not more than 4% of the contract value of the construction contract, which our Directors estimate would not exceed RMB32,000.

As further advised by our PRC Legal Advisers, no fines will be imposed on us for failing to obtain the building ownership certificates in accordance with the existing PRC laws and regulations.

During the Track Record Period, there has been no accident causing injuries owing to the structural safety of the Canopy or the Electricity Distribution Room. Although the relevant government authorities have so far taken no steps in demanding the demolition of these structures or imposing the aforementioned penalties, there is no assurance that the relevant government authorities will not take any action. Demolition of the Canopy and relocation of the Electricity Distribution Room may be necessary if the relevant government authorities decide to take enforcement action against us.

Our Directors consider that the demolition of the Canopy and relocation of the Electricity Distribution Room in respect of the aforesaid properties will not have a material impact on our operation for the reasons described below:

(i) the Canopy is mainly used to place our semi-finished products temporarily on rainy days when they are transferred between the production warehouse and storage warehouse. In the event of demolition of the Canopy, we plan to cover our semi-finished products by other means and our Directors believe that this will not result in any material adverse effect on our operation and financial conditions. In the event of demolition of the Electricity Distribution Room, we plan to relocate the same into our production warehouse. As a contingency plan, we have already identified one suitable site area in our production warehouse to relocate the Electricity Distribution Room. We estimate that the cost of relocation, which include the cost of reconnection of all electricity cables, will be not more than RMB360,000. The estimated cost of relocation does not include the aforementioned possible maximum fine and the demolishing costs of the Electricity Distribution Room. If so required, we estimate that it will take no more than 7 days to complete the relocation process, during which it is estimated that our operation and business will not be halted as we intend to increase our production volume beforehand to replenish our stock of products to cater for our customers' demands while we are implementing the relocation plan. Having considered the cost of demolition of the Canopy and the cost of relocation for the Electricity Distribution Room mentioned above, our Directors are of the view that it will not have a material financial and operating impact on us; and

(ii) Sunrise International and Mr. Chen Hao have agreed to provide indemnity to the Group in respect of the loss arising from this incident of non-compliance of the relevant PRC laws and regulations. For further details of the indemnities provided by Sunrise International and Mr. Chen Hao, please refer to the paragraph headed "G. Other information" in Appendix VI to the prospectus.

The relevant lessor does not have legal title to lease a storage warehouse to Xiezhong Beijing

Xiezhong Beijing has leased a property being used as storage warehouse with an aggregate gross floor area of approximately 674.20 sq.m. in Tongzhou District, Beijing. As advised by our PRC Legal Advisers, the storage warehouse is erected on a piece of farmers collectively-owned land (農民集體所有地) which was leased by lessor from the relevant village committee. The warehouse was constructed by the lessor without obtaining the necessary planning, construction permits and building ownership certificate. As advised by our PRC Legal Advisers, pursuant to 中華人民共和國土地管理法 (the Law of Land Administration of the PRC*), farmers' collectively-owned land shall not be leased, transferred or rented for non-agricultural construction, except in certain circumstances and the lessor could be ordered by the relevant land administrative departments to make correction within a prescribed time limit and confiscate the proceeds generated from the breach and impose a fine. As a result, our PRC Legal Advisers are of the view that Xiezhong Beijing could be ordered to cease occupation of the storage warehouse.

In the event that the relevant government authority orders Xiezhong Beijing to cease occupation of the storage warehouse, we plan to minimise our exposure to adverse impact on our operation by adopting a contingency plan of relocating to another storage warehouse. We estimate that the cost to be incurred during the relocation process will mainly be transportation cost with an estimated sum of approximately RMB1,500. We estimate the monthly rental cost of a storage warehouse of similar size to be approximately RMB8,300 per month and it will take no more than 3 days to complete the relocation process, during which it is estimated that our operation and business will not be halted. Having considered the cost of relocation of our storage warehouse and the monthly rental fee payable, our Directors are of the view that it will not have a material financial and operating impact on us.

LEGAL PROCEEDINGS AND REGULATORY COMPLIANCE

As at the Latest Practicable Date, we were not a party to any material arbitration, litigation or administrative proceedings which could be expected to have a material adverse effect on our business or results of operations. We are not aware of any pending or threatened arbitration, litigation or administrative proceedings against us.

During the years ended 31 December 2009 and 2010, Xiezhong Nanjing extended Inter-enterprise Loans to Aotecar Nanjing, Xiezhong Liaoning and 北京智科投資管理有限公司 (Beijing Zhike Investment Management Co., Ltd*), in order to provide short term financing to Aotecar Nanjing for it to repay its existing bank loans such that it can renew the bank loans, and to provide working capital financing to Xiezhong Liaoning and Beijing Zhike Investment Management Co., Ltd. The amounts of these Inter-enterprise Loans range from RMB2 million to RMB20 million. As at the Latest Practicable Date, all Inter-enterprise Loans have been fully settled. The aggregated income gained by Xiezhong Nanjing as a result of these Inter-enterprise Loans amounts to approximately RMB1.1 million.

Our PRC Legal Advisers are of the view that the Inter-enterprise Loans were inter-enterprise lending that violate 貸款通則 (Lending General Provision*) promulgated by the PBOC which state that non-banking institutions are not permitted to engage in lending business in the PRC. A fine which amounts to 1 to 5 times of the lender's income resulting from these violation activities may be imposed by the PBOC for such inter-enterprise lending. Besides, according to 中華人民共和國行政處罰法 (the Law of the PRC on Administrative Penalty*), where an illegal act is not discovered within two years of its commission, administrative penalty shall no longer be imposed and the period of time shall be counted from the date the illegal act is committed. Since part of the Inter-enterprise Loans had been fully repaid two years ago, our PRC Legal advisers are of the view that our Group would only be penalized in respect of interest income, which, as we calculated, amounted to approximately RMB713,000 (out of the total interest income of RMB1.1 million gained by Xiezhong Nanjing from Inter-enterprise Loans). Therefore, we estimate that the fine payable by Xiezhong Nanjing as a result of violation of 貸款通則 (Lending General Provision*) would be approximately RMB713,000 to RMB3,565,000.

In 2010, Xiezhong Nanjing had received advances from 南京協眾集團房地產開發有限公司 (Nanjing Xiezhong Group Property Development Co. Ltd.*) as borrower of an Inter-enterprise Loan in the amount of RMB10 million which has been fully settled. Our PRC Legal Advisers have advised that according to the relevant PRC laws and regulations, Xiezhong Nanjing as borrower of such advances, will not be penalized.

As confirmed by our PRC Legal Advisers, except as disclosed in this prospectus, we have complied with, in all material respects, all the relevant laws and regulations applicable to the Group's operations in the PRC and obtained all necessary licenses and approvals from the relevant authorities to carry out our business in all material aspects.

Indemnity by Sunrise International and Mr. Chen Hao

Sunrise International and Mr. Chen Hao have executed the Deed of Indemnity in favour of our Group whereby they will jointly and severally indemnify each of the members of the Group against, inter alia, all expenses, payments, sums, outgoings, fees, demands, claims, damages, losses, costs (including, but not limited to, legal and other professional costs), charges, liabilities, fines, penalties and tax which any member of the Group may incur, suffer or accrue, directly or indirectly, from or on the basis of or in connection with the non-compliance incidents of the relevant PRC laws and regulations by any member of the Group in the PRC described above in the paragraphs headed "Employees", "Properties" and "Legal Proceedings and Regulatory Compliance" in this section. For further details of the Deed of Indemnity, please refer to the paragraph headed "G. Other information — 1. Indemnity for tax and other matters" in Appendix VI to the prospectus.

MEASURES TO STRENGTHEN CORPORATE GOVERNANCE PROCEDURES

Our Company has adopted the following measures to prevent reoccurrence of material non-compliance incidents in the future:

Incidents	Prevention measures
Lack of planning and construction permits, completion acceptance report and building ownership certificates for some of the properties in the Jiangning Plant and the relevant lessor does not have legal title in respect of a storage warehouse leased by Xiezhong Beijing (as more particularly described in the paragraph headed "Properties" in this section)	Future property development would only be commenced after the necessary licenses and permits have been obtained. Properties under development would only be used after the respective authorities had inspected the properties and issued the necessary licenses and permits. We will only enter into lease agreements after the lessor has provided all relevant title documents. Our compliance officers will be in charge to oversee the regulatory compliance aspect of all property transaction in the future and report to the Directors as to the timing when the relevant construction work can be started or when the relevant properties can be used or leased. Our compliance officers will be assisted by external PRC legal advisers in performing their duties. We will also engage external PRC legal advisers to conduct due diligence on property title for us. Where the property transaction is complicated and requires extensive devotion of time, we will engage external PRC legal advisers to take charge of the transaction for us.

Incidents	Prevention measures
Failure to fully pay social insurance (as more particularly described in the paragraph headed "Employees" in this section)	Reinforcement education regarding the importance of participation in the social insurance scheme would be provided to all new employees. We will make the social insurance fund contributions for all of our PRC employees in accordance with the relevant PRC laws and regulations. Our human resources department will be responsible for ensuring that social insurance contribution is duly made by the Group and the employees. Our finance department will carry out internal checking on a quarterly basis to ensure that we are making the social contribution in accordance with the relevant PRC laws and regulations.
Inter-enterprise loans (as more particularly described in the paragraph headed "Legal Proceedings and Regulatory Compliance" in this section)	The Group will not advance or receive any Inter-enterprise Loans after the Listing. We will consult our external PRC legal adviser before we enter into any loan transaction (other than bank loans).

In order to prevent future occurrence of legal non-compliance by our PRC subsidiaries and joint-controlled entity in the PRC, a compliance committee comprising all independent non-executive Directors as established by the Board will oversee the matter and ensure compliance with the PRC laws and regulations. The compliance committee will be assisted by external PRC legal advisers in performing its duties. To ensure ongoing compliance with the relevant laws and regulations in the PRC on a daily operation basis, Mr. Xin Fangwei, one of our senior management officer, and Mr. Chui Wing Fai, our company secretary, have been appointed as our internal compliance officers. Mr. Xin and Mr. Chui are responsible for managing matters on connection with regulatory compliance of our PRC operations. To reinforce Mr. Xin and Mr. Chui's performance as our internal compliance officers in the PRC, we will also appoint PRC legal adviser to handle all legal and compliance matters of our Group and to advise us on legal and compliance matters in relation to our Group's operation.

As a matter of implementation of effective preventive measures in order to further ensure ongoing compliance with the relevant laws and regulations in the PRC, we have planned to adopt the following measures:

- Meetings and seminars will be arranged for our senior management from time to time to discuss and study regulatory requirements and latest updates thereof applicable to our business operations.

- All senior management and staff will be required to report to and/or notify our Directors, our compliance officers or our external PRC legal adviser promptly of any events which are subject of any possible violations of various regulatory requirements.

- Regular training programmes will be held to improve our staff's legal knowledge.

Our Directors are of the view that the above measures will improve our staff's understanding of the relevant rules and regulations in the PRC and enable us to strengthen our internal control environment both at the working level and at the monitoring level, and therefore, the above measures should be adequate and effective to ensure our Group's ongoing compliance with the relevant rules and regulations in the PRC.