THIS CIRCULAR IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION

If you are in doubt as to any aspect of this circular or as to the action to be taken, you should consult your stockbroker or other registered dealer in securities, bank manager, solicitor, professional accountant or other professional adviser.

If you have sold or transferred all your shares in Ko Yo Chemical (Group) Limited (the "**Company**"), you should at once hand this circular and the accompanying form of proxy to the purchaser(s) or the transferee(s) or to the bank, stockbroker or other agent through whom the sale or transfer was effected for transmission to the purchaser(s) or the transferee(s).

This circular is for information purpose only and does not constitute an invitation or offer to acquire, purchase or subscribe for the securities of the Company.

KOYO

Ko Yo Chemical (Group) Limited
玖源化工(集團)有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 827)

(I) SHARE CONSOLIDATION
(II) CHANGE IN BOARD LOT SIZE
(III) ISSUE OF NEW SHARES AND CONVERTIBLE BONDS UNDER SPECIFIC MANDATE
(IV) LOAN FINANCING
(V) INCREASE IN AUTHORISED SHARE CAPITAL
(VI) APPLICATION FOR WHITEWASH WAIVER
AND
(VII) NOTICE OF EGM

Financial adviser to the Company

LY CAPITAL LIMITED
絡繹資本有限公司

Financial adviser to the Subscriber

博大資本國際有限公司
Partners Capital International Limited

Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders

八方金融有限公司
OCTAL Capital Limited

A letter from the Board is set out on pages 8 to 28 of this circular.

A letter from the Independent Board Committee containing its recommendation to the Independent Shareholders is set out on pages 29 to 30 of this circular.

A letter from Octal Capital Limited, the Independent Financial Adviser, containing its advice to the Independent Board Committee and the Independent Shareholders is set out on pages 31 to 65 of this circular.

A notice convening the EGM to be held at 11:00 a.m. on 13 October 2014 at Suite No. 02, 31st Floor, Sino Plaza, 255-257 Gloucester Road, Causeway Bay, Hong Kong is set out on pages 169 to 171 of this circular. Whether or not you intend to attend the EGM, please complete and return the enclosed form of proxy in accordance with the instructions printed thereon and return it to the Company's share registrar in Hong Kong, Union Registrars Limited, 18th Floor, Fook Lee Commercial Centre, Town Place, 33 Lockhart Road, Wanchai, Hong Kong as soon as possible and in any event, not less than 48 hours before the time fixed for holding the EGM or any adjournment thereof (as the case may be). Completion and return of the form(s) of proxy will not preclude you from attending and voting in person at the EGM or at any adjourned meeting thereof should you so wish.

22 September 2014

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EXPECTED TIMETABLE FOR THE SHARE CONSOLIDATION

Expected timetable

Set out below is the expected timetable for the implementation of the Share Consolidation. Dates and time specified below are Hong Kong dates and time. The below expected timetable is subject to the satisfaction of all the conditions of the Share Consolidation, including without limitation, the approval of the Share Consolidation by Shareholders at the EGM, and is therefore for indicative purpose only. Further announcement(s) (if any) will be made by the Company regarding any significant change to the following expected timetable as and when appropriate:

	2014
Latest time for lodging the proxy form for use at the EGM	11:00 a.m., Thursday, 9 October
Date of the EGM	11:00 a.m., Monday, 13 October
Announcement of voting results of the EGM	Monday, 13 October
Effective Date of the Share Consolidation	Tuesday, 14 October
Dealings in the Consolidated Shares commence	9:00 a.m., Tuesday, 14 October
Free exchange of existing share certificates for new share certificate for the Consolidated Share commences	Tuesday, 14 October
Original counter for trading in Existing Shares in board lot size of 20,000 Existing Shares (in the form of existing shares certificate) temporarily closes	9:00 a.m., Tuesday, 14 October
Temporary counter for trading in Consolidated Shares in board lot size of 4,000 Consolidated Shares (in the form of existing share certificates) opens	9:00 a.m., Tuesday, 14 October
Original counter for trading in Consolidated Shares in new board lot size of 4,000 Consolidated Shares (in the form of new share certificates) re-opens	9:00 a.m., Tuesday, 28 October
Parallel trading in Consolidated Shares in the form of new share certificates and existing share certificates commences	9:00 a.m., Tuesday, 28 October
Operation of odd lot trading facility for the Consolidated Shares commences	9:00 a.m., Tuesday, 28 October
Parallel trading in Consolidated Shares in the form of new share certificates and existing share certificates ends	4:00 p.m., Monday, 17 November
Operation of odd lot trading facility for the Consolidated Shares ends	4:00 p.m., Monday, 17 November

	2014
Temporary counter for trading in Consolidated Shares in board lot size of 4,000 Consolidated Shares (in the form of existing share certificates) closes	4:00 p.m., Monday, 17 November
Last day for free exchange of existing share certificates for new share certificates of the Consolidated Shares	Wednesday, 19 November

In this circular, the following expressions shall have the following meanings unless the context indicates otherwise:

"acting in concert"	has the meaning ascribed to it under the Takeovers Code;
"Announcement"	the announcement of the Company dated 14 August 2014 in relation to, among other things, the Share Consolidation and the issue of the New Shares and the Convertible Bonds;
"Asian Equity"	Asian Equity Special Opportunities Portfolio Master Fund Ltd, a company incorporated in the Cayman Islands;
"associate"	has the meaning ascribed to it under the Listing Rules;
"Bondholder"	holder of the Convertible Bonds;
"Board"	the board of Directors of the Company;
"Business Day"	a day, other than a Saturday or Sunday or a public holiday, on which commercial banks are open for business in Hong Kong;
"Company"	Ko Yo Chemical (Group) Limited, an exempted company incorporated in the Cayman Islands with limited liability whose shares are listed on the Stock Exchange;
"connected persons"	has the meaning ascribed to it under the Listing Rules;
"Consolidated Shares"	ordinary shares of HK$0.10 each in the share capital of the Company after the Share Consolidation becoming effective;
"Conversion Price"	the initial conversion price of the Convertible Bonds of HK$0.32 per Conversion Share, subject to the usual adjustments;
"Convertible Shares"	new Consolidated Shares which may fall to be allotted and issued upon exercise of the conversion rights attaching to the Convertible Bonds;
"Convertible Bonds"	the 7% coupon convertible bonds due 2024 in an aggregate principal amount of HK$832,000,000 proposed to be issued to the Subscriber pursuant to the Subscription Agreement;
"Directors"	the directors of the Company;
"Effective Date"	the effective date of the Share Consolidation, tentatively 14 October 2014;
"EGM"	the extraordinary general meeting of the Company to be held on 13 October 2014 to approve, among others, the Share Consolidation, the Specific Mandate and the Whitewash Waiver;

"Executive"	Executive Director of the Corporate Finance Division of the SFC or any of its delegates;
"Existing Shares"	existing ordinary shares of HK$0.02 each in the share capital of the Company;
"Group"	the Company and its subsidiaries;
"Guangan Factory"	the production facilities of the chemical project of the Company for 500,000 tonnes of methanol and 300,000 of ammonia in Guangan City, Sichuan Province, the PRC. Details of which are set out in the announcements of the Company dated 12 June 2014 and 9 September 2014;
"HK$"	Hong Kong dollar, the lawful currency of Hong Kong;
"Hong Kong"	the Hong Kong Special Administrative Region of the PRC;
"Hong Kong Share Registrar"	Union Registrars Limited, the share registrar of the Company in Hong Kong;
"IFC"	International Finance Corporation, a member of the World Bank Group who became a Shareholder pursuant to the subscription agreement dated 16 April 2009, details of which are included in the announcement of the Company dated 17 April 2009;
"Independent Board Committee"	an independent board committee established by the Board, comprising all the non-executive Directors, namely Mr. Hu Xiaoping, Mr. Woo Che-Wor, Alex, Mr. Qian Laizhong and Mr. Sun Tongchuan, to advise the Independent Shareholders as to the fairness and reasonableness of the terms of the Subscription Agreement and the Whitewash Waiver and as to voting;
"Independent Financial Adviser" or "Octal Capital"	Octal Capital Limited, a corporation licensed to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities under the SFO (Chapter 571 of the Laws of Hong Kong), who has been appointed as the independent financial adviser to the Independent Board Committee and the Independent Shareholders in respect of, among other things, the Subscription Agreement and the Whitewash Waiver

"Independent Shareholders"	for the purpose of the Subscription Agreement, the transactions contemplated thereunder and the Whitewash Waiver, Shareholders other than the Subscriber, Mr. Li and Mr. Yuan Bai and their respective concert parties and any other Shareholders who are interested or involved in the Subscription Agreement (including the Specific Mandate) and/or the Whitewash Waiver;
"Independent Third Parties"	individual or company who or which is independent of and not connected with any Directors, chief executive and substantial Shareholders of the Company, subsidiaries of the Company and any of their respective associates;
"Last Trading Date"	28 July 2014, being the last trading day for the Existing Shares before the date of the Announcement;
"Latest Practicable Date"	19 September 2014, being the latest practicable date prior to the printing of this circular for ascertaining certain information referred to in this circular;
"Listing Rules"	the Rules Governing the Listing of Securities on the Stock Exchange;
"Loan"	the interest-free loan of a principal amount of HK$200,000,000 advanced to the Group pursuant to the Loan Agreement;
"Loan Agreement"	the loan agreement dated 30 July 2014 entered into by the Subscriber as the lender and the Company as the borrower in relation to the Loan;
"Mr. Li"	Mr. Li Weiruo, an executive director of the Company and existing controlling shareholder of the Company;
"Mr. KM Cheng"	Mr. Cheng Kin Ming, the ultimate beneficial owner of the Subscriber and the Placing Agent;
"New Shares"	the 800,000,000 new Consolidated Shares proposed to be allotted and issued to the Subscriber pursuant to the Subscription Agreement;
"PA International"	PA International Opportunity VII Limited, a company incorporated in the British Virgin Islands;
"PAML"	Partners Asset Management (HK) Limited, a company incorporated in Hong Kong with limited liability indirectly wholly owned by Mr. KM Cheng, licensed to carry on type 4 (advising on securities) and type 9 (asset management) regulated activities under the SFO;

"Placing Agent"	Partners Capital Securities Limited, a company incorporated in Hong Kong with limited liability indirectly wholly owned by Mr. KM Cheng, licensed to carry on type 1 (dealing in securities) regulated activities under the SFO;
"Placing Agreement"	the placing agreement dated 30 July 2014 entered into between the Company and the Placing Agent;
"PRC"	the People's Republic of China;
"Relevant Period"	the period beginning six months prior to 31 July 2014 and up to the Latest Practicable Date;
"RMB"	Renminbi, the lawful currency of the PRC;
"SFC"	the Securities and Futures Commission of Hong Kong;
"SFO"	the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong);
"Share Consolidation"	the proposed share consolidation of every five (5) issued and unissued Existing Shares of HK$0.02 each in the share capital of the Company into one (1) Consolidated Share of HK$0.10 each;
"Share Options"	the 61,700,000 outstanding share options granted pursuant to the share option scheme of the Company adopted on 10 June 2003; and the 210,900,000 outstanding share options granted pursuant to the share option scheme of the Company adopted on 18 September 2008;
"Share Option Schemes"	the share option schemes of the Company adopted on 10 June 2003 and 18 September 2008;
"Shareholders"	holders of the Existing Shares and the Consolidated Shares, where appropriate;
"Sichuan Ko Yo"	四川玖源農資化工有限公司 (Sichuan Ko Yo Agrochem Co., Limited), a wholly-owned subsidiary of the Company, principally engaged in the sale of chemical products including sodium carbonate, ammonia, and chemical fertilisers including urea and ammonium chloride in the PRC;

"Specific Mandate"	the specific mandate to be granted to the Directors by the Independent Shareholders at the EGM to issue and allot the New Shares and the Conversion Shares;
"Stock Exchange"	The Stock Exchange of Hong Kong Limited;
"Subscriber"	Asia Pacific Resources Development Investment Limited, a company incorporated in the British Virgin Islands and is wholly beneficially owned by Mr. KM Cheng, other than the Existing Shares held through PAML, the Subscriber and Mr. KM Cheng are third parties independent of and not connected with the Company and its connected persons;
"Subscription Agreement"	the subscription agreement dated 30 July 2014 (as supplemented by a supplemental agreement dated 29 August 2014) entered into between the Company and the Subscriber in relation to the subscription of New Shares and the Convertible Bonds;
"Takeovers Code"	the Hong Kong Code on Takeovers and Mergers;
"Warrants"	the warrants (from which 187,500,000 Existing Shares will be issued if fully exercised) issued by the Company on 9 July 2012. On 18 September 2014, the Company received a notice of exercise from PAG to exercise in full of all such outstanding warrants and the existing shares pursuant to such exercise of the warrants are to be alloted on 23 September 2014;
"Whitewash Waiver"	a waiver from the Executive in respect of the obligations of the Subscriber and parties acting in concert with it to make a mandatory offer under Rule 26 of the Takeovers Code as a result of the subscription for the New Shares and the Convertible Bonds under the Subscription Agreement pursuant to the Note 1 on dispensation from Rule 26 of the Takeovers Code;
"World Bank Group"	the International Bank for Reconstruction and Development, an international organization established by Articles of Agreement among its member countries;
"%"	per cent.

Ko Yo Chemical (Group) Limited
玖源化工(集團)有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 827)

Executive Directors:-
Mr. Li Weiruo (Chairman)
Mr. Yuan Bai
Ms. Chi Chuan
Ms. Man Au Vivian
Mr. Li Shengdi
Mr. Li Feng
Mr. Li Ciping

Independent non-executive Directors:-
Mr. Hu Xiaoping
Mr. Woo Che-Wor, Alex
Mr. Qian Liaizhong
Mr. Sun Tongchuan

Registered office:-
Cricket Square
Hutchins Drive
P.O. Box 2681
Grand Cayman KY1-1111
Cayman Islands

Principal place of business in Hong Kong:-
Suite No. 02, 31st Floor, Sino Plaza
255-257 Gloucester Road
Causeway Bay
Hong Kong

22 September 2014

To the Shareholders

Dear Sir or Madam,

(I) SHARE CONSOLIDATION
(II) CHANGE IN BOARD LOT SIZE
(III) ISSUE OF NEW SHARES AND CONVERTIBLE BONDS UNDER SPECIFIC MANDATE
(IV) LOAN FINANCING
(V) INCREASE IN AUTHORISED SHARE CAPITAL
(VI) APPLICATION FOR WHITEWASH WAIVER
AND
(VII) NOTICE OF EGM

INTRODUCTION

Reference is made to the Announcement and the announcements by the Company dated 20 August 2014, 25 August 2014 and 19 September 2014 in relation to, among others, the Share Consolidation, the change in board lot size, the issue of New Shares and Convertible Bonds under Specific Mandate, loan financing, increase in authorised share capital and the application for Whitewash Wavier.

The purpose of this circular is to give you, among other things, (a) further details of the Share Consolidation, the Specific Mandate, the Whitewash Waiver, and the increase in the authorised share capital of the Company; (b) the recommendation of the Independent Board Committee to the Independent Shareholders; (c) the letter of advice from the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders in relation to the Specific Mandate and the Whitewash Waiver; and (d) a notice convening the EGM.

SHARE CONSOLIDATION

The Board proposes to implement the Share Consolidation on the basis that every five (5) issued and unissued Existing Shares of HK$0.02 each in the share capital of the Company will be consolidated into one (1) Consolidated Share of HK$0.10 each.

Conditions of the Share Consolidation

The Share Consolidation is conditional on:

(i) the passing of an ordinary resolution by the Shareholders at the EGM to approve the Share Consolidation; and

(ii) the Stock Exchange granting the listing of, and permission to deal in, the Consolidated Shares to be in issue upon the Share Consolidation becoming effective.

Effects of the Share Consolidation

As at the Latest Practicable Date, the authorised share capital of the Company was HK$400,000,000 divided into 20,000,000,000 Existing Shares of HK$0.02 each, of which 7,899,284,615 Existing Shares have been allotted and issued as fully paid or credited as fully paid. Immediately upon the Share Consolidation becoming effective and on the assumption that the Company does not allot, issue or repurchase any Existing Shares from the Latest Practicable Date up to the Effective Date, the authorised share capital of the Company shall become HK$400,000,000 divided into 4,000,000,000 Consolidated Shares of HK$0.10 each, of which 1,579,856,923 Consolidated Shares will be in issue.

Upon the Share Consolidation becoming effective, the Consolidated Shares shall rank *pari passu* in all respects with each other in accordance with the memorandum and articles of association of the Company. Other than the expenses to be incurred in relation to the Share Consolidation, the implementation thereof will not alter the underlying assets, business operations, management or financial position of the Company or the proportionate interests or rights of the Shareholders, save for any fractional Consolidated Share to which may arise.

Listing application

An application will be made by the Company to the Stock Exchange for the listing of, and permission to deal in, the Consolidated Shares to be in issue upon the Share Consolidation becoming effective and those Consolidated Shares which may fall to be issued upon exercise of the Warrants and the Share Options.

No part of the share capital of the Company is listed or dealt in on any other stock exchanges and no such listing or permission to deal is being or is proposed to be sought.

Share capital structure of the Company before and after the Share Consolidation

The following table sets out the effect on the share capital structure of the Company before and immediately after the Share Consolidation, assuming that no further Existing Shares will be issued from the Latest Practicable Date up to the Effective Date:

	Immediately before the Share Consolidation	**Immediately after the Share Consolidation**
Nominal value per share	HK$0.02	HK$0.10
Authorised share capital of the Company	HK$400,000,000 divided into 20,000,000,000 shares of HK$0.02 each	HK$400,000,000 divided into 4,000,000,000 shares of HK$0.10 each
Issued share capital of the Company	HK$157,985,692.3 divided into 7,899,284,615 shares of HK$0.02 each	HK$157,985,692.3 divided into 1,579,856,923 shares of HK$0.10 each

Change in board lot size

The Existing Shares are currently traded on the Stock Exchange in board lot size of 20,000 Existing Shares. Upon the Share Consolidation becoming effective, the board lot size for trading in the Consolidated Shares will change to 4,000 Consolidated Shares.

Based on the closing price of HK$0.37 per Existing Share (equivalent to HK$1.85 per Consolidated Share) as quoted on the Stock Exchange as at the Latest Practicable Date, the board lot value is HK$7,400 in the current board lot size of 20,000 Existing Shares and the board lot value in the proposed new board lot size of 4,000 Consolidated Shares will remain the same at HK$7,400.

The change in board lot size will not, by itself, affect any of the rights of the Shareholders. As from 14 October 2014, the new share certificates will be issued in board lot size of 4,000 Consolidated Shares each (except for odd lots or where the Hong Kong Share Registrar is otherwise instructed).

REASONS FOR THE SHARE CONSOLIDATION AND THE CHANGE IN BOARD LOT SIZE

The Existing Shares were generally trading at a price around HK$0.10. The Board is of the opinion that the Share Consolidation will bring about a corresponding increase in the trading price of the Consolidated Shares and the higher trading price may attract more potential investors. The change in board lot size will maintain the trading amount for each board lot at an optimal level. Accordingly, the Board is of the view that the Share Consolidation and the change in board lot size are in the interest of the Company and the Shareholders as a whole.

Arrangement on odd lot trading

In order to facilitate the trading of odd lots of the Consolidated Shares as a result of the Share Consolidation, the Company appointed Partners Capital Securities Limited to provide matching services, on a best effort basis, to those Shareholders who wish to purchase or to sell their holdings of odd lots of the Consolidated Shares at their own expense to make up a full board lot.

Shareholders who wish to take advantage of this facility should contact Mr. Steven Tang of Partners Capital Securities Limited at telephone number 2157 5429 during office hours. Shareholders should note that successful matching of the sale and purchase of odd lots of the Consolidated Shares is not guaranteed and will depend on, among other things, there being adequate amounts of odd lots of the Consolidated Shares available for such matching.

Shareholders may also make their own arrangements to top-up or sell their holdings of odd lots of the Consolidated Shares at their own expense. For the avoidance of doubt, Shareholders who purchase odd lots of the Consolidated Shares shall pay the relevant purchase price and normal transaction costs for which they are otherwise responsible.

Shareholders are recommended to consult their stockbrokers, other registered dealers in securities, bank managers, solicitors, professional accountants or other independent professional advisers if they are in any doubt about the matching facility described above.

Fractional Consolidated Shares arrangement

Fractional Consolidated Shares arising from Share Consolidation will be aggregated and sold by the Company through the designated broker for the benefit of the relevant registered Shareholders and net proceeds after deduction of all transaction costs will be refunded in cash, on pro rata basis, to the registered Shareholders holding fractional Consolidated Shares and whose names appeared on the register of members of the Company as of the Effective Date.

The Board shall at its absolute discretion sell such aggregated fractional Consolidated Shares at any time within one month from the Effective Date and on such terms as it considers appropriate, provided that the amount of the sale proceeds will exceed the cost and expense of the sale of those fractional Consolidated Shares. Any sum refunded to the relevant registered Shareholders shall be paid not later than 15 Business Days after the Company has received the net sale proceeds. The Hong Kong

Share Registrar will arrange this refund to the relevant registered Shareholders. All refund unclaimed for one year from the payment made will be forfeited and shall revert to the Company. Fractional Consolidated Shares will only arise in respect of the entire shareholding of a holder of the Consolidated Shares regardless of the number of share certificates held by such holder.

Exchange of share certificates

Subject to the Share Consolidation becoming effective, which is expected to be on 14 October 2014, Shareholders may during the business hours, on or after 14 October 2014 until 19 November 2014 (inclusive) submit share certificates for the Existing Shares to the Hong Kong Share Registrar, Union Registrars Limited at 18th Floor, Fook Lee Commercial Centre, Town Place, 33 Lockhart Road, Wanchai, Hong Kong, to exchange, at the expense of the Company, for new share certificates for the Consolidated Shares on the basis of every five (5) Existing Shares for one (1) Consolidated Share, without any fractional Consolidated Share. It is expected that the new certificates for the Consolidated Shares will be available for collection within 10 Business Days after the submission of the existing share certificates for the Existing Shares to the Hong Kong Share Registrar for exchange. Thereafter, certificates for the Existing Shares will be accepted for exchange for new share certificates for the Consolidated Shares only on payment by the Shareholders of a fee of HK$2.50 (or such other amount as may from time to time be specified by the Stock Exchange) per each new certificate to be issued or per each existing certificate to be cancelled. Subject to the Share Consolidation becoming effective, with effect from 14 October 2014, the existing share certificates in blue colour for the Existing Shares will cease to be valid for trading and settlement purpose, but will remain valid and effective as documents of title and trading will only be effected in the Consolidated Shares, the share certificates of which will be issued in red colour.

Adjustments to Warrants and Share Options

As at the Latest Practicable Date, there are:

(a) outstanding Warrants which can be convertible into 187,500,000 Existing Shares upon the exercise of the subscription rights attaching thereto; and

(b) outstanding 272,600,000 Share Options which are convertible into 272,600,000 Existing Shares upon the exercise of the subscription rights attaching thereto.

The Warrants were issued to Asian Equity and PA International and the initial exercise price is HK$0.16. Details of the Warrants are set out in the Company's announcement dated 29 June 2012. On 18 September 2014, the Company received a notice of exercise from PAG whereby PAG exercised the subscription rights attaching to the Warrants to subscribe for 187,500,000 Existing Shares, which are to be allotted and issued on 23 September 2014.

Details of the outstanding Share Options are set out in the paragraph headed "2. Share Capital, Options, Warrants and Convertible Securities — (b) Options, warrant and convertible securities — Share Options" in Appendix II to this circular.

Save as aforesaid, the Company has no other outstanding convertible securities, options or warrants in issue which confer any right to subscribe for, convert or exchange into the Existing Shares as at the Latest Practicable Date.

Pursuant to the terms of the Warrants and the Share Option Schemes, the issue of the New Shares and the Share Consolidation will cause adjustments to the respective conversion prices of the outstanding Warrants and Share Options. The Company will appoint its auditor or a financial adviser to review and certify the basis of such adjustments to the respective conversion prices of the outstanding Warrants and Share Options in accordance with the Listing Rules, the terms of the Warrants and the Share Option Schemes. Further announcement(s) will be made by the Company regarding details of such adjustments (if any) as and when appropriate.

ISSUE OF NEW SHARES AND CONVERTIBLE BONDS UNDER SPECIFIC MANDATE

The Placing Agreement

The Company entered into the Placing Agreement with the Placing Agent on 30 July 2014, pursuant to which the Company has engaged the Placing Agent to act as the placing agent for the private placement of the New Shares and the Convertible Bonds and to introduce subscribers to subscribe for the New Shares and the Convertible Bonds. Under the Placing Agreement, the Company has agreed to pay, on a success basis, the Placing Agent a placement commission of 1.5% of the proceeds of the issue of the New Shares and the Convertible Bonds (amounting to approximately HK$16.32 million). The Placing Agent is indirectly wholly owned by Mr. KM Cheng, who also owns indirectly the entire issued share capital of the Subscriber.

The Placing Agent successfully introduced the Subscriber, the only potential investor expressed interests in subscribing for the New Shares and Convertible Bonds, to the Company. The Company decided to enter into the Subscription Agreement with the Subscriber, the terms of the Subscription Agreement were negotiated between the Company and the Subscriber. The Company is of the view that paying commission to any placing agents for introducing subscribers on success basis is reasonable. The placement commission fee was determined after arm's length negotiation between the Company and the Placing Agent and the Directors considered that the terms of the Placing Agreement are fair and reasonable.

According to the Placing Agent, although both of the Placing Agent and the Subscriber are indirectly beneficially wholly owned by Mr. KM Cheng, they are separate entities. Mr. KM Cheng, who is not a principal of the Placing Agent, does not participate in the daily operation of the Placing Agent. The Placing Agent, being a holder of the licence to carry out type 1 (dealing in securities) regulated activities under the SFO, participated in identifying potential investors to subscribe for the New Shares and Convertible Bonds and it is in the Placing Agent's normal course of business to act as the placing agent of listed companies in their proposed fund raising exercises. The Subscriber is a passive investor introduced to the Company by the Placing Agent whom end up being the only subscriber expressed interests in participating in the proposed financing transaction of the Company and entered into the Subscription Agreement and the Loan Agreement with the Company after arm's length negotiation.

THE SUBSCRIPTION AGREEMENT

Date

30 July 2014 (as supplemented by a supplemental agreement dated 29 August 2014)

Parties

Issuer : the Company

Subscriber : Asia Pacific Resources Development Investment Limited

Pursuant to the Subscription Agreement, the Subscriber conditionally agrees to subscribe and the Company conditionally agrees to allot and issue to the Subscriber (a) the 800,000,000 New Shares at an issue price of HK$0.32 per New Share; and (b) the Convertible Bonds of a principal amount of HK$832,000,000. The aggregate consideration for the proposed subscription of the New Shares and the Convertible Bonds, being HK$1,088,000,000, shall be payable by the Subscriber in cash upon completion of the Subscription Agreement.

Conditions

Completion of the transactions under the Subscription Agreement is subject to, among others, the following conditions precedent:

(a) the passing of a resolution at the EGM approving the Share Consolidation and the Share Consolidation becomes unconditional;

(b) the Subscriber has notified the Company that it accepts the due diligence results of the members of the Group in aspects including financial, operation, taxation and assets;

(c) the listing status of the Consolidation Shares has not been revoked or objected by the Stock Exchange or the SFC as a result of the transactions under the Subscription Agreement;

(d) the passing of the following resolution(s) by the Independent Shareholders at the EGM approving:

   (i) the Specific Mandate; and the Subscription Agreement and the transactions contemplated under the Subscription Agreement,

   (ii) the Whitewash Waiver,

(e) the Executive having granted the Whitewash Waiver;

(f) the listing committee of the Stock Exchange having approved the listing of, and permission to deal in, the New Shares and the Conversion Shares and such approval not having been revoked;

(g) the warranties under the Subscription Agreement remain true and accurate and not misleading;

(h) the Company having fully complied with its obligations, covenants and undertakings under the Subscription Agreement;

(i) save as previously disclosed by the Company, there having no material adverse change in the business, operation or financial status of any member of the Group;

(j) no order, judgment, restrictions or decisions having been made, promulgated or adopted by judicial or governmental authority or regulatory authority to restrict or prohibit the transactions under the Subscription Agreement;

(k) no proceedings having been initiated or threatened by any third parties with any judicial or governmental authority in any jurisdictions to restrict or prohibit the transactions under the Subscription Agreement, declare the transactions under the Subscription Agreement illegal or seek for a remedy of a material nature;

(l) all consents and approvals (if any) from third parties which are considered as necessary for the subscription of the New Shares and the Convertible Bonds having been obtained in form and substance to the satisfaction of the Subscriber and such consents and approvals remain valid;

(m) the signing of an undertaking by the Company and the Subscriber whereby, upon completion of the Subscription Agreement, the Subscriber is entitled by written notice to the Company to nominate a director to the Board; and

(n) the Company and the Subscriber having obtained all consents and approvals necessary for consummation of the transactions contemplated by the Subscription Agreement and such consents and approvals remain valid on the completion of the Subscription Agreement and the relevant authority having not promulgated any rules or regulations which prohibit or materially delay the execution of the Subscription Agreement.

Save for the conditions referred to in paragraphs (a), (c), (d)(i), (f) and (k) above, the other conditions can be waived by the Subscriber. If the Subscriber waives the condition referred to in paragraphs (d)(ii) and (e) above, it will comply with the provisions of the Takeovers Code including but not limited to the making of a general offer under Rule 26.1 of the Takeovers Code. The Company undertakes to use its best endeavor to procure the fulfilment of the condition referred to in paragraphs (a), (c), (d)(i), (f) and (m) above as soon as possible. In the event any of the conditions are not fulfilled or waived by the earlier of (a) 31 January 2015; or (b) one month after the EGM, the Subscription Agreement shall automatically be terminated and of no effect on the parties thereto and the transactions contemplated under the Subscription Agreement will not proceed.

The New Shares

Assuming the Share Consolidation has become effective and there is no change in the issued share capital of the Company or exercise of the Warrants and Share Options other than the Share Consolidation from the Latest Practicable Date and up to the completion of the Subscription Agreement, the New Shares will represent (i) approximately 50.6% of the Consolidated Shares in issue; (ii) approximately 33.6% of the Consolidated Shares in issue as enlarged by the issue of the New Shares; and (iii) approximately 16.1% of the Consolidated Shares in issue as enlarged by the issue of the New Shares and the Conversion Shares.

The New Shares will be issued free from any encumbrances or third party rights of any kind and upon issue will rank *pari passu* in all respects with each other and with the Consolidated Shares in issue in accordance with the memorandum and articles of association of the Company.

An application will be made by the Company to the Stock Exchange for the listing of, and permission to deal in, the New Shares.

The Convertible Bonds

The principal term of the Convertible Bonds are summarized as follows:

Principal amount:	HK$832,000,000
Issue price:	100% of the principal amount
Conversion Price:	HK$0.32 per Conversion Share, subject to adjustment events of (i) share consolidation or share subdivision or reclassification of shares; (ii) issue any shares credited as fully paid by way of capitalisation of profits or reserves; (iii) issue of shares in lieu of a cash dividend; (iv) capital distribution; (v) offer to holders of shares of the Company new shares for subscription by way of rights issue, or grant to holders of shares of the Company any rights to subscribe for new shares; (vi) issue any shares or grant any rights to subscribe for new shares at a price per new share which is less than 80% of the market price; or (vii) issue any securities which by their terms are convertible into or exchangeable for or carry rights to acquire or subscribe for new shares at a price per new share which is less than 80% of the market price. The term "market price" refers to the average of the closing prices of shares of the Company on the Stock Exchange in the five trading days preceding the day on or as of which the market price is to be ascertained. The Directors confirmed that the exercise of the subscription rights attaching to the Warrants and the Share Options will not trigger an adjustment to the Conversion Price.

Interest rate:	7% per annum
Issue date:	Date of completion of the Subscription Agreement
Maturity date:	The tenth anniversary from the date of issue
Conversion period:	The Convertible Bonds are convertible in whole or in part by the Bondholder at any time from the issue date to the business day immediately preceding the maturity date of the Convertible Bonds.
Conversion Shares:	The Conversion Shares will be issued free from any encumbrances or third party rights of any kind and upon issue will rank *pari passu* in all respects with each other and with the New Shares in issue in accordance with the memorandum and articles of association of the Company. Based on the initial Conversion Price of HK$0.32 per Conversion Share, subject to adjustments, a maximum number of 2,600,000,000 Conversion Shares will be allotted and issued upon exercise of the conversion rights attached to the Convertible Bonds in full, which, assuming the Share Consolidation becoming effective and there is no change in the issued share capital of the Company or exercise of the Warrants and Share Options other than the Share Consolidation from the Latest Practicable Date up to the completion of the Subscription Agreement, represent: (i) approximately 164.6% of the Consolidated Shares in issue; (ii) approximately 109.3% of the Consolidated Shares in issue as enlarged by the issue of the New Shares; and (iii) approximately 52.2% of the Consolidated Shares in issue as enlarged by the issue of the New Shares and the Conversion Shares.
Ranking of the Convertible Bonds:	The Convertible Bonds constitute general and unsecured obligations of the Company and rank (subject to any obligations preferred by mandatory provisions of law) equally and without any reference amongst themselves.
Transferability:	Subject to the Listing Rules, the grant of approval for the listing and permission to deal in the Conversion Shares and other relevant approvals and requirements, the Convertible Bonds are freely transferable by the Bondholders.

Redemption by the Company:	On the maturity date, the Company will redeem all the outstanding amount of the Convertible Bonds at a redemption amount equal to 100% of the principal amount of the Convertible Bonds together with the outstanding interest accrued thereon.
Event of default:	If any event of default set out in the terms and conditions of the Convertible Bonds occurs, the Bondholder may give notice to the Company that the Convertible Bonds together with the interest accrued thereon will become immediately due and payable.
Voting rights at general meeting:	The Bondholder shall not be entitled to attend or vote at general meeting of the Company by reason only of it being a Bondholder.
Listing:	No application will be made for a listing of the Convertible Bonds on any stock exchange. An application will be made by the Company to the Stock Exchange for the listing of, and permission to deal in, the Conversion Shares to be issued upon the exercise of the conversion rights attached to the Convertible Bonds.
Other:	No Conversion Shares will be issued if the public float of the Company will fall below 25% after such issue.

The issue price of the New Shares and the Conversion Price

The issue price of the New Shares of HK$0.32 per New Share and the initial Conversion Price of HK$0.32 per Conversion Share were determined and agreed after arm's length negotiations between the Company and the Subscriber, taking into account the Group's existing financial position, liquidity of the Existing Shares in the market and the recent trading prices of the Existing Shares.

The issue price of the New Shares of HK$0.32 per New Share and the initial Conversion Price of HK$0.32 per Conversion Share represent:

(a) a discount of approximately 82.7% to the adjusted closing price per Consolidated Share of HK$1.85 based on the closing price of HK$0.37 per Existing Share as quoted on the Stock Exchange on 19 September 2014, being the Latest Practicable Date and adjusted for the effect of the Share Consolidation;

(b) a discount of approximately 41.8% to the adjusted closing price per Consolidated Share of HK$0.55 based on the closing price of HK$0.11 per Existing Share as quoted on the Stock Exchange on 28 July 2014, being the Last Trading Day and adjusted for the effect of the Share Consolidation;

(c) a discount of approximately 28.3% to the average of the adjusted closing prices per Consolidated Share of HK$0.446 based on the average of the closing prices of approximately HK$0.089 per Existing Share as quoted on the Stock Exchange for the five consecutive trading days ended on the Last Trading Day.

(d) a discount of approximately 25.4% to the average of the adjusted closing prices per Consolidated Share of HK$0.429 based on the average of the closing prices of approximately HK$0.086 per Existing Share as quoted on the Stock Exchange for the ten consecutive trading days ended on the Last Trading Day; and

(e) a discount of approximately 65.59% to the Group's adjusted audited consolidated net asset per Consolidated Share as at 31 December 2013 of approximately HK$0.930, based on the audited consolidated net asset per Existing Share of HK$0.186 as at 31 December 2013 and a total of 1,439,056,923 Consolidated Shares as at the date of the Subscription Agreement (assuming the Share Consolidation has become effective) and the Group's audited consolidated net asset value attributable to owners of the Company of approximately RMB1,069,032,000 as at 31 December 2013.

Completion

Completion for the subscription of the New Shares and the Convertible Bonds shall take place on the tenth (10th) Business Day after the date on which the conditions precedents to the Subscription Agreement are satisfied or waived or such other date as the Company and the Subscriber may agree.

SPECIFIC MANDATE

The New Shares and the Convertible Bonds shall be issued pursuant to the Specific Mandate to be granted to the Directors which will be sought from the Independent Shareholders who are permitted to vote in the EGM.

EFFECT ON SHAREHOLDING OF THE COMPANY FOLLOWING COMPLETION OF THE ISSUE OF NEW SHARES AND THE CONVERSION SHARES

The shareholding structure of the Company before and after the issue of the New Shares and the Conversion Shares are and will be as follows:

(a) **Assuming the Warrants and the Share Options have not been exercised**

	As at the Latest Practicable Date *(Note 6)*		Upon Share Consolidation		Upon issue of New Shares		Upon full exercise of the conversion rights attached to the Convertible Bonds	
	Existing Shares	*%*	*Consolidated Shares*	*%*	*Consolidated Shares*	*%*	*Consolidated Shares*	*% (for illustration) (note 5)*
Mr. Li (and persons acting in concert with him)	2,924,440,000	37.02	584,888,000	37.02	584,888,000	24.58	584,888,000	11.75
Other executive Directors (Note 1)	460,424,000	5.83	92,084,800	5.83	92,084,800	3.87	92,084,800	1.85
IFC (Note 3)	414,724,615	5.25	82,944,923	5.25	82,944,923	3.49	82,944,923	1.67
Subscriber (and persons acting in concert with it)	3,180,000	0.04	636,000	0.04	800,636,000	33.64	3,400,636,000	68.29
PAG (Note 4)	192,700,000	2.44	38,540,000	2.44	38,540,000	1.62	38,540,000	0.77
Public (Note5)	3,903,816,000	49.42	780,763,000	49.42	746,931,200	32.80	780,763,000	15.67
Total:	7,899,284,615	100	1,579,856,923	100	2,379,856,923	100	4,979,856,923	100

(b) **Assuming the Warrants and Share Options have been exercised in full as at the Latest Practicable Date**

	As at the Latest Practicable Date *(Note 6)*		Upon Share Consolidation		Upon issue of New Shares		Upon full exercise of the conversion rights attached to the Convertible Bonds	
	Existing Shares	*%*	*Consolidated Shares*	*%*	*Consolidated Shares*	*%*	*Consolidated Shares*	*% (for illustration) (note 5)*
Mr. Li (and persons acting in concert with him) (Note 2)	2,930,940,000	35.06	586,188,000	35.06	586,188,000	23.71	586,188,000	11.56
Other executive Directors (Note 1, 2)	584,524,000	6.99	116,904,800	6.99	116,904,800	4.73	116,904,800	2.30
IFC (Note 3)	414,724,615	4.96	82,944,923	4.96	82,944,923	3.36	82,944,923	1.64
Subscriber (as persons acting in concert with it)	3,180,000	0.04	636,000	0.04	800,636,000	32.39	3,400,636,000	67.05
PAG (Note 4)	380,200,000	4.55	76,040,000	4.55	76,040,000	3.08	76,040,000	1.50
Public (Note 5)	4,045,816,000	48.40	809,163,200	48.40	809,163,200	32.73	809,163,200	15.95
Total:	8,359,384,615	100	1,671,876,923	100	2,471,876,923	100	5,071,876,923	100

Note 1: As at the Latest Practicable Date, the 460,424,000 Existing Shares are held as to 366,464,000 Existing Shares by Mr. Yuan Bai, 62,640,000 Existing Shares by Ms. Chi Chuan and 31,320,000 Existing Shares by Ms. Man Au Vivian.

Note 2: Mr. Li has 6,500,000 Share Options, Mr. Yuan Bai has 17,000,000 Share Options, Mr. Chi Chuan has 23,000,000 Share Options, Ms. Man Au Vivian has 23,000,000 Share Options, Mr. Li Shengdi has 25,000,000 Share Options, Mr. Li Ciping has 12,000,000 Share Options, Mr. Hu Xiaoping has 6,000,000 Share Options, Mr. Woo Che-wor, Alex has 6,000,000 Share Options, Mr. Qian Laizhong has 6,100,000 Share Options and Mr. Sun Tongchuan has 6,000,000 Share Options.

Note 3: IFC, a member of the World Bank Group, is the largest global development institution focused exclusively on the private sector. Currently IFC is also a creditor of the Group.

Note 4: PA International Opportunity VII Limited, is a company limited by shares incorporated in the British Virgin Islands and is wholly owned by Pacific Alliance Asia Opportunity Fund L.P. (acting through its general partner, Pacific Alliance Group Asset Management Limited), a fund managed by PAG (formerly known as the Pacific Alliance Group), one of Asia's largest Asia-focused fund managers with offices across Asia including Hong Kong, Shanghai, Beijing and Tokyo and each of them is principally engaged in the business of investment holding.

Note 5: Since no Conversion Shares will be issued if the public float will fall below 25% after such issue, the shareholding percentages in this column are for illustration purpose only.

Note 6: On 18 September 2014, the Company received a notice of exercise from PAG whereby PAG exercised the subscription rights attaching to the Warrants to subscribe for 187,500,000 Existing Shares (the "**Warrant Shares**"). Such Warrant Shares will be allotted and issued on 23 September 2014. Upon the allotment of such Warrant Shares, the issued share capital of the Company will be 8,086,784,615 Existing Shares and there are no outstanding Warrants.

The issue of the New Shares and full conversion of the Convertible Bonds will trigger an obligation on the Subscriber and persons acting in concert with it under the Takeovers Code to make a general offer for all the securities of the Company other than those already owned or agreed to be acquired by them, unless the Whitewash Waiver is granted by the Executive and approved by the Independent Shareholders at the EGM by poll. The Subscriber has made an application to the Executive for the Whitewash Waiver.

Details of the implications under the Takeovers Code are set out in the sub-section headed "Implications under the Takeovers Code" in the section headed "Letter from the Board" of this circular.

Apart from Mr. Li's undertaking as state in the sub-section headed "Undertaking by Mr. Li" in the section headed "Letter from the Board" of this circular, the other Directors who have beneficial shareholdings in the Company intend not to accept the offer in the event that the Subscriber makes a mandatory general offer for all the securities of the Company.

The Directors note that upon full conversion of the Convertible Bonds, the public float of the Company will fall below 25%. The Company and the Subscriber will monitor the public float when exercise the conversion rights attaching to the Convertible Bonds so that the public float requirements under Rule 8.08(1)(a) of the Listing Rules will always be complied with. The Company and the Subscriber will take appropriate measures to ensure the compliance with the public float requirement at all times. These measures include (a) not to issue any Conversion Shares if the public float of the Company will fall below 25% after such issue; (b) the Subscriber may place down its Consolidated

Shares to Independent Third Parties; (c) Mr. Li and Mr. Yuan Bai may place down their Consolidated Shares to Independent Third Parties; (d) a placing of new Consolidated Shares to Independent Third Parties; and (e) a combination of the above. Notwithstanding the above measure, the terms and conditions of the Convertible Bonds will include a provision that no Conversion Shares would be issued if the public float will fall below 25% after such issue.

THE LOAN AGREEMENT

Date

30 July 2014

Parties

Lender: the Subscriber

Borrower: the Company

Principal amount and interest rate

HK$200,000,000 interest free

Term

10 August 2014 to 31 January 2015

Security

The loan is secured by 100% equity interest in Sichuan Ko Yo and a personal guarantee given by Mr. Li.

Others

A default interest rate of 10% per annum will be imposed on any default amount. Upon the occurrence of an event of default, the Loan will become immediately due and payable. The Loan may be advanced by the Subscriber's subsidiary or affiliate to any of the Company's wholly-owned subsidiary if it is so directed by the Subscriber and the Company, respectively.

As of 11 August 2014, the Company has received the principal amount of HK$200,000,000 pursuant to the Loan Agreement.

FUND RAISING ACTIVITIES IN THE PAST TWELVE MONTHS

The Company had not conducted any other equity fund raising activities in the past twelve months immediately preceding the Latest Practicable Date.

REASONS FOR THE ISSUE OF NEW SHARES AND THE CONVERTIBLE BONDS AND THE ENTERING INTO THE LOAN AGREEMENT

The Company was incorporated in the Cayman Islands with limited liability. The Company is an investment holding company and its subsidiaries are principally engaged in research and development, manufacture, marketing and distribution of chemical products, chemical fertilizers and bulk blending fertilizers.

The estimated net proceeds of the issue of the New Shares and the Convertible Bonds and the Loan (after deduction of commissions, professional fees and other administrative expenses of a total of approximately HK$18.95 million) will be approximately HK$1.02 billion, which will strengthen the Company's financial position and help to renew its existing bank loans up to an outstanding principal amount of RMB478.4 million and the net proceeds will be used as working capital of the Group in respect of (i) the Guangan Factory which recently launched production, (ii) any possible new project, and (iii) general working capital. Those loans to be renewed originally will be matured from September 2014 to January 2015.

The Company currently intends to apply the net proceeds from the issue of New Shares and the Convertible Bonds as to:

(i) approximately HK$420.0 million for the first phase of the expansion project of the Guangan Factory;

(ii) approximately HK$380 million for possible new projects, including as to (aa) approximately HK$180.0 million for second phase of the Group's Dazhou plant; (bb) approximately HK$125.0 million to finance the construction of a new phosphoric acid plant; and (cc) approximately HK$75.0 million for new materials (Polyphenylene Sulfide) project; and

(iii) approximately HK$200.0 million as general working for the Group.

Details of the new projects have been disclosed in the latest financial results of the Company.

The Directors confirmed that the Company has not changed its business strategy or plans as disclosed in the latest financial results.

The Directors consider that the proceeds from the issue of New Shares and Convertible Bonds will improve the cash position of the Company and strengthen its equity base, which allow the Company to ask for a lower interest rate from the existing lending banks as interest rate reflects the risk premium of lending. The Company will then be in a better position to request its existing lending banks to renew existing loans at lower interest rate.

If existing banks are unable to offer a competitively lower interest rate, the Company will raise new loans from those other banks to repay existing facilities. Existing banks may also raise their credit limit whilst offer a lower interest rate. In such case, the Company will also be able to enjoy a lower interest rate as well.

The Group currently owes a loan in the sum of US$6.0 million to IFC which is to be repaid in 2017. The Company has no current intention to use the proceeds from the issue of the New Shares and the Convertible Bonds and the Loans to repay the loan from IFC before 2017 since (i) for early repayment of the IFC loan, the Company will be required to pay an early repayment charge and (ii) as the Company intends to apply such proceeds to facilitate the renewal of part of its existing bank loans at a lower interest rate, where those bank loans are generally having an effective interest rate of over 9%, which is higher than that of the IFC loan, so early repayment of such IFC loan provides less financial benefit to the Company.

Saved as disclosed for IFC, the Group's existing creditor banks are not existing Shareholders of the Company.

The Directors currently intend to use the loan amount of HK$200 million advanced to the Group under the Loan Agreement to finance the construction and as working capital of the Guangan Factory for its commencement of production. The Directors consider that the Loan Agreement provide additional financing facilities to the Company and can help to renew part of its existing loans so that a lower interest rate can be secured. The Directors have considered other capital market fund raising methods, including bank loans and issue of equity and/or convertible debt instruments. However, in view of the recent business performance of the Company (loss making for the first half of 2014) and existing debt level of the Company, no additional assets can be pledged to obtain financing and to minimize interest expenses, such financing options are not considered.

Despite that the New Shares and the Convertible Bonds will be issued at a deep discount, the Directors are of the view that this exercise raises additional capital that is sufficient to meet the Company's financial needs at a reasonable cost. The Directors (including the Independent Board Committee, whose opinion are set forth in the letter from the Independent Board Committee on pages 29 to 30 of this circular after considering the advice of the Independent Financial Adviser as to the fairness and reasonableness of the terms of the Subscription Agreement and the Whitewash Waiver) are of the view that the issue of the New Shares and the Convertible Bonds offer a good opportunity to raise additional capital for the Company and to strengthen the financial position of the Company.

Accordingly, the Directors (including the Independent Board Committee, whose opinion are set forth in the letter from the Independent Board Committee on pages 29 to 30 of this circular after considering the advice of the Independent Financial Adviser as to the fairness and reasonableness of the terms of the Subscription Agreement and the Whitewash Waiver) consider that (i) the entry into the Subscription Agreement and the transactions contemplated thereunder and the issue of the New Shares and the Convertible Bonds are in the interests of the Company and the Shareholders as a whole; and (ii) all the relevant terms of the Subscription Agreement, the Loan Agreement and the issue of the New Shares and the Convertible Bonds are fair and reasonable.

INFORMATION ON THE SUBSCRIBER

The Subscriber is an investment holding company incorporated in the British Virgin Islands wholly beneficially owned by Mr. KM Cheng. Mr. KM Cheng is a businessman and a Hong Kong permanent resident. Mr. KM Cheng is also one of the substantial shareholders holding approximately 26.4% interests of Shunfeng Photovoltaic International Limited (Stock code 1165) as at the Latest

Practicable Date, the shares of which are listed on the main board of the Stock Exchange. As at the Latest Practicable Date, PAML, a company indirectly wholly owned by Mr. KM Cheng and acting in concert of the Subscriber, beneficially holds 3,180,000 Existing Shares. PAML being a company engaged in the business of asset management, also holds another 6,000,000 Existing Shares for its clients under discretionary account in its ordinary course of business.

INTENTION OF THE SUBSCRIBER

It is the intention of the Subscriber that the Group will continue its current business. The Subscriber has no intention to make any major changes to the business or employment of the employees of the Group or redeploy the fixed assets of the Group. Save and except that the Subscriber will be entitle to nominate a director to the Board upon completion of the Subscription Agreement, the Subscriber not be able to nominate directors to the Company, other than as in its capacity as a Shareholder in accordance with the articles of association of the Company in the event of it holding the New Shares, and where applicable the Conversion Shares.

IMPLICATIONS UNDER THE TAKEOVERS CODE

Whitewash Waiver

Upon the issue of the New Shares and full conversion of the Convertible Bonds, assuming that there is no other change in the issued share capital of the Company, the Subscriber will be interested in aggregate 3,400,636,000 Consolidated Shares, representing approximately 215.25% of the Consolidated Shares in issue upon the Share Consolidation has become effective, and approximately 68.29% of the Consolidated Shares in issue as enlarged by the issuance of the New Shares and the Conversion Shares.

Under Rule 26 of the Takeovers Code, the acquisition of voting rights from less than 30% of voting rights to 30% or more will trigger an obligation on the Subscriber and persons acting in concert with it to make a general offer for all the securities of the Company other than those already owned or agreed to be acquired by them, unless the Whitewash Waiver is granted by the Executive and approved by the Independent Shareholders at the EGM by way of poll.

The Subscriber has made an application to the Executive for the Whitewash Waiver in respect of the Subscription Agreement and the allotment and issue of the Conversion Shares upon full conversion of the Convertible Bonds. The Whitewash Waiver will be subject to, among other things, approval by the Independent Shareholders at the EGM by way of poll.

If the Whitewash Waiver is approved by the Independent Shareholders, the shareholding of the Subscriber in the Company upon the issue of the New Shares and the Conversion Shares to the Subscriber will exceed 50%. The Subscriber may further increase its shareholdings in the Company without incurring any further obligations under Rule 26 of the Takeovers Code to make a general offer.

None of the Subscriber and persons acting in concert with it has acquired or disposed of or entered into any agreement or arrangement to acquire or dispose of any voting rights in the Company during the six months period prior to the date of the holding announcement of the Company dated 31

July 2014. Save as the 3,180,000 Existing Shares held by PAML as beneficial owner and the 6,000,000 Existing Shares held under discretionary account, none of the Subscriber and persons acting in concert with it are interested in any issued Existing Shares or other relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) of the Company as at the Latest Practicable Date.

As at the Latest Practicable Date, save for the Subscription Agreement and the 3,180,000 Existing Shares beneficially held by PAML and the 6,000,000 Existing Shares held by PAML for its clients under discretionary account, (a) the Subscriber and persons acting in concert with it do not hold, control or have direction over any outstanding options, warrants, or any securities that are convertible into Existing Shares or any derivatives in respect of securities in the Company, or hold any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company; (b) the Subscriber and persons acting in concert with it did not borrow or lend any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company; (c) there is no arrangement referred to in Note 8 to Rule 22 of the Takeovers Code (whether by way of option, indemnity or otherwise) in relation to the relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) of the Company or of the Subscriber which might be material to the Subscription Agreement and the Whitewash Waiver; (d) there is no agreement or arrangement to which any of the Subscriber or persons acting in concert with it is a party which relates to circumstances in which it may or may not invoke or seek to invoke a pre-condition or a condition to the Subscription Agreement and the Whitewash Waiver; and (e) none of the Subscriber or persons acting in concert with it has received any irrevocable commitment to vote for or against the Subscription Agreement or the Whitewash Waiver.

Subscriber's reservation of rights to waive the Whitewash Waiver

The grant and approval of the Whitewash Waiver is condition precedent to the completion of the Subscription Agreement. In the case where the Subscription Agreement is approved by the Independent Shareholders in the EGM and the Whitewash Waiver is not granted or approved by the Independent Shareholders, the Subscriber reserves its right as to whether or not to waive such condition. If the Subscriber waives such condition, it will comply with the provisions of the Takeovers Code to make a general offer under Rule 26.1 of the Takeovers Code.

Undertaking by Mr. Li

As at the Latest Practicable Date, Mr. Li is interested in 2,924,440,000 Existing Shares, representing approximately 37.02% of the Existing Shares in issue. Mr. Li has undertaken to the Subscriber that in the event that the Subscriber makes a mandatory general offer for all the securities of the Company other than those already owned or agreed to be acquired by them under Rule 26 of the Takeovers Code, he will not accept or procure the acceptance of such offer for the securities in the Company he holds.

INCREASE IN AUTHORISED SHARE CAPITAL

In order to accommodate the issue of the New Shares and the Conversion Shares and to provide additional flexibility to the Company, the Board proposes to increase the authorised share capital of the Company from HK$400,000,000 divided into 4,000,000,000 Consolidated Shares to

HK$800,000,000 divided into 8,000,000,000 Consolidated Shares by the creation of an additional 4,000,000,000 Consolidated Shares. This proposed increase in the authorised share capital of the Company is subject to and conditional upon (a) the Share Consolidation becomes effective; and (b) the approval of the Shareholders by passing an ordinary resolution at the EGM.

GENERAL

The Independent Board Committee, comprising all the independent non-executive Directors, namely Mr. Hu Xiaoping, Mr. Woo Che-Wor, Alex, Mr. Qian Laizhong and Mr. Sun Tongchuan, has been formed to advise the Independent Shareholders as to the fairness and reasonableness of the terms of the Subscription Agreement and the Whitewash Waiver and as to voting after taking into account the advice from the Independent Financial Adviser. Octal Capital Limited has been approved by the Independent Board Committee and appointed by the Company as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders as to the fairness and reasonableness of the terms of the Subscription Agreement and the Whitewash Waiver.

EGM

Set forth on pages 169 to 171 of this circular is a notice convening the EGM to be held at 11:00 a.m., on Monday, 13 October 2014 at Suite No. 02, 31st Floor, Sino Plaza, 255-257 Gloucester Road, Causeway Bay, Hong Kong at which ordinary resolutions will be proposed to approve, among other things, (a) the Share Consolidation and increase in authorised share capital, and (b) the Specific Mandate, the Subscription Agreement and the Whitewash Waiver.

The voting in relation to the Share Consolidation and increase in authorised share capital, the Specific Mandate, the Subscription Agreement and the Whitewash Waiver will be conducted by way of poll whereby the Subscriber, Mr. Li and Mr. Yuan Bai and their respective concert parties will abstain from voting on the resolution in relation to the Subscription Agreement, the transactions contemplated thereunder, the Specific Mandate and the Whitewash Waiver, as the Subscriber is interested in, and Mr. Li and Mr. Yuan Bai were involved in discussions and meetings with the Placing Agent and meetings and negotiations with Mr. KM Cheng in relation to the Subscription Agreement, PAML, which beneficially holds 3,180,000 Existing Shares and another 6,000,000 Existing Shares under discretionary account, will abstain from voting in the EGM. To the best knowledge, information and belief of the Directors having made all reasonable enquiries, no Shareholder will be required to abstain from voting on the resolution in relation to the Share Consolidation and increase in authorised share capital.

As at the Latest Practicable Date, the issued share capital of the Company was 7,899,284,615 Existing Shares of HK$0.02 each, 272,600,000 Share Options and Warrants (from which 187,500,000 Existing Shares will be issued if fully exercised) in issue. The Company had no other class of relevant securities (as defined under Note 4 to Rule 22 of the Takeovers Code) in issue in accordance with the Takeovers Code.

Associates of the Company (as defined in the Takeovers Code including a person who owns or controls 5% or more of any class of relevant securities of the Company or any person who as a result of any transaction owns or controls 5% or more of any class of relevant securities of the Company) are reminded to disclose their dealings in the relevant securities (as defined under Note 4 to Rule 22 of the Takeovers Code) of the Company.

A form of proxy for use at the EGM is enclosed with this circular. Whether or not you are able to attend the EGM, you are requested to complete and return the accompanying form of proxy in accordance with the instructions printed thereon as soon as practicable and in any event not less than 48 hours before the time fixed for holding the EGM (or any adjournment thereof) to the office of the Company's branch share registrar in Hong Kong, Union Registrars Limited, 18th Floor, Fook Lee Commercial Centre, Town Place, 33 Lockhart Road, Wanchai, Hong Kong. Completion and return of the form of proxy will not preclude you from attending and voting in person at the EGM or any adjournment thereof should you so wish and in such event, the instrument appointing a proxy shall be deemed to be revoked.

Shareholders and potential investors should note that the Subscription Agreement is subject to the fulfillment and waive of certain conditions and may or may not proceed. Shareholders and potential investors are reminded to exercise caution when dealings in the shares of the Company.

RECOMMENDATION

The Directors (including the independent non-executive Directors after taking the advice of the Independent Financial Adviser) consider that the terms of the Subscription Agreement and the Whitewash Waiver are fair and reasonable and in the interests of the Company and the Independent Shareholders as a whole, and recommend the Independent Shareholders to vote in favour of the relevant resolutions to be proposed at the EGM.

The Independent Shareholders are strongly advised to consider the "Letter from the Independent Board Committee" set out on pages 29 to 30 of this circular which contains the recommendation of the Independent Board Committee to the Independent Shareholders in respect of the terms of the Subscription Agreement and the Whitewash Waiver, and the "Letter from the Independent Financial Adviser" set out on pages 31 to 65 this circular which contains the recommendation and opinions of the Independent Financial Adviser in respect of the terms of the Subscription Agreement and the Whitewash Waiver and the principal factors and reasons taken into consideration before deciding to vote in favour of or against the resolutions to be proposed at the EGM.

ADDITIONAL INFORMATION

Your attention is drawn to the information as set out in the appendices to this circular and the notice of the EGM.

Yours faithfully,
For and on behalf of the Board
Ko Yo Chemical (Group) Limited
Li Wei Ruo
Chairman

The following is the text of the letter from the Independent Board Committee setting out its recommendation to the Independent Shareholders in relation to the Subscription and the Whitewash Waiver:

Ko Yo Chemical (Group) Limited
玖源化工(集團)有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 827)

22 September 2014

To the Independent Shareholders

Dear Sir or Madam,

(I) ISSUE OF NEW SHARES AND CONVERTIBLE BONDS UNDER SPECIFIC MANDATE AND (II) APPLICATION FOR WHITEWASH WAIVER

INTRODUCTION

We refer to the circular of the Company dated 22 September 2014 (the "**Circular**"), of which this letter forms part. Terms used herein have the same meanings as those defined in the Circular unless otherwise specified.

We have been appointed by the Board to form the Independent Board Committee to advise the Independent Shareholders as to: (i) whether the terms of the Subscription Agreement and the Whitewash Waiver are fair and reasonable so far as the Independent Shareholders are concerned; (ii) whether the terms of the Subscription Agreement and the Whitewash Waiver are in the interests of the Company and the Shareholders as a whole; and (iii) whether the Independent Shareholders should vote in favour of the resolutions to approve the Subscription Agreement and the Whitewash Waiver at the EGM.

Octal Capital Limited has been appointed the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders to opine on: (i) whether the terms of the Subscription Agreement and the Whitewash Waiver are fair and reasonable so far as the Independent

Shareholders are concerned; (ii) whether the terms of the Subscription Agreement and the Whitewash Waiver are in the interests of the Company and the Shareholders as a whole; and (iii) whether the Independent Shareholders should vote in favour of the resolutions to approve the Subscription Agreement and the Whitewash Waiver at the EGM.

We wish to draw your attention to the letter from the Independent Financial Adviser set out on pages 31 to 65 of the Circular which contain, among other things, its advice and recommendations regarding the Subscription Agreement and the Whitewash Waiver and the principal factors and reasons taken into consideration for its advice and recommendations.

We also wish to draw your attention to the letter from the Board set out on pages 8 to 28 of the Circular and the additional information set out in the appendices to the Circular.

RECOMMENDATION

Having taken into account the advice and recommendations of the Independent Financial Adviser and the principal factors and reasons taken into consideration by it in arriving at its opinion, we consider that the Subscription Agreement and the Whitewash Waiver are fair and reasonable so far as the Independent Shareholders are concerned and the Subscription Agreement and the Whitewash Waiver are in the interests of the Company and the Shareholders as a whole. Accordingly, we recommend the Independent Shareholders to vote in favour of the relevant resolutions to be proposed at the EGM to approve the Subscription and the Whitewash Waiver.

Yours faithfully,
For and on behalf of
the Independent Board Committee of
Ko Yo Chemical (Group) Limited

Mr. Hu Xiaoping **Mr. Woo Che-Wor, Alex** **Mr. Qian Laizhong** **Mr. Sun Tongchuan**
Independent non-executive Directors

The following is the text of the letter of advice from the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders in respect of the Subscription Agreement and the Whitewash Waiver for the purpose of incorporation into this circular.

八方金融有限公司
OCTAL Capital Limited

Octal Capital Limited
801-805, 8th Floor, Nan Fung Tower
88 Connaught Road Central
Hong Kong

22 September 2014

To the Independent Board Committee
and Independent Shareholders

Dear Sirs,

ISSUE OF NEW SHARES AND CONVERTIBLE BONDS UNDER SPECIFIC MANDATE AND APPLICATION FOR WHITEWASH WAIVER

INTRODUCTION

We refer to our engagement as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in respect of the Subscription Agreement and the transactions contemplated thereunder (the "**Subscription**") and the Whitewash Waiver**,** details of which are set out in the letter from the Board (the "**Letter from the Board**") contained in the circular (the "**Circular**") of the Company to the Shareholders dated 22 September 2014, of which this letter forms part, which has been despatched by the Company to the Independent Shareholders in relation to the Subscription Agreement and the Whitewash Waiver. Unless the context requires otherwise, capitalised terms used in this letter shall have the same meanings as ascribed to them under the section headed "Definitions" in the Circular.

As set out in the Letter from the Board, the Company and the Subscriber entered into the Subscription Agreement whereby the Subscriber conditionally agrees to subscribe and the Company conditionally agrees to allot and issue to the Subscriber (a) the New Shares at an issue price of HK$0.32 per New Share; and (b) the Convertible Bonds of a principal amount of HK$832,000,000. The issue of the New Shares and the Convertible Bonds will be subject to the terms and conditions of the Subscription Agreement and the Specific Mandate to be approved by the Independent Shareholders at the EGM by ordinary resolution.

Upon the issue of the New Shares and full conversion of the Convertible Bonds but before the full exercise of the Warrants and the Share Options, the Subscriber will be interested in 3,400,636,000 Consolidated Shares, representing approximately 215.25% of the Consolidated Shares in issue upon the Share Consolidation becomes effective, and approximately 68.29% of the Consolidated Shares in issue as enlarged by the issuance of the New Shares and the Conversion Shares.

Under Rule 26 of the Takeovers Code, the acquisition of voting rights from less than 30% of voting rights to 30% or more will trigger an obligation on the Subscriber and persons acting in concert with it to make a general offer for all the securities of the Company other than those already owned or agreed to be acquired by them, unless the Whitewash Waiver is granted by the Executive and approved by the Independent Shareholders by way of poll. An application has been made by the Subscriber to the Executive for the Whitewash Waiver in respect of the Subscription Agreement and allotment and issue of the Conversion Shares upon full conversion of the Convertible Bonds. The Whitewash Waiver, if granted by the Executive, will be subject to, among other things, approval by the Independent Shareholders at the EGM by way of poll. The grant and approval of the Whitewash Waiver is a condition precedent to the completion of the Subscription Agreement. In the case where the Subscription Agreement is approved by the Independent Shareholders in the EGM and the Whitewash Waiver is not granted or approved by the Independent Shareholders, the Subscriber reserves its right as to whether or not to waive such condition. If the Subscriber waives such condition, it will comply with the provisions of the Takeovers Code to make a general offer under Rule 26.1 of the Takeovers Code.

None of the Subscriber and persons acting in concert with it has acquired or disposed of or entered into any agreement or arrangement to acquire or dispose of any voting rights in the Company during the six months period prior to the date of the holding announcement of the Company dated 31 July 2014. Save as the 3,180,000 Existing Shares held by PAML as beneficial owner and the 6,000,000 Existing Shares held under discretionary account, none of the Subscriber and persons acting in concert with it are interested in any issued Existing Shares or other relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) of the Company as at the Latest Practicable Date.

As at the Latest Practicable Date, save for the Subscription Agreement and the 3,180,000 Existing Shares beneficially held by PAML and the 6,000,000 Existing Shares held by PAML for its clients under discretionary account, (a) the Subscriber and persons acting in concert with it do not hold, control or have direction over any outstanding options, warrants, or any securities that are convertible into Existing Shares or any derivatives in respect of securities in the Company, or hold any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company; (b) the Subscriber and persons acting in concert with it did not borrow or lend any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company; (c) there is no arrangement referred to in Note 8 to Rule 22 of the Takeovers Code (whether by way of option, indemnity or otherwise) in relation to the relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) of the Company or of the Subscriber which might be material to the Subscription Agreement and the Whitewash Waiver; (d) there is no agreement or arrangement to which any of the Subscriber or persons acting in concert with it is a party which relates to circumstances in which it may or may not invoke or seek to invoke a pre-condition or a condition to the Subscription Agreement and the Whitewash Waiver; and (e) none of the Subscriber or persons acting in concert with it has received any irrevocable commitment to vote for or against the Subscription Agreement or the Whitewash Waiver.

The Independent Board Committee, comprising all of the four independent non-executive Directors, namely Mr. Hu Xiaoping, Mr. Woo Che-Wor, Alex, Mr. Qian Laizhong and Mr. Sun Tongchuan, has been established to consider the terms of the Subscription Agreement and the Whitewash Waiver and the transactions contemplated thereunder, and to advise the Independent Shareholders on whether they are on normal commercial terms, fair and reasonable and in the interests of the Company and the Shareholders as a whole, and to advise the Independent Shareholders as to whether to vote in favour of the relevant resolutions to be proposed at the EGM. We, Octal Capital Limited, have been appointed as the independent financial adviser to advise the Independent Board Committee in this regard.

The appointment of Octal Capital as the independent financial adviser in respect of the Subscription Agreement and the Whitewash Waiver has been approved by the Independent Board Committee. Octal Capital is not connected with the directors, chief executive and substantial shareholders of the Company or the Subscriber or any of their respective subsidiaries or their respective Associates or parties acting in concert with any of them and do not have any shareholding, directly or indirectly, in any member of the Group or any right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Group as at the Latest Practicable Date and therefore is considered suitable to give independent advice to the Independent Shareholders. During the last two years, there was no engagement between the Group and Octal Capital. Apart from normal professional fees payable to us in connection with this appointment, no arrangement exists whereby Octal Capital will receive any fees or benefits from the Group or the directors, chief executive and substantial shareholders of the Company or the Subscriber or any of its subsidiaries or their respective associates or parties acting in concert with any of them.

In formulating our opinion, we have relied on the accuracy of the information and representations contained in the Circular and have assumed that all information and representations made or referred to in the Circular as provided by the executive Directors were true at the time they were made and continue to be true as at the date of the Circular. We have also relied on our discussion with the executive Directors regarding the Group, the Subscription Agreement and the Whitewash Waiver, including the information and representations contained in the Circular. We have also assumed that all statements of belief, opinion and intention made by the executive Directors respectively in the Circular were reasonably made after due enquiry. We consider that we have reviewed sufficient information to reach an informed view, to justify our reliance on the accuracy of the information contained in the Circular and to provide a reasonable basis for our advice. We have no reason to suspect that any material facts have been omitted or withheld from the information contained or opinions expressed in the Circular nor to doubt the truth, accuracy and completeness of the information and representations provided to us by the executive Directors. We have not, however, conducted an independent in-depth investigation into the business and affairs of the Group and the Subscriber and their respective associates, nor have we carried out any independent verification of the information supplied to us. The Company will notify the Shareholders of any material changes after the Latest Practicable Date and throughout the offer period (as defined under the Takeovers Code) as soon as possible in accordance with Rule 9.1 of the Takeovers Code. The Independent Shareholders will also be notified of any material changes to such information provided and our opinion as soon as possible after the Latest Practicable Date and throughout the offer period (as defined under the Takeovers Code).

THE SUBSCRIPTION AGREEMENT

Principal factors and reasons considered

In arriving at our opinion regarding the terms of the Subscription Agreement, we have considered the following principal factors and reasons:

(i) **Information on the Group**

The Company was incorporated in the Cayman Islands with limited liability. The Company is an investment holding company and its subsidiaries are principally engaged in research and development, manufacture, marketing and distribution of chemical products, chemical fertilizers and bulk blending fertilizers.

- ***Financial information of the Group***

Financial performance

The following is a summary of the financial results of the Group for each of the three years ended 31 December 2013 and the six months ended 30 June 2013 and 30 June 2014 as extracted from the Company's annual reports and interim reports:

	Year ended 31 December			**Six months ended 30 June**	
	2011	**2012**	**2013**	**2013**	**2014**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
	(audited)	(audited)	(audited)	(unaudited)	(unaudited)
Turnover	1,426,888	1,346,970	1,339,252	680,756	738,166
- Bulk blending and compound fertilizers	167,000	153,000	86,000	33,423	29,973
- Urea	907,000	919,000	730,000	427,486	337,629
- Ammonia	209,000	205,000	186,000	105,684	108,062
- Ammonium bicarbonate	9,000	2,000	—	—	—
- Others *(Note 1)*	135,000	68,000	337,000	114,163	262,502
Cost of sales	1,144,540	1,019,752	1,202,342	570,467	686,160
Gross profit	282,348	327,218	136,910	110,289	52,006
Profit/(loss) before taxation	105,783	128,598	(64,257)	30,689	(27,254)
Profit/(loss) for the year attributable to owners of the Company	100,154	101,612	(57,056)	25,430	(23,082)

Source: Annual and interim reports of the Company

Note:

1. Others refer to carbon dioxide and the trading of urea, phosphate fertilizers, potash fertilizers, sodium carbonate, ammonia and methanol.

For the year ended 31 December 2012 ("**FY2012**")

Pursuant to the annual report of the Company for FY2012, the Group recorded a turnover of approximately RMB1,347.0 million, representing a decrease of approximately 5.6% as compared to approximately RMB1,426.9 million of the year ended 31 December 2011 ("**FY2011**"). The Group's sales volume excluding trading portion amounted to approximately 585,000 tonnes, representing a decrease of approximately 13.2% as compared to approximately 674,000 tonnes in FY2011. The mild decrease in turnover was attributable to a decrease in the market prices of the Group's products in the second half of the year owing to depressed industry condition, particularly for the urea and the liquid ammonia products. On the other hand, the decrease in the Group's sales volume was due to (i) the temporary adjustment to its natural gas supply plan by Sinopec which led to the downward revision of production plan of Group's Dazhou plant; and (ii) the overhaul at the Group's Dazhou plant in December 2012, which lasted for around 20 days, caused the Group failing to capture the favourable market conditions in December 2012, which in turn affected the sales volume of the products. Despite the foregoing, the Group recorded a profit attributable to owners of the Company amounted to approximately RMB101.6 million, representing an increase of approximately 1.4% as compared to approximately RMB100.2 million of FY2011 which was partly attributable to the relatively stable operation at the Dazhou plant throughout the year, the constant improvement in product quality and brand reputation of the Group's products and temporary suspension of operation at Dazhu plant which has been performed unsatisfactorily since 2011.

Gross profit margin of the Group increased from approximately 19.8% in FY2011 to approximately 24.3% in FY2012. The increase in the gross profit margin was due to the smooth production of the Group's Dazhou plant and the temporary closure of the Dazhu plant. During FY2012, the major products of the Group were (i) bulk blending and compound fertilizers; (ii) urea; and (iii) ammonia. Sales quantity of bulk blending and compound fertilizers decreased by approximately 12.6% to approximately 77,891 tonnes, while the sales revenue also declined by approximately 8.4% to approximately RMB153.0 million. Urea products contributed the most to the Group's revenue, recording revenue of approximately RMB919.0 million, increased slightly by approximately 1.3% as compared to FY2011. Sales quantity of urea remained stable at around 420,000 tonnes level in FY2012. Sales quantity of ammonia increased by approximately 4.9%, however its sales revenue decreased slightly by approximately 1.9% to approximately RMB205.0 million.

For the year ended 31 December 2013 ("**FY2013**")

Pursuant to the annual report of the Company for FY2013, the Group recorded a turnover of approximately RMB1,339.3 million, representing a slight decrease of approximately 0.6% as compared to FY2012. The Group's sales volume of fertilizers and chemical products amounted to approximately 531,000 tonnes, representing a decrease of approximately 9.2% as compared to 585,000 tonnes of FY2012. The decline in turnover and sales volume of the Group was attributable to an excess supply of products in the industry, coupled with increasing competition and weak market sentiment in the Chinese market, causing the average selling price of the Group's products to decrease by approximately RMB300 per tonne which contributed much to the weak performance of the Group during FY2013. Gross profit margin of the Group decreased from approximately 24.3% in FY2012 to approximately 10.2% in FY2013. The decrease in gross profit margin was similarly due to the decline in selling price of products, and the increase in the trading portion of the Group's business which caused the cost of sales of the Group increased by approximately 17.9% as compared to that of 2012. The Group recorded a loss attributable to owners of the Company that amounted to approximately RMB57.1 million, which was decreased significantly from a profit attributable to owners of the Company of approximately RMB101.6 million in FY2012. As disclosed in the Company's annual report for FY2013, the loss making position of the Group was a concerted effect of sluggish China domestic economic growth, and the challenging business environment in the Chinese chemical fertilizer industry that is characterised by an excessive production capacity, weak market demand and increasing competition, which significantly decelerated industry revenues during the year.

In FY2013, (i) bulk blending and compound fertilizers; (ii) urea; and (iii) ammonia continued to be the major products of the Group. Sales quantity of bulk blending and compound fertilizers decreased by approximately 34.6% to approximately 50,937 tonnes, while the sales revenue declined by approximately 43.8% to approximately RMB86.0 million. As for urea, though the sales quantity and sales revenue decreased by approximately 7.2% and 20.6% respectively compared to FY2012, it remained as the largest source of revenue for the Group, generating approximately 54.5% of the Group's turnover. Sales quantity of ammonia increased by approximately 6.1% whilst its sales revenue decreased by approximately 9.3%, which was mostly due to the decline in average selling price during the year. The decrease in sales revenue of urea and ammonia was generally in line with the overall decline in turnover.

We note that the Company's independent auditor had drawn attention to the Group's net current liabilities as at 31 December 2013, and to the consolidated net loss and net operating cash outflows of the Group for FY2013 as set out in its report in respect of the Group's consolidated financial statements for FY2013. The independent auditor had considered that such financial conditions indicated the existence of a material uncertainty which might cast significant doubt about the Group's ability to continue as a going concern without qualifying its true and fair opinion on the Group's consolidated financial statements. Further information regarding the Group's net current liabilities position and the net operating cash outflow are detailed in the sections headed "Financial position" and "Cash flow position" below.

For the six months ended 30 June 2014

For the six months ended 30 June 2014, the Group recorded a turnover of approximately RMB738.2 million, representing an increase of approximately 8.4% as compared with that of the corresponding period in 2013. However, cost of sales for the period amounted to approximately RMB686.2 million, representing an increase of approximately 20.3% as compared with that of the corresponding period in 2013, resulting in a loss for the period attributable to owners of the Company of approximately RMB23.1 million, representing a decrease of approximately 190.8% as compared to that of the corresponding period in 2013. The gross profit margin of the Group decreased from approximately 16.2% to 7.0%, which was mainly due to the decrease in selling price of products as a result of market downturn and an increase in trading volume portion that have a lower gross profit margin. The decrease in profit attributable to owners of the Company and gross profit margin was attributable to the fact that the declining trend of the demand and price in the chemical fertilizer industry continued from the second half of 2013. The total sales volume (excluding the trading portion) of the Group reached approximately 285,000 tonnes, representing a slight increase of approximately 4.0% as compared with that of the corresponding period in 2013 which was mainly attributable to the fact that the Group capitalised on the rising demand for fertilizer in summer to boost sales for the second quarter and the growth momentum displayed in the sales volume of trading products.

Financial position

The table below summaries the consolidated financial position of the Group as at 31 December 2011, 2012, 2013 and 30 June 2014:

	As at 31 December			As at 30 June
	2011	**2012**	**2013**	**2014**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
	(audited)	(audited)	(audited)	(unaudited)
Assets				
Non-current assets	1,924,458	2,489,505	2,990,714	3,249,406
Current assets	1,324,658	1,954,458	2,453,229	2,173,962
Total assets	3,249,116	4,443,963	5,443,943	5,423,368
Equity				
Capital and reserves attributable to the equity holders of the Company	1,020,060	1,118,072	1,069,032	1,045,950
Non-controlling interest	—	3,600	3,267	4,167
Total equity	1,020,060	1,121,672	1,072,299	1,050,117

	As at 31 December			As at 30 June
	2011	**2012**	**2013**	**2014**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
	(audited)	(audited)	(audited)	(unaudited)
Liabilities				
Non-current liabilities	379,758	935,752	1,130,462	1,016,328
Current liabilities	1,849,298	2,386,539	3,241,182	3,356,923
Total liabilities	2,229,056	3,322,291	4,371,644	4,373,251
Total equity and liabilities	3,249,116	4,443,963	5,443,943	5,423,368
Net current liabilities	(524,640)	(432,081)	(787,953)	(1,182,961)
Total assets less current liabilities	1,399,818	2,057,424	2,202,761	2,066,445
Net assets	1,020,060	1,121,672	1,072,299	1,050,117

Source: Annual and interim reports of the Company

The total assets of the Group amounted to approximately RMB3,249.1 million, RMB4,444.0 million and RMB5,443.9 million as at 31 December 2011, 2012 and 2013 respectively. As at 30 June 2014, the total assets of the Group amounted to RMB5,423.4 million, which primarily comprised property, plant and equipment and pledged bank deposits, which respectively accounted for approximately 50.2% and 27.7% of the total assets of the Group as at 30 June 2014.

The total liabilities of the Group amounted to approximately RMB2,229.1 million, RMB3,322.3 million and RMB4,371.6 million as at 31 December 2011, 2012 and 2013 respectively. As at 30 June 2014, long-term and short-term borrowings were the major items of liabilities of the Group, which together accounted for approximately 85.2% of the total liabilities of the Group as at 30 June 2014.

The Group consistently recorded a net current liabilities position for each of the three years ended 31 December 2013. As at 31 December 2012, the net current liabilities of the Group amounted to approximately RMB432.1 million, which further increased to approximately RMB788.0 million as at 31 December 2013. The Group continued to record a net current liabilities position of approximately RMB1,183.0 million as at 30 June 2014 which was primarily attributable to increase in short-term borrowings and trade and other payables.

The net assets of the Group (excluding non-controlling interest) amounted to approximately RMB1,046.0 million as at 30 June 2014.

We understand that the Group has been financing its business operations and developments mainly via long-term and short-term bank borrowings, which is the primary reason that the Group consistently recorded a net current liability position. The following table sets forth the breakdown of the Group's total borrowings as at 31 December 2011, 2012, 2013 and 30 June 2014:

	As at 31 December			As at 30 June
	2011	**2012**	**2013**	**2014**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
	(audited)	(audited)	(audited)	(unaudited)
Long-term borrowings	284,655	808,324	1,040,218	926,189
Short-term borrowings	1,448,846	1,933,961	2,583,575	2,632,151
Current portion of long-term borrowings	93,329	129,098	207,510	168,031
Total borrowings	1,826,830	2,871,383	3,831,303	3,726,371

Source: Annual and interim reports of the Company

As at 31 December 2012, the Group's total borrowings amounted to approximately RMB2,871.4 million, representing an increase of approximately 57.2% as compared to 31 December 2011. As at 31 December 2013, the Group's total borrowings further increased to approximately RMB3,831.3 million, representing an increase of approximately 33.4% as compared to 31 December 2012. As at 30 June 2014, it slightly decreased by approximately 2.7% to approximately RMB3,726.4 million. As at 30 June 2014, short-term borrowings accounted for approximately 70.6% of the Group's total borrowings. As advised by the Company, the primary uses of the net borrowings (borrowing less the pledged bank deposits) were for the construction of the Group's Dazhou Plant and Guangan plant. During the six months ended 30 June 2014, short-term borrowings amounted to approximately RMB765.4 million have been renewed.

As at 31 December 2013, the long-term bank borrowings are secured by (i) bank deposits of approximately RMB301.2 million; (ii) certain land use rights with a total net book value of approximately RMB32.9 million; (iii) property, plant and equipment with a total net book value of approximately RMB1,242.4 million; (iv) investment property with a total net book value of approximately RMB13.7 million; (v) 100% equity interest in Ko Yo Development Co., Ltd and Dazhou Ko Yo Chemical Industry Co., Ltd which were effectively owned by the Company, and (vi) guarantee of Mr. Li Weiruo, a Shareholder and Director. The average effective interest rate of long-term bank borrowings as at 31 December 2013 was approximately 7.83%.

As at 31 December 2013, the Group's short-term borrowings that amounted to approximately RMB2,010.0 million were secured by bank deposits of approximately RMB1,414.4 million and guaranteed by Mr. Li Weiruo, a Shareholder and Director. The borrowings were issued at fixed interest rates which range from approximately 5.60% to 8.86% per annum. As at 31 December 2013 short-term borrowings of approximately RMB2,191.6 million were repayable within 6 months.

The Group's gearing ratios were approximately 358.4% and 256.8% as at 31 December 2013 and 2012 respectively. As at 30 June 2014, the Group's gearing ratio was approximately 356.3%. The gearing ratios were calculated as total interest-bearing borrowings divided by total equity attributable to owners of the Company. The increase in the gearing ratio from 256.8% in FY2012 to 358.4% in FY2013 and 356.3% as at 30 June 2014 was mainly due to the increase of borrowings which are used for the construction of the Guangan project. Such high gearing ratios of the Group indicates that the Group's operations have been significantly dependent on interest-bearing borrowings and leaves the Group more vulnerable to the fluctuations in the external business environments.

Cash flow position

The table below summaries the cash flow position of the Group for each of the year ended 31 December 2011, 2012 and 2013:

	Year ended 31 December		
	2011	**2012**	**2013**
	RMB'000	*RMB'000*	*RMB'000*
	(audited)	(audited)	(audited)
Net cash generated/(used in) from operating activities	145,666	148,082	(135,483)
Net cash used in investing activities	(294,227)	(582,075)	(543,412)
Net cash generated from financing activities	208,689	652,651	445,171
Net increase/(decrease) in cash and cash equivalents	60,128	218,658	(233,724)

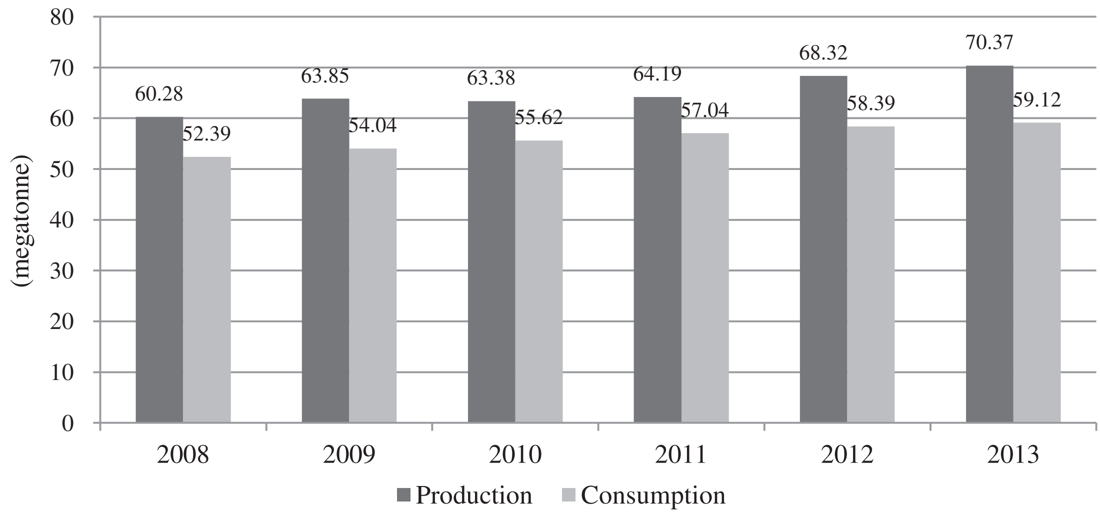
Source: Annual reports of the Company

We note that the Group has recorded net operating cash inflow in 2011 and 2012 but the Group recorded a net operating cash outflow that amounted to approximately RMB135.5 million. We further notice that despite the Group recorded a loss attributable to Shareholders in each of the financial years ended 31 December 2009 and 2010, the Group still managed to maintain a net operating cash inflow for the respective years, thus making FY2013 to be the only financial year that the Company has recorded a net operating cash outflow ever since its successful transfer to the Main Board of the Stock Exchange from the Growth Enterprise Market in 2008. The operating cash outflow recorded in FY2013 was attributable to (i) the substantial increase in trade and other receivables during FY2013 due to the increase in prepayment for raw materials and the increase in prepaid input value-added tax for the machineries in the Guangan plant; and (ii) the fact that the Group recorded a loss before tax for the year. In FY2013, cash used in investing activities was primarily for the purchase of property, plant and equipment while cash generated from financing activities was primarily proceeds from borrowings. As a result of the net operating cash outflow, the Group recorded a net decrease in cash and cash equivalents of approximately RMB233.7 million in FY2013, as compared to a net increase in cash and cash equivalents of approximately RMB218.7 million in FY2012.

- ***Industry overview and prospects***

Chemical fertilizer products generally cover nitrogen, potassium, phosphate and compound fertilizer which is a mix of these three types of fertilizers. Among all nitrogen-based fertilizers, ammonia (and its solutions) and urea are the most common ones. They are applied to soils or plant tissues to support or enhance the growth of crops. The chart below sets forth the production and consumption volume of chemical fertilizers in China during the period of 2008 to 2013:

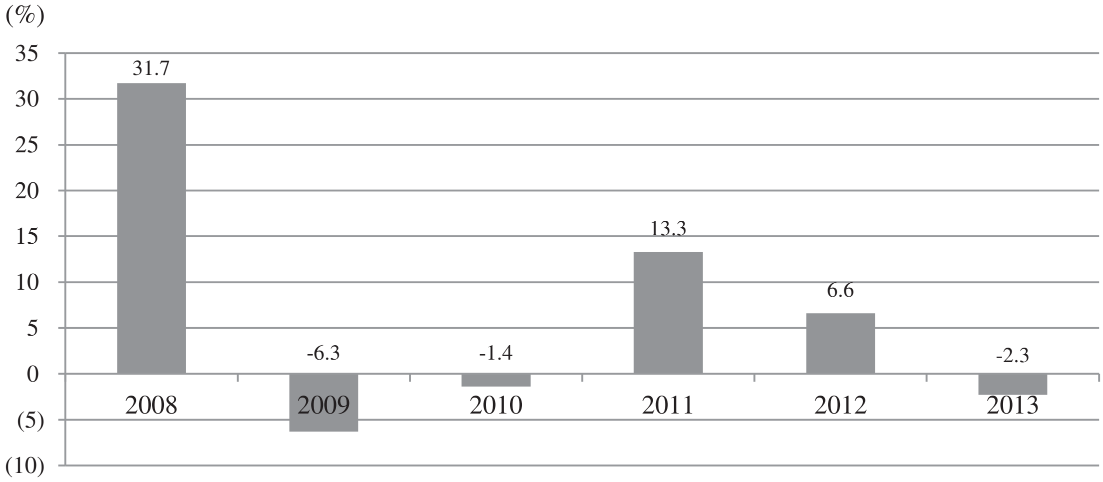
Production and consumption volume of chemical fertilizer in China, 2008-2013



Source: The National Bureau of Statistics of China

The production and consumption volume of chemical fertilizers in China displayed a stable yet mild increasing trend over the six-year period. The compound annual growth rate of production volume during the period is approximately 2.6% while that of consumption volume slightly lags behind at approximately 2.0%. The increase in production volume was supported by the Chinese government's preferential tax and energy policies towards the fertilizer industry that stimulated the expansion of production capacity of chemical fertilizers. In 2013, the production and consumption volume of chemical fertilizers in China were approximately 70.37 megatonnes ("**Mt**") and 59.12 Mt respectively, creating the largest excess supply of approximately 12.25 Mt in the period.

Rate of change of price level of chemical fertilizer in China, 2008-2013



Source: The National Bureau of Statistics of China

Regarding the historical price trend of chemical fertilizers in China, pursuant to the chemical fertilizer price index produced by the National Bureau of Statistics of China, price level of chemical fertilizers in China fluctuated moderately during 2009 to 2013. After experiencing a significant price increase in 2008, the price level of fertilizers in China slightly declined for two consecutive years. It then rebounded by approximately 13.3% in 2011, followed by another increase in 2012 of approximately 6.6%. In 2013, the price level declined by approximately 2.3%, partly attributable to the excessive production capacity during the year.

Pursuant to the《化肥工業「十二五」發展規劃》(The 12th Five-Year Planning on Chemical Fertilizer Industry) published by the Ministry of Industry and Information Technology of China in February 2012, it is predicted that the demand for chemical fertilizers in China would maintain the rising momentum and achieve an overall increase of approximately 5.4% during the entire 12th five-year period. The Ministry has also established a target production capacity expansion rate of approximately 4.4% during the period. Specifically for urea products, it is suggested the production volume should constitute approximately 70% of all nitrogen-based fertilizers by the end of the 12th five-year period, as compared to 55% in the year 2010.

Given the increasing awareness on industrial efficiency and environmental protection, it is expected that the future emphasis of the fertilizer industry would be reducing pollutant emission and increasing the fertilizer application efficiency. Meanwhile, it is stated in the planning that as the market price fixing mechanism matures, the present preferential policies in favor of the fertilizer industry would gradually fade out, bringing challenges as well as opportunities to the chemical fertilizer manufacturers in China.

(ii) **Background to and reasons for the Subscription Agreement**

Background and intention of the Subscriber

The Subscriber, Asia Pacific Resources Development Investment Limited, is an investment holding company incorporated in the British Virgin Islands wholly beneficially owned by Mr. KM Cheng. Mr. KM Cheng is a businessman and a Hong Kong permanent resident. Mr. KM Cheng is also one of the substantial shareholders holding approximately 26.4% interests of Shunfeng Photovoltaic International Limited (stock code: 1165) as at the Latest Practicable Date, the shares of which are listed on the main board of the Stock Exchange. As at the Latest Practicable Date, PAML, a company indirectly wholly owned by Mr. KM Cheng and acting in concert of the Subscriber, beneficially holds 3,180,000 Existing Shares. PAML, being a company engaged in the business of asset management, also holds another 6,000,000 Existing Shares for its clients under discretionary account in its ordinary course of business.

It is the intention of the Subscriber that the Group will continue to carry on its current business. The Subscriber has no intention to make any major changes to the business or employment of the employees of the Group or to redeploy the fixed assets of the Group. Save and except that the Subscriber will be entitled to nominate a director to the Board upon completion of the Subscription Agreement, the Subscriber will be unable to nominate other directors to the Company other than as in its capacity as a Shareholder in accordance with the Articles of Association of the Company.

Reasons for the Subscription

As set out in the Letter from the Board, the Company intends to utilise the net proceeds of the issue of the New Shares and the Convertible Bonds and the Loan of approximately HK$1.02 billion to strengthen the Company's financial position and help to renew its existing bank loans up to an outstanding principal amount of RMB478.4 million and as working capital of the Group in respect of (i) the Guangan factory which recently launched production, (ii) any possible new project, and (iii) general working capital. Those loans to be renewed originally will be matured from September 2014 to January 2015.

The Directors consider that the proceeds from the issue of New Shares and Convertible Bonds will improve the cash position of the Company and strengthen its capital base, which would put the Company at a better position to obtain lower interest rates from banks while the Company renews its existing loans. In the event of existing banks are unable to offer a competitively lower interest rate, the Company will consider to secure additional loans from other banks to repay the existing facilities. The Company may also benefits from a higher credit limit and lower interest rate offered by banks.

As advised by the Company, the net proceeds from the Subscription are intended for the following uses: (i) HK$420 million for the Group's first phase of expansion project at the Guangan plant where HK$230 million is for the settlement of the plant construction costs and HK$190 million is for the general working capital of the plant; (ii) HK$180 million for the second phase of project at the Dazhou plant to finance the expansion of the plant; (iii) HK$125 million for the construction of the phosphoric acid plant; (iv) HK$75 million for the new materials (polyphenylene sulfide) projects; and (v) the remaining net proceeds of approximately HK$200 million for the general working capital of the Group.

The Group currently owes a loan in the sum of US$6.0 million to IFC which is to be repaid in 2017. The Company has no current intention to use the proceeds from Subscription and the Loans to repay the loan from IFC before 2017 since (i) for early repayment of the IFC loan, the Company will be required to pay an early repayment charge and (ii) as the Company intends to apply such proceeds to facilitate the renewal of part of its existing bank loans at a lower interest rate, where those bank loans generally carry an effective interest rate of over 9%, which is higher than that of the IFC loan, thus early repayment of such IFC loan provides less financial benefit to the Company.

Based on the information provided by the Company, as at the Latest Practicable Date, the Group had short-term borrowings (excluding the acceptance notes) of approximately RMB1,041.3 million which are repayable within a year and long-term borrowings of approximately RMB1,085.6 million which are repayable before 2019. The short-term borrowings (excluding the acceptance notes) carry fixed interest rates that range from 6.0% to 9.8% per annum and we note that the majority of them have interest rates of over 8.0% per annum. Total short-term borrowings (excluding the acceptance notes) amounted to approximately RMB284.6 million are secured by bank deposits of approximately RMB125.5 million. Based on the Group's capital resources and amount of cash and cash equivalents on hand as at 30 June 2014, we note that it is highly unlikely that the Group will have sufficient resources to repay the short-term borrowings in the coming year and the Company advised that the Group will seek to renew the short-term borrowings when they come due. Failure in repayment or renewal of the existing short-term borrowings may result in the repossession of collateral and severely affect the Group's ability to obtain any other loans in the future, which in turn may hinder the future growth and prospects of the Group.

In addition to obtaining borrowings, to finance the construction of Guangan project, the Company entered into a bonds subscription agreement and a warrant subscription agreement with Asian Equity and PA International on 29 June 2012, pursuant to which, Asian Equity and PA International subscribed for a bond of HKD140 million (equivalent to RMB113 million) issued by the Company at the nominal interest rate of 9% per annum and the Company issued warrants at nil consideration to Asian Equity and PA International to subscribe 875,000,000 ordinary shares of HKD0.02 each from the Company at an exercise price of HKD0.16 per share. The bonds are due by 7 July 2015, subject to an early redemption put options held by Asian Equity and PA International, which were guaranteed by Mr. Li Weiruo, a Shareholder and Director. The effective interest rate of the borrowing from Asian Equity and PA International as at 31 December 2013 was approximately 26.21%. To our knowledge such bond subscription agreement in 2012 was the most recent fund raising activity conducted by the Company.

Based on the Company's annual and interim reports, we set out below the Group's interest coverage ratios (calculated by dividing operating profit by interest expense of bank borrowings) for the years ended 31 December 2011, 2012, 2013 and the six months ended 30 June 2014.

	Year ended 31 December			Six months ended 30 June
	2011	**2012**	**2013**	**2014**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Operating profit	181,714	222,102	18,202	10,320
Total interest cost (net) *(Note 1)*	85,343	129,868	147,775	105,936
Interest coverage ratio (times)	2.13	1.71	0.12	0.10

Note:

1. Total interest cost refers to the sum of interest expense and capitalised interest expense.

The Group's interest coverage slightly decreased from approximately 2.13 times for FY2011 to approximately 1.71 times in FY2012, and further plunged to approximately 0.12 time in FY2013. For the six months ended 30 June 2014, it remained at a considerable low level of approximately 0.10 time. The significant decrease in interest coverage ratio for FY2013 is primarily attributable to the decline in operating profit and indicates that the Group was not generating sufficient revenues to satisfy its interest expenses and its ability to repay its borrowings is highly questionable.

Given such heavy interest burden of the Group, coupled with the Group's net current liabilities as at 31 December 2013 and the consolidated net loss and net operating cash outflows of the Group for FY2013 as previously discussed, we concur with the view of the Group's independent auditor that such financial conditions indicated the existence of a material uncertainty which might cast significant doubt about the Group's ability to continue as a going concern. Given the facts that (i) the FY2013 was the first and only financial year that the Company recorded a net operating cash outflow; (ii) the Company was consistently in a net current liabilities position; (iii) the Group recorded a net loss in FY2013 and the six months ended 30 June 2014; and (iv) the Group's business activities are substantially financed by short-term and long-term borrowings in which the Group was facing increasing difficulties in meeting its interest obligations or repaying such loans, we are of the view that it is unlikely that the Group could turn around the situation with its internal recourses in a reasonable timeframe and thus the considerable net proceeds from the Subscription provides an immediate and effective means for the Group to replenish its working capital and reduce its interest obligations which is favourable to the financial performance of the Group in the near future.

On the other hand, we understand that part of the net proceeds from the Subscription is intended to channel towards the Group's future expansion projects. We note from the annual and interim reports of the Company that the Group's first phase of expansion project, the Guangan factory located in Xinqiao Energy and Chemical Park in Guangan, is capable of producing

300,000 tonnes of synthetic ammonia and 500,000 tonnes of methanol annually. Construction commenced in 2012 and completed in late 2013, however due to a delay in supply of natural gas and industrial water, the trial production of the factory has only commenced in June 2014. The Company expects that the first phase of the project in Guangan will materialise trial production with material input in the third quarter of 2014, and will achieve a production rate of 85% by the end of the year. We understand that the Company has gradually established a sales network for the newly-added methanol and liquid ammonia products through discussion and trades on a trial basis, and has entered into long-term supply agreements and strategic cooperation agreements with a number of domestic and international methanol purchasers, where such purchase amount exceeds the annual production capacity of the plant so that the product sales of the Guangan plant was largely ensured. The Company considers the completion and commencement of operation of the Guangan project marks the diversification of the Group's business to the fine chemical industry which requires higher technological inputs and with the recovery of the methanol market, the Directors expects the Guangan project will be a new growth driver for the Group's operations in the future.

Meanwhile, the Group's second phase of project, a 300,000 tonnes of urea and 40,000 tonnes of melamine production facility in the Group's Dazhou plant, has completed the optimisation of urea production technology as well as the perfection and optimisation of melamine production technology in the first half of 2014. Melamine is a high value-added chemical product with urea as its raw material and the production of melamine is expected to further extend the product offerings, optimise the product mix and improve the profitability of the Group. Upon completion of the second phase of project, the Dazhou plant would achieve an annual production capacity of 500,000 tonnes of synthetic ammonia, 800,000 tonnes of urea and 40,000 tonnes of melamine.

In addition to the first and second phase of the expansion projects, the Company also had plans to engage in the production of industrial-grade phosphoric acid in the future. The Group obtained the mining rights for a phosphate mine located at Qingping Township, Mianzhu City, Sichuan Province in 2010 and intended to commence the construction of the project once the intellectual property rights of the kiln process for producing phosphoric acid developed by the Group has been secured and the design of the project has been completed. Further, in 2013 the Group has initiated a preliminary research on new materials (polyphenylene sulfide) with an aim of diversifying into technologically advanced and high value-adding products in the future.

Given the abovementioned development plans, we are of the view that the first phase and second phase of the Group's expansion projects provide additional momentum to the future growth of the Group and the net proceeds from the Subscription provide greater flexibility and additional resources to the Group to cope with the challenges ahead brought by the projects and ensure the smooth implementation of the expansion projects in the near future.

We understand that the Directors have considered and the Company was in negotiations with banks and other financial institutions in 2014 in respect of alternative financing means, such as additional bank borrowings and issuance of equity and/or convertible debt instruments. As advised by the Company, such alternative financing methods turned out to be unsuccessful owing to the loss-making financial results of the Group for the first half of 2014 and the existing debt level of the Group and thus the Directors considered the Subscription offer a good opportunity to strengthen the financial position of the Company.

Having considered the benefits to the Group from the Subscription, the worsening of the Group's financial position as stated above, and the lack of alternative financing means available to the Company, we concur with the Directors' view that the Subscription offer a good opportunity to replenish immediate working capital for the Group and to strengthen the financial position of the Company and we consider that the Subscription is in the interests of the Company and the Shareholders as a whole.

(iii) **Principal terms of the Subscription Agreement**

Issue of New Shares

Pursuant to the Subscription Agreement, the Subscriber conditionally agrees to subscribe and the Company conditionally agrees to allot and issue to the Subscriber the 800,000,000 New Shares at an issue price of HK$0.32 per New Share (the "**Issue Price**").

Assuming the Share Consolidation has become effective and there is no change in the issued share capital of the Company or exercise of the Warrants and Share Options other than the Share Consolidation from the Latest Practicable Date and up to the completion of the Subscription Agreement, the New Shares will represent (i) approximately 50.6% of the Consolidated Shares in issue; (ii) approximately 33.6% of the Consolidated Shares in issue as enlarged by the issue of the New Shares; and (iii) approximately 16.1% of the Consolidated Shares in issue as enlarged by the issue of the New Shares and the Conversion Shares.

The New Shares will be issued free from any encumbrances or third party rights of any kind and upon issue will rank *pari passu* in all respects with each other and with the Consolidated Shares in issue in accordance with the memorandum and articles of association of the Company. An application has been made by the Company to the Stock Exchange for the listing of, and permission to deal in, the New Shares.

Issue of the Convertible Bonds

Pursuant to the Subscription Agreement, the Subscriber conditionally agrees to subscribe and the Company conditionally agrees to allot and issue to the Subscriber the Convertible Bonds of a principal amount of HK$832,000,000 and a conversion price of HK$0.32 per Conversion Share subject to adjustment events of (i) share consolidation or share subdivision or reclassification of shares; (ii) issue any shares credited as fully paid by way of capitalisation of profits or reserves; (iii) issue of shares in lieu of a cash dividend; (iv) capital distribution; (v) offer to holders of shares of the Company new shares for subscription by way of rights issue, or grant to holders of shares of the Company any rights to subscribe for new shares; (vi) issue any shares or grant any rights to subscribe for new shares at a price per new share which is less than 80% of the market price; or (vii) issue any securities which by their terms are convertible into or exchangeable for or carry rights to acquire or subscribe for new shares at a price per new share which is less than 80% of the market price. The term "market price" here refers to the average of the closing prices of the Shares of the Company on the Stock Exchange in the five trading days preceding the day on or as of which the market price is to be ascertained. The Convertible Bonds carry a 7% interest rate and shall mature on the tenth anniversary from the date of issue.

The Convertible Bonds are convertible in whole or in part by the Bondholder at any time from the issue date to the business day immediately preceding the maturity date of the Convertible Bonds. The Conversion Shares will be issued free from any encumbrances or third party rights of any kind and upon issue will rank *pari passu* in all respects with each other and with the New Shares in issue in accordance with the memorandum and articles of association of the Company.

Based on the initial Conversion Price of HK$0.32 per Conversion Share, subject to adjustments, a maximum number of 2,600,000,000 Conversion Shares will be allotted and issued upon exercise of the conversion rights attached to the Convertible Bonds in full, which, assuming the Share Consolidation becoming effective and there is no change in the issued share capital of the Company or exercise of the Warrants and Share Options other than the Share Consolidation from the date of this announcement up to the completion of the Subscription Agreement, represent: (i) approximately 164.6% of the Consolidated Shares in issue; (ii) approximately 109.3% of the Consolidated Shares in issue as enlarged by the issue of the New Shares; and (iii) approximately 52.2% of the Consolidated Shares in issue as enlarged by the issue of the New Shares and the Conversion Shares.

The Issue Price and the Conversion Price

We note that the Issue Price of HK$0.32 per New Share and the initial Conversion Price of HK$0.32 per Conversion Share were determined and agreed after arm's length negotiations between the Company and the Subscriber, taking into account the Group's existing financial position, liquidity of the Existing Shares in the market and the recent trading prices of the Existing Shares.

The Issue Price of HK$0.32 per New Share and the initial Conversion Price of HK$0.32 per Conversion Share represent:

(a) a discount of approximately 41.8% to the adjusted closing price per Consolidated Share of HK$0.55 based on the closing price of HK$0.11 per Existing Share as quoted on the Stock Exchange on 28 July 2014, being the Last Trading Day and adjusted for the effect of the Share Consolidation;

(b) a discount of approximately 28.3% to the average of the adjusted closing prices per Consolidated Share of HK$0.446 based on the average of the closing prices of approximately HK$0.089 per Existing Share as quoted on the Stock Exchange for the five consecutive trading days ended on the Last Trading Day;

(c) a discount of approximately 25.4% to the average of the adjusted closing prices per Consolidated Share of HK$0.429 based on the average of the closing prices of approximately HK$0.086 per Existing Share as quoted on the Stock Exchange for the ten consecutive trading days ended on the Last Trading Day;

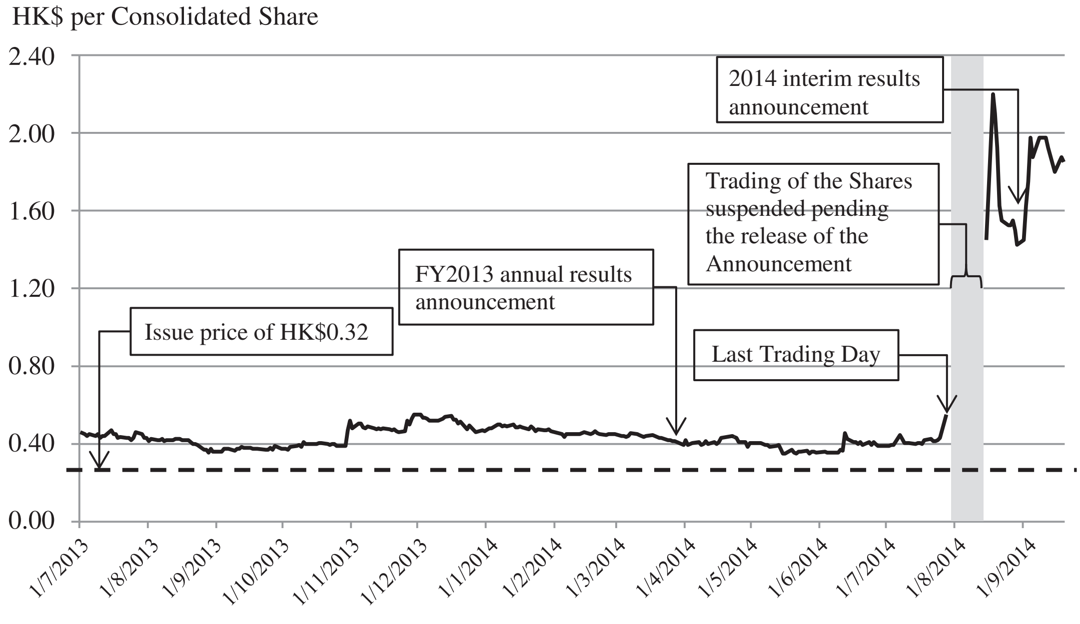
(d) a discount of approximately 82.7% to the average of the adjusted closing prices per Consolidated Share of HK$1.850 based on the closing prices of approximately HK$0.370 per Existing Share as quoted on the Stock Exchange on the Latest Practicable Date and adjusted for the effect of the Share Consolidation;

(e) a discount of approximately 65.6% to the Group's adjusted audited consolidated net asset per Consolidated Share as at 31 December 2013 of approximately HK$0.930, based on the audited consolidated net asset per Existing Share of HK$0.186 as at 31 December 2013 and a total of 1,439,056,923 Consolidated Shares as at the date of the Subscription Agreement (assuming the Share Consolidation has become effective) and the Group's audited consolidated net asset value attributable to owners of the Company of approximately RMB1,069,032,000 as at 31 December 2013;

(f) a discount of approximately 65.1% to the Group's adjusted unaudited consolidated net asset per Consolidated Share as at 30 June 2014 of approximately RMB0.727 (equivalent to approximately HK$0.916), based on the unaudited consolidated net asset per Existing Share of RMB0.145 (equivalent to approximately HK$0.183) as at 30 June 2014 and a total of 1,439,056,923 Consolidated Shares as at the date of the Subscription Agreement (assuming the Share Consolidation has become effective) and the Group's audited consolidated net asset value attributable to owners of the Company of approximately RMB1,046.0 million as at 30 June 2014.

Historical performance of Share price

For the purpose of comparing the Issue Price with the market price of the Shares, we plot the adjusted closing price per Consolidated Share traded on the Stock Exchange from 1 July 2013 (being the 12-month period prior to the date of the Announcement which it is a commonly used tenure for such analysis purpose) to 28 July 2014 (being the Last Trading Day) (the "**Pre-announcement Period**") and further up to the Latest Practicable Date (the "**Review Period**") as follows:



Source: Infocast

During the Pre-announcement Period, the adjusted closing prices per Consolidated Share ranged from HK$0.350 to HK$0.550 with an average adjusted closing price of HK$0.429 per Consolidated Share. The highest closing price per Consolidated Share HK$0.550 was recorded on 29 November 2013, 2 December 2013 and the Last Trading Day, while the lowest closing price per Consolidated Share HK$0.350 was recorded on 15, 21 and 27 May 2014 respectively. During the Pre-announcement Period, the Issue Price and the Conversion Price represents (i) a discount of approximately 8.6% to the lowest closing price per Consolidated Share of HK$0.350; (ii) a discount of approximately 41.8% to the highest closing price per Consolidated Share of HK$0.550; and (iii) a discount of approximately 25.4% to the 12-month average closing price of the Pre-announcement Period.

During the Review Period, the highest closing price per Consolidated Share was HK$2.200 which was recorded on 18 August 2014 whilst the lowest closing price per Consolidated Share was the same as the Pre-announcement Period being HK$0.350. The Issue Price and the Conversion Price represents a discount of approximately 85.5% to the highest closing price per Consolidated Share and a discount of approximately 8.6% to the lowest closing price per Consolidated Share during the Review Period. The Issue Price and the Conversion Price is also below the adjusted closing prices per Consolidated Share during the entire Review Period.

On 28 July 2014, being the Last Trading Day, we note that there were unusual price movements in the morning trading session where the adjusted closing price per Consolidated Share increased by approximately 27.9% to HK$0.550. The Company released an announcement confirming that the Board was unaware of any reasons for such price movements, save for (i) the Guangan plant has fulfilled the condition for entering production stage and (ii) the Company was in negotiation with third parties for possible financing. Trading in the Existing Shares was suspended in the afternoon of 28 July 2014 and remained suspended until the release of the Announcement. On 14 August 2014 subsequent to the release of the Announcement, trading of the Shares resumed and the adjusted closing price per Consolidated Share on the same day surged by approximately 163.6% to HK$1.450 as compared to the previous closing price of HK$0.550 recorded on the Last Trading Day. The share price continued to rise and reached HK$2.200 per Consolidated Share on the next trading day being 18 August 2014, in which such closing price of HK$2.200 per Consolidated Share was the highest closing price recorded during the Review Period. We are unaware of any reasons that had caused the closing prices to fluctuate substantially during the other trading days in the Review Period.

Historical trading liquidity of the Shares

We set out below the trading liquidity of the Existing Shares during the Review Period and up to the Latest Practicable Date:

Month	**Highest daily turnover (number of Existing Shares)**	**Average daily turnover (number of Existing Shares)** *(Note 1)*	**Number of trading days with no turnover** *(days)*	**Percentage of average daily turnover to total number of Existing Shares in issue**	**Percentage of average daily turnover to total number of Existing Shares held by public Shareholders** *(Note 2)*
2013					
Jul	7,980,000.0	2,431,818.2	0	0.03%	0.06%
Aug	11,800,000.0	3,598,571.4	0	0.05%	0.08%
Sep	13,380,000.0	4,754,150.0	0	0.06%	0.11%
Oct	142,000,000.0	12,117,619.0	1	0.16%	0.28%
Nov	53,840,000.0	10,689,523.8	0	0.14%	0.25%
Dec	16,040,000.0	4,814,500.0	0	0.06%	0.11%

Month	Highest daily turnover (number of Existing Shares)	Average daily turnover (number of Existing Shares) *(Note 1)*	Number of trading days with no turnover *(days)*	Percentage of average daily turnover to total number of Existing Shares in issue	Percentage of average daily turnover to total number of Existing Shares held by public Shareholders *(Note 2)*
2014					
Jan	15,700,000.0	3,755,199.3	0	0.05%	0.09%
Feb	18,820,000.0	3,768,421.1	0	0.05%	0.09%
Mar	8,480,000.0	2,622,619.0	0	0.03%	0.06%
Apr	7,940,000.0	2,250,000.0	1	0.03%	0.05%
May	20,160,000.0	2,598,000.0	5	0.03%	0.06%
Jun	56,300,000.0	7,137,000.0	0	0.09%	0.17%
Jul	73,080,000.0	9,311,578.9	0	0.12%	0.22%
Aug	1,535,532,032.0	570,237,765.8	0	7.41%	13.24%
Sep (up to and including the Latest Practicable Date)	711,265,024.0	217,622,145.1	0	2.83%	5.05%

Source: Infocast

Note:

1. Average daily trading volume is calculated by diving the total trading volume for the month/period by the number of trading days during the month/period which exclude any trading day on which trading of the Shares on the Stock Exchange was suspended for the whole trading day.

2. Public Shareholders refer to Shareholders other than the Subscriber, the executive Directors and their respective concert parties and any other Shareholders who are interested or involved in the Subscription Agreement (including the Specific Mandate) and/or the Whitewash Waiver.

The average daily turnover volume in the Review Period was within the range of 2,250,000 Existing Shares (approximately 0.03% of total number of Existing Shares in issue) and 570,237,765.8 Existing Shares (approximately 7.41% of total number of Existing Shares in issue). We note from the above table that trading in the Existing Shares had been generally thin during the Pre-announcement Period, with the average daily trading volume below 0.3% of the total number of issued Existing Shares held by Independent Shareholders. We are unaware of any major events that significantly influenced the trading liquidity during the Pre-announcement Period. Subsequent to the release of the Announcement on 14 August 2014, we note that trading of the Existing Shares in August has significantly increased, reaching an average daily turnover of 570,237,765.8 Existing Shares which is approximately 61 times of that of July. Based on the above, we consider that the trading volume of the Existing Shares during the entire Review Period was considerably thin, despite the higher trading volume in August and September 2014. The low liquidity of the Shares may imply that lack of interest from potential investors to invest in the Shares and it may render the Company difficult in finding investors for fundraising activity to support the business activities of the Group.

Historical discount of market price to net asset value per Share

We have compared the historical closing price of the Existing Shares against the then published net asset value (excluding non-controlling interests) per Existing Share, which we assumed was generally available to the market from the date of publication of the relevant full year or interim results announcements and that the closing price of the Existing Shares has reflected such information.

Period	Published consolidated net asset value per Existing Share *(HK$)*	Closing price per Existing Share *(HK$)*			Premium/ (discount) over/ to net asset value per Existing Share		
		Highest	**Lowest**	**Average**	**Highest**	**Lowest**	**Average**
25/8/2012[(1)] - 25/3/2013	0.188[(2)]	0.146	0.113	0.127	-22.2%	-39.8%	-32.3%
26/3/2013[(1)] - 23/8/2013	0.192[(2)]	0.116	0.079	0.097	-39.5%	-58.8%	-49.5%
24/8/2013[(1)] - 24/3/2014	0.201[(2)]	0.110	0.071	0.090	-45.2%	-64.6%	-55.4%
25/3/2014[(1)] - Last Trading Day	0.186[(2)]	0.110	0.070	0.080	-40.9%	-62.4%	-57.2%
Simple average of the discounts to the net asset value per Existing Share represented by the average closing price for the above respective periods							-48.6%

Source: Infocast; Annual and interim reports of the Company

Notes:

1. The first trading day immediately after the publication of the Company's full year or interim results announcements.

2. Based on the net assets attributable to the owners of the Company and the number of Existing Shares as at the respective period-end date. Figures in RMB are translated into HKD at the exchange rates quoted by the People's Bank of China as at the respective period-end date.

We note that the market price of the Existing Shares have been consistently trading at a discount to the then underlying net asset value per Share of the Company at all times since 25 August 2012 (being the first trading day immediately after the publication of the Company's 2012 interim results announcement) to the Last Trading Date. During such period, the discount of the closing price of the Existing Shares to the net asset value per Existing Share ranges from approximately 22.2% to 64.6% with the average being approximately 48.6%.

The Issue Price and the Conversion Price of HK$0.32 represents a discount of approximately 65.6% to the adjusted net asset value per Consolidated Share as at

31 December 2013 of approximately HK$0.930. Given the facts that the Existing Shares have been trading at an average discount of approximately 48.6% to the then net asset value per Share of the Company and the discount represented by the Issue Price and the Conversion Price is close to the lower end of the range of the historical discount to the net asset value per Share of the Company, we are of the view that the Issue Price and the Conversion Price is acceptable.

Comparison with peer companies

The Issue Price and the Conversion Price of the Convertible Bonds are agreed between the Company and the Subscriber with reference to the recent trading prices of the Existing Shares. With a view to analysing the market price of the Existing Shares (valuation of the Company) and thus the Issue Price and the Conversion Price, we have compared the price/earnings multiple (the "**P/E ratio**") and the price-to-book ratio (the "**P/B ratio**") of the Company with those of other companies listed on the Stock Exchange which are principally engaged in, among others, the manufacture and distribution of fertilizers, including chemical, biological and compound fertilizers (the "**Market Comparables**"). We also set out the gearing ratio of the Market Comparables for comparison. We consider the Market Comparables set forth in the table below an exhaustive list given such criteria.

Stock code	**Company**	**Share price on the Last Trading Day**	**Market capitalisation as at the Last Trading Day**	**Latest published earnings per share**	**Latest published net asset value per share**	**P/E ratio**	**P/B ratio**	**Gearing ratio**
		HK$	*HK$'million*	*HK$*	*HK$*	*times*	*times*	*%*
		(Note 1)	*(Note 1)*	*(Note 2)*	*(Note 3)*			*(Note 4)*
297	Sinofert Holdings Limited	1.15	8,078.12	(0.09)	2.37	N/A	0.49	22.2%
509	Century Sunshine Group Holdings Limited	1.01	2,902.32	0.08	0.76	12.61	1.32	15.1%
1073	China Agrotech Holdings Limited	0.21	209.37	0.15	1.93	1.36	0.11	55.1%
1866	China XLX Fertiliser Limited	2.66	2,660.00	0.34	3.19	7.92	0.83	17.3%
3983	China BlueChemical Limited	4.10	7,261.10	0.45	3.91	9.02	1.05	0.2%
8189	Tianjin TEDA Biomedical Engineering Company Limited	0.72	507.60	0.02	0.14	37.61	5.08	50.8%
	Mean					13.70	1.48	26.8%
	Median					9.02	0.94	19.8%
	Maximum					37.61	5.08	55.1%
	Minimum					1.36	0.11	0.2%
	The Company *(Note 5)*	0.55	791.48	(0.05)	0.93	N/A	0.59	358.4%
	The Subscription *(Note 6)*	0.32			0.92		0.35	

Source: Website of the Stock Exchange

Notes:

1. Market capitalisation and closing share price figures of the Market Comparables are sourced from the website of the Stock Exchange.

2. Figures are extracted from the annual reports of the Market Comparables for their latest financial year, where figures in RMB are translated at an exchange rate of RMB1 = HK$1.2719.

3. The net asset value per share of the Market Comparables is calculated by dividing the latest published net assets (excluding non-controlling interests) by the number of shares as at the respective period-end date. Figures in RMB are translated at an exchange rate of RMB1 = HK$1.2719.

4. The gearing ratio is calculated by dividing total interest-bearing borrowings by total equity attributable to owners of the company.

5. Figures have been adjusted assuming the Share Consolidation has become effective on the Last Trading Day.

6. The P/B ratio of the Subscription is calculated by dividing the Issue Price and the Conversion Price of HK$0.32 by the net asset value per Consolidated Share of the Company as at 30 June 2014 being approximately HK$0.916.

Though the market capitalisation of the Market Comparables varies from HK$209.37 million to HK$8,078.12 million, we consider that the principal business of the Market Comparables are largely comparable to that of the Company and the elimination of those with a large market capitalisation will reduce the sample size of the Market Comparables and as such may result in a less thorough comparison. As the Group recorded a loss attributable to the owners of the Company in the latest full financial year, the P/E ratio analysis is not applicable to the Company and the information of the Market Comparables is thus provided for reference only. We note that the P/B ratio of the Subscription is approximately 0.35 time, which is lower than the mean of the Market Comparables being approximately 1.48 times and the median of the Market Comparables being approximately 0.94 time, however still falls within the range of the Market Comparables between 0.11 time and 5.08 times.

Despite the fact that the P/B ratio represented by the Subscription is lower than the mean and median of the Market Comparables, we also note that all of the Market Comparables had a low gearing ratio that ranged from approximately 0.2% to 55.1% and none of which recorded a net current liability position, as compared to the consistent net current liability position of the Group and the extremely high gearing of the Group being approximately 358.4% as at 31 December 2013 which is far above any of the Market Comparables. Given the above, and taking into consideration (i) the fact that the P/B ratio of the Company implied by the closing price of the Existing Shares on the Last Trading Day was already below the mean and median of the Market Comparables; (ii) the historical discounts of the Share price to the net asset value per Share of the Company; (iii) the immediate improvement in the Group's gearing, liquidity and working capital position upon the completion of the Subscription; and (iv) the low P/B ratio of the Subscription still falls within the range of the Market Comparables, we consider that the P/B ratio represented by the Subscription is acceptable.

Comparison of the Issue Price and the Conversion Price

To further assess the fairness and reasonableness of the Issue Price and the Conversion Price, we have conducted a comparable analysis through identifying companies listed on the Stock Exchange which announced subscription or placement of new shares and/or issuance of convertible bonds from 1 January 2014 up to and including the Latest Practicable Date with a total issue size of at least HK$500 million. We consider the purpose of limiting the analysis timeframe to 2014 is to compare the Issue Price and the Conversion Price with those of the comparable companies in the recent stock market environment and with the similar market sentiment, while selecting comparable transactions with a total issue size of at least HK$500 million better reflects the preference and risk appetite of investors who make sizable investments in listed companies, given the considerable net proceeds from the Subscription of approximately HK$1,020.0 million. Based on the above, we have, by searching through published information on the Stock Exchange's website, identified an exhaustive list of 25 subscription or placement of new shares and/or issuance of convertible bonds (the "**Transaction Comparables**"), as set out in the table below. We consider such selection criteria to be reasonable and meaningful for identifying the Transaction Comparables for comparison purpose.

During the aforesaid period, no subscription/placement or issuance of convertible bonds of listed company engaged in the business of chemical fertilizers could be identified based on the above selection criteria. However, while this analysis is aiming at comparing the respective subscription/placing/conversion price towards their prevailing market price, we therefore consider our analysis taking into account all comparable transactions of similar issue size during the period without limiting to a particular industry is fair and reasonable. Though the circumstances under each of the Transaction Comparables may be different, we consider that our comparable analysis on the Issue Price and the Conversion Price is useful for the Independent Shareholders' information and reference given that the selected review period has produced a reasonable size of samples for comparison purpose.

Date of announcement	Stock code	Company	Transaction type	Subscription /placing /conversion price *(HK$)*	Premium/ (discount) over/ to the closing price of the shares as at the last trading day prior to the date of the corresponding announcement	Premium/ (discount) over/ to the closing price of the shares for the last 5 consecutive trading days	Premium/ (discount) over/ to the closing price of the shares for the last 10 consecutive trading days	Premium/ (discount) over/ to the net asset value per share *(Note 1)*
6/1/2014	986	China Environmental Energy Investment Limited	Placing of convertible bonds	0.50	-56.1%	-52.7%	-45.6%	N/A
22/1/2014	956	China Suntien Green Energy Corporation Limited	Placing of H shares	3.35	-6.2%	-7.2%	-4.8%	23.7%

Date of announcement	Stock code	Company	Transaction type	Subscription /placing /conversion price *(HK$)*	Premium/ (discount) over/ to the closing price of the shares as at the last trading day prior to the date of the corresponding announcement	Premium/ (discount) over/ to the closing price of the shares for the last 5 consecutive trading days	Premium/ (discount) over/ to the closing price of the shares for the last 10 consecutive trading days	Premium/ (discount) over/ to the net asset value per share *(Note 1)*
23/1/2014	241	Citi 21CN Company Limited	Issue of subscription shares	0.30	-63.9%	-61.8%	-61.2%	304.5%
12/2/2014	2319	China Mengniu Dairy Company Limited	Subscription for new shares	42.50	15.3%	17.6%	18.9%	322.7%
25/2/2014	1101	China Rongsheng Heavy Industries Group Holdings Limited	Issue of convertible bonds	1.05	-27.1%	-28.6%	-28.2%	-61.1%
28/2/2014	451	Same Time Holdings Limited	Subscription for new shares	4.00	-70.4%	-68.1%	-65.4%	-21.0%
11/3/2014	1060	China Vision Media Group Limited	Subscription of new shares	0.50	-21.9%	-8.8%	9.4%	159.3%
25/3/2014	1868	Neo-Neon Holdings Limited	Issue of subscription shares	0.90	-50.0%	-50.0%	-50.5%	-42.1%
31/3/2014	1833	Intime Retail (Group) Company Limited	Subscription of new shares	7.5335	-13.7%	-15.4%	-14.3%	32.0%
31/3/2014	1833	Intime Retail (Group) Company Limited	Subscription of convertible bonds	7.9102	-9.4%	-11.1%	-10.1%	38.6%
10/4/2014	555	Rexlot Holdings Limited	Issue of convertible bonds	1.4070	34.0%	36.0%	44.4%	97.4%
1/5/2014	1101	China Rongsheng Heavy Industries Group Holdings Limited	Issue of convertible bonds	1.07	-20.1%	-20.9%	-20.9%	-4.5%
14/5/2014	651	China Ocean Shipbuilding Industry Group Limited	Issue of convertible bonds	0.20	-33.3%	-21.3%	-12.7%	N/A
14/5/2014	267	CITIC Pacific Limited	Share subscription	13.48	-1.8%	-0.6%	-0.8%	-54.6%
27/5/2014	1165	Shunfeng Photovoltaic International Limited	Placing of new shares	10.00	-8.9%	-6.3%	-9.4%	840.2%
2/6/2014	2389	Genvon Group Limited	Placing of new shares	0.25	-43.2%	-41.3%	-42.9%	51.5%
11/6/2014	295	Kong Sun Holdings Limited	Subscription of new shares	0.36	-59.6%	-59.2%	-58.9%	119.2%
11/7/2014	899	Asia Resources Holdings Limited	Placing of convertible notes	0.38	5.6%	5.0%	4.1%	-85.5%
14/8/2014	1236	National Agricultural Holdings Limited	Placing of new shares	3.04 *(Note 2)*	4.8%	4.1%	5.4%	254.7%

Date of announcement	Stock code	Company	Transaction type	Subscription /placing /conversion price *(HK$)*	Premium/ (discount) over/ to the closing price of the shares as at the last trading day prior to the date of the corresponding announcement	Premium/ (discount) over/ to the closing price of the shares for the last 5 consecutive trading days	Premium/ (discount) over/ to the closing price of the shares for the last 10 consecutive trading days	Premium/ (discount) over/ to the net asset value per share *(Note 1)*
22/8/2014	1004	Rising Development Holdings Limited	Issue of convertible bonds	3.39	-19.1%	-19.9%	-21.3%	545.4%
25/8/2014	307	Up Energy Development Group Limited	Placing of new shares	1.00	-8.3%	-8.6%	-4.3%	-67.4%
28/8/2014	269	China Resources and Transportation Group Limited	Issue of convertible bonds	0.40	21.2%	24.6%	21.2%	113.1%
4/9/2014	721	China Financial International Investments Limited	Subscription of new shares	0.20	-66.7%	-65.4%	-63.9%	5.3%
17/9/2014	85	China Electronics Corporation Holdings Company Limited	Placing of new shares	1.63	-15.1%	-16.8%	-14.2%	447.7%
18/9/2014	967	Sound Global Limited	Subscription of new shares	8.10	-9.2%	-7.3%	-3.3%	139.8%
		Mean			-20.9%	-19.3%	-17.2%	137.3%
		Median			-15.1%	-15.4%	-12.7%	51.5%
		Max			34.0%	36.0%	44.4%	840.2%
		Min			-70.4%	-68.1%	-65.4%	-85.5%
		The Subscription		**0.32**	**-41.8%**	**-28.3%**	**-25.4%**	**-65.6%**

Source: Website of the Stock Exchange

Notes:

1. The net asset value of the Market Comparables are extracted from their annual reports of the latest financial year, where figures in RMB are translated at an exchange rate of RMB1 = HK$1.2719. The net asset value of Market Comparables that recorded a net liability position is shown as not applicable ("N/A").

2. The placing price of HK$3.04 is the average of the high-end and the low-end of the placing price range.

The Transaction Comparables show on average (i) a discount of approximately 20.9% to the closing price of the last trading day prior to the date of the corresponding announcement; (ii) a discount of approximately 19.3% to the closing prices of the last five consecutive trading days prior to the date of the corresponding announcement; and (iii) a discount of approximately 17.2% to the closing prices of the last ten consecutive trading days prior to the date of the corresponding announcement.

As previously discussed in the paragraph headed "Historical performance of Share price", we note that there were unusual price movements on the Last Trading Day where the adjusted closing price per Consolidated Share increased by approximately 27.9% to HK$0.550 per Consolidated Share. As such, we consider that such price movements have distorted the discount of the Issue Price and the Conversion Price to the closing price of the Last Trading Day that renders such comparison less meaningful and accordingly we consider examining the discount to closing prices of the last five and ten consecutive trading days serves as a better means in determining the fairness and reasonableness of the Issue Price and the Conversion Price.

Upon comparison, we note that the Issue Price and the Conversion Price represent a discount of approximately 28.3% and 25.4% to the closing prices of the last five and ten consecutive trading days ended on the Last Trading Day respectively, which are deeper than the means of the Transaction Comparables being approximately 19.3% and 17.2% respectively, but still fall within the ranges of the discounts/premiums of the Transaction Comparables. We further note that among all the Transaction Comparables approximately one-third of them asked for a discount of over 30% to the closing price of the last trading day. Based on the above, and taking into account the worsening financial position and performance of the Group which would be less appealing to potential investors, and the lack of alternative fund raising methods available to the Company, we are of the view that it is understandable for the Company to increase the attractiveness by offering investors a deeper discount to the historical Share price and thus we consider that the Issue Price and the Conversion Price are fair and reasonable.

The Issue Price and the Conversion Price represents a discount to the net asset value per Consolidated Share of approximately 65.6%, which is considerably deeper than the mean and the median of the Transaction Comparables. Nevertheless, considering (i) historically since 25 August 2012 the market price of the Shares have been trading at an discount ranging from approximately 22.2% to 64.6% to the then net asset value per Share at all times as discussed in the paragraph headed "Historical discount of market price to net asset value per Share" above; (ii) the worsening financial performance and position of the Group, in particular the consistent net current liability position and high gearing of the Group; (iii) the immediate improvement in the Group's gearing, liquidity and working capital upon the completion of the Subscription; and (iv) such discount to the net asset value per Share still falls within the range of the Transaction Comparables, we are of the view that it is also understandable for the Company to increase the attractiveness to investors by offering a deeper discount to the net asset value per Share and accordingly we consider the Issue Price and the Conversion Price are fair and reasonable so far as Independent Shareholders are concerned.

Comparison of the terms (excluding the conversion price) of the Conversion Bonds

Date of announcement	Stock code	Company	Conversion price *(HK$)*	Maturity *(years)*	Interest rate *(per annum)*	Effective interest rate *(per annum)*
6/1/2014	986	China Environmental Energy Investment Limited	2.50	2.0	1.0%	1.0%
25/2/2014	1101	China Rongsheng Heavy Industries Group Holdings Limited	1.05	2.5	7.0%	7.0%
31/3/2014	1833	Intime Retail (Group) Company Limited	7.9102	3.0	1.5%	1.5%
10/4/2014	555	Rexlot Holdings Limited	1.4070	5.0	4.5%	4.5%
1/5/2014	1101	China Rongsheng Heavy Industries Group Holdings Limited	1.07	2.5	7.0%	7.0%
14/5/2014	651	China Ocean Shipbuilding Industry Group Limited	0.20	3.0	7.5%	7.5%
11/7/2014	899	Asia Resources Holdings Limited	0.38	2.0	12.0%	12.4%
22/8/2014	1004	Rising Development Holdings Limited	3.39	2.0	3-month HIBOR[1] + 5.5%	6.0%
28/8/2014	269	China Resources and Transportation Group Limited	0.40	3.0	9.0%	9.0%
		Mean		2.9	5.8%	6.2%
		Median		2.5	7.0%	7.0%
		Maximum		5.0	12.0%	12.4%
		Minimum		2.0	1.0%	1.0%
		The Convertible Bonds	**0.32**	**10.0**	**7.0%**	**7.0%**

Source: Website of the Stock Exchange

Notes:

1. The 3-month Hong Kong Interbank Offered Rate ("HIBOR") was 0.37% per annum as quoted by the Hong Kong Association of Banks as at the date of the company's announcement.

The above table sets forth the major terms of the convertible bonds issued by the Transaction Comparables companies (the "**CB Comparables**"). We note that the maturity term of the Convertible Bonds of 10 years is considerably above the range and the mean of the CB Comparables. We consider a longer maturity term could delay the one-off repayment of principal amount of the Convertible Bonds and increase the probability of the holder(s) of the Convertible Bonds for conversion which may help to reduce the financial burden of the Group in the upcoming 10 years' period. We also note that the Convertible Bonds carry 7% effective interest rate per annum which is equal to the median of the CB Comparables and mildly higher than the mean of the CB Comparables being approximately 6.2%. We consider the issue of Convertible Bonds allows the Group to raise a considerable amount of fund at a relatively low finance cost. Having considered the size, the maturity term and the interest rate of the Convertible Bonds which are favourable to the Group, we consider the terms of the Convertible Bonds is in the interest of the Company and its Shareholders.

Despite the Issue Price and the Conversion Price of the Convertible Bonds represents moderate discounts to the adjusted closing prices of the Consolidated Shares, having considered (i) the benefits of the Subscription to the Group as discussed in the section headed "Background to and reasons for the Subscription Agreement"; (ii) the thin liquidity in the trading of the Existing Shares in the Review Period; (iii) the discounts of the Issue Price and the Conversion Price to the adjusted closing prices of the Consolidated Shares fall within the range of the Transaction Comparables; (iv) the terms of the Convertible Bonds (excluding the Conversion Price) are favourable to the Group and similar to those of the CB Comparables; (v) the historical discount of Share price to the net asset value per Share; (vi) the P/B ratio of the Subscription falls within the range of the Market Comparables; and (vii) the deeper discount would increase the attractiveness and willingness to potential investors for injection of funds into the Company, we consider that the Issue Price and the Conversion Price of the Convertible Bonds are fair and reasonable so far as the Company and the Independent Shareholders are concerned.

(iv) **Financial impact of the Subscription**

Working capital/cash flow

As per the interim report of the Company for the six months ended 30 June 2014, the Group had cash and cash equivalents of approximately RMB117.0 million and net current liabilities of approximately RMB1,183.0 million. Upon completion of the Subscription, the liquidity and cash position of the Group would be substantially improved as the Subscription will raise estimated net proceeds of approximately HK$1.02 billion. The Group's bank balances would substantially increase and the net current liabilities position of the Group would be greatly improved subject to all other things remaining unchanged. As such we are of the view that the Group's available working capital and net current liabilities are expected to be significantly improved upon completion of the Subscription.

Earnings

Given the net proceeds from the Subscription will substantially strengthen the Group's capital position and partly will be used for repaying and renewing the Group's existing borrowings, the Company would be at a better position to negotiate for lower interest rates from banks when the Company renews its existing loans. As a result the Group's interest expense obligation could be reduced which in turn will benefit the earnings of the Company. However immediately upon completion of the Subscription Agreement and assuming no conversion of the Convertible Bonds during its tenure, the Convertible Bonds would charge an interest expense to the Company at the rate of 7% per annum on the outstanding principal amount of the Convertible Bonds. In addition, according to the relevant accounting standard in Hong Kong, the discount of conversion price to market price will be recorded as fair value changes in relation to the issue of the Convertible Bonds and thus is likely to have a material immediate negative impact to the earnings of the Group.

Net asset value

As per the interim report of the Company for the six months ended 30 June 2014, as at 30 June 2014 the Group's net asset value (excluding non-controlling interest) was approximately RMB1,046.0 million and the net asset value per Consolidated Share was approximately RMB0.73. Upon completion of the Subscription and based on the estimated net proceeds of approximately HK$1.02 billion, the Group's net asset value immediately after the Subscription would increase by roughly such amount. Upon full exercise of the conversion rights attached to the Convertible Bonds, we estimate the Group's net asset value per Consolidated Share would decrease. We are of the view that such decrease in net asset value per Consolidated Share upon full exercise of the conversion rights attached to the Convertible Bonds is acceptable given the Subscription will greatly replenish the Group's working capital and improve the Group's financial position as well as provide additional capital resources to the Group's upcoming expansion projects.

Gearing

As previously discussed in the section headed "Information on the Group — Financial information of the Group", the Group's gearing ratios were approximately 356.3%, 358.4% and 256.8% as at 30 June 2014, 31 December 2013 and 2012 respectively. Upon completion of the Subscription, the Group's total equity attributable to owners of the Company would considerably increase, which is expected to result in a drop in the Group's gearing ratio. Given the above we are of the view that the Group's gearing ratio will be improved upon completion of the Subscription.

Based on the foregoing, the Subscription would have an overall positive effect on the Group's financial position upon completion of the Subscription. On such basis, we are of the view that the Subscription is in the interests of the Company and the Shareholders as a whole.

(v) **Effect on the shareholding structure of the Company**

Reference is made to the shareholding structure of the Company as set out in the section headed "Effect on Shareholding of the Company Following Completion of the Issue of New Shares and the Conversion Shares" in the Letter from the Board. Upon issue of the New Shares, the shareholding of the public Shareholders will be diluted from approximately 57.11% to approximately 37.91%. The shareholding of the public Shareholders will be further diluted to approximately 18.11% upon full exercise of the conversion rights attached to the Convertible Bonds (for illustration purpose only as no Conversion Share will be issued if the public float of the Company will fall below 25%).

Taking into account the above factors, in particular, the following:

(i) the worsening financial performance and position of the Group, including the consistent net current liabilities position of the Company for the three years ended 31 December 2013 and the six months ended 30 June 2014, the loss for the year recorded in FY2013 and the six months ended 30 June 2014 and the net operating cash outflow in FY2013;

(ii) the lack of alternate fund raising method available to the Company;

(iii) the generally thin liquidity in the trading of the Existing Shares in the Review Period;

(iv) the Subscription will greatly strengthen the Company's capital base and working capital position as well as the net asset position and gearing position of the Group;

(v) the fairness and reasonableness of the Issue Price and the Conversion Price of the Convertible Bonds of HK$0.32 in the section headed "Principal terms of the Subscription Agreement" above;

(vi) the proposed use of proceeds to finance the Group's first phase and second phase expansion projects at the Group's Guangan and Dazhou factories as discussed in the section "Background to and reasons for the Subscription Agreement" above,

we consider that the Subscription is an acceptable mean of fund raising by the Company and the shareholding dilution effects upon completion of the Subscription is acceptable so far as the Independent Shareholder are concerned.

THE WHITEWASH WAIVER

Upon the issue of the New Shares and full conversion of the Convertible Bonds, assuming that there is no other change in the issued share capital of the Company, the Subscriber will be interested in aggregate 3,400,636,000 Consolidated Shares, representing approximately 215.25% of the Consolidated Shares in issue upon the Share Consolidation has become effective, and approximately 68.29% of the Consolidated Shares in issue as enlarged by the issuance of the New Shares and the Conversion Shares.

Under Rule 26 of the Takeovers Code, the acquisition of voting rights from less than 30% of voting rights to 30% or more will trigger an obligation on the Subscriber and persons acting in concert with it to make a general offer for all the securities of the Company other than those already owned or agreed to be acquired by them, unless the Whitewash Waiver is granted by the Executive and approved by the Independent Shareholders at the EGM by way of poll. The Subscriber has made an application to the Executive for the Whitewash Waiver in respect of the Subscription Agreement and the allotment and issue of the Conversion Shares upon full conversion of the Convertible Bonds. The Whitewash Waiver will be subject to, among other things, approval by the Independent Shareholders at the EGM by way of poll.

The Independent Shareholders should note that if the Whitewash Waiver is approved by the Independent Shareholders, the shareholding of the Subscriber in the Company upon the issue of the New Shares and the Conversion Shares to the Subscriber will exceed 50%. The Subscriber may further increase its shareholdings in the Company without incurring any further obligations under Rule 26 of the Takeovers Code to make a general offer.

The Independent Shareholders should also note that the grant and approval of the Whitewash Waiver is condition precedent to the completion of the Subscription Agreement. In the case where the Subscription Agreement is approved by the Independent Shareholders in the EGM and the Whitewash Waiver is not granted or approved by the Independent Shareholders, the Subscriber reserves its right as to whether or not to waive such condition. If the Subscriber waives such condition, it will comply with the provisions of the Takeovers Code to make a general offer under Rule 26.1 of the Takeovers Code. Mr. Li, the existing controlling shareholder of the Company, has undertaken to the Subscriber that in the event that the Subscriber makes a mandatory general offer for all the securities of the Company other than those already owned or agreed to be acquired by them under Rule 26 of the Takeovers Code, he will not accept or procure the acceptance of such offer for the securities in the Company he holds. As at the Latest Practicable Date, Mr. Li is interested in 2,924,440,000 Existing Shares, representing approximately 37.02% of the Existing Shares in issue.

Having considered the benefits of the Subscription as mentioned in the previous sections in this letter, in particular, (i) the Subscription is a reasonable financing means available to the Group; (ii) the Subscription would strengthen the Group's capital base and working capital position and provide funding for the Group's expansion projects; (iii) the dilution effect to the Independent Shareholders as a result of the Subscription is acceptable and unavoidable ; (iv) the Subscription would have an overall positive effect on the financial position of the Group in terms of the net asset value, cash flows and gearing upon completion of the Subscription, and (v) all the other factors as discussed under the section headed "Principal factors and reasons considered" above, we are of the view that the granting of the Whitewash Waiver is fair and reasonable and in the interests of the Company and the Shareholders as a whole as far as the Independent Shareholder are concerned.

RECOMMENDATION

Having considered the principal factors and reasons, in particular,

(i) the worsening financial performance and position of the Group, including the consistent net current liabilities position of the Company for the three years ended 31 December 2013 and the six months ended 30 June 2014, the loss for the year recorded in FY2013 and the six months ended 30 June 2014 and the net operating cash outflow recorded in FY2013;

(ii) the lack of alternate fund raising method available to the Company;

(iii) the Subscription provides an immediate and effective means for the Group to replenish its working capital and reduce its interest obligations, as well as improve the net asset position and gearing position of the Group;

(iv) the proposed use of proceeds to finance the Group's first phase and second phase expansion projects at the Group's Guangan and Dazhou factories as discussed in the section "Background to and reasons for the Subscription Agreement" above;

(v) the generally thin liquidity in the trading of the Existing Shares in the Review Period;

(vi) the fairness and reasonableness of the Issue Price and the Conversion Price as discussed in the section headed "Principal terms of the Subscription Agreement" above;

(vii) the shareholding dilution effects upon completion of the Subscription is acceptable; and

(viii) the grant and approval of the Whitewash Waiver is condition precedent to the completion of the Subscription Agreement,

we are of the opinion that the terms of the Subscription Agreement and the Whitewash Waiver are fair and reasonable so far as the Independent Shareholders are concerned and are in the interests of the Company and the Shareholders as a whole. Accordingly, we recommend the Independent Shareholders, and the Independent Board Committee to advise the Independent Shareholders, to vote in favour of the ordinary resolutions to be proposed at the EGM for approving the Subscription Agreement and the Whitewash Waiver.

Yours faithfully,
For and on behalf of
Octal Capital Limited

Alan Fung	**Louis Chan**
Managing Director	*Director*

Note: Mr. Alan Fung has been a responsible officer of Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities since 2003. Mr. Fung has more than 20 years of experience in corporate finance and investment banking and has participated in and completed various advisory transactions in respect of mergers and acquisitions, connected transactions and transactions subject to the compliance to the Takeovers Code of listed companies in Hong Kong. Mr. Louis Chan has been a responsible officer of Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities since 2008. Mr. Chan has more than 10 years of experience in corporate finance and investment banking and has participated in and completed various advisory transactions in respect of mergers and acquisitions, connected transactions and transactions subject to the compliance to the Takeovers Code of listed companies in Hong Kong.

1. FINANCIAL SUMMARY

The following is a summary of the consolidated results and financial information of the Group for the three years ended 31 December 2011, 2012 and 2013 and the six months ended 30 June 2014, details of which were extracted from the annual reports of the Company for each of the years ended 31 December 2011, 2012 and 2013 and the interim report of the Company for the six months ended 30 June 2014:

	For the year ended 31 December			For the six months ended 30 June
	2011	**2012**	**2013**	**2014**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
		(audited)		*(unaudited)*
Turnover	1,426,888	1,346,970	1,339,252	738,166
Cost of sales	(1,144,540)	(1,019,752)	(1,202,342)	(686,160)
Gross profit	282,348	327,218	136,910	52,006
(Loss)/Profit before taxation	105,783	128,598	(64,257)	(27,254)
Income tax benefit/(expense)	(5,629)	(26,986)	6,868	4,172
Profit for the year/the period attributable to:				
Equity holders of the Company	100,154	101,612	(57,056)	(23,082)
Non-controlling interests	—	—	(333)	—
(Loss)/Profit per share attributable to equity holders of the Company (expressed in RMB per share)				
- Basic	0.0140	0.0141	(0.0079)	(0.0032)
- Diluted	0.0138	0.0141	(0.0079)	(0.0032)
Dividends				
Dividend	—	—	—	—
Dividend per share (RMB)	—	—	—	—

The auditors of the Company for each of the three years ended 31 December 2011, 2012 and 2013, PricewaterhouseCoopers, did not issue any qualified opinion on the financial statements of the Group for each of the three years ended 31 December 2011, 2012 and 2013.

The Group did not have any items which are exceptional because of size, nature or incidence for each of the three years ended 31 December 2011, 2012 and 2013 and for the six months ended 30 June 2014.

2. AUDITED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2013

The following information is extracted from the audited financial statements of the Group as set out in the annual report of the Company for the year ended 31 December 2013:

Consolidated Balance Sheet

		As at 31 December	
		2013	**2012**
	Note	*RMB'000*	*RMB'000*
Assets			
Non-current assets			
Land use rights	5	53,027	54,216
Property, plant and equipment	6	2,568,621	2,087,704
Investment properties	7	13,654	—
Mining right	8	334,306	334,306
Other intangible assets	9	10,898	11,168
Deferred income tax assets	21	10,208	2,111
		2,990,714	2,489,505
Current assets			
Inventories	11	43,259	58,631
Trade and other receivables	12	360,905	112,908
Prepaid income tax, net		7,300	4,536
Pledged bank deposits	13	1,726,298	1,228,847
Cash and cash equivalents	14	116,683	350,752
		2,254,445	1,755,674
Non-current assets held for sale	15	198,784	198,784
		2,453,229	1,954,458
Total assets		5,443,943	4,443,963
EQUITY			
Capital and reserves attributable to the equity holders of the Company			
Share capital	16	138,618	138,618
Reserves	17	930,414	979,454
		1,069,032	1,118,072

	Note	As at 31 December 2013 RMB'000	2012 RMB'000
Non-controlling interest	17	3,267	3,600
Total equity		1,072,299	1,121,672
LIABILITIES			
Non-current liabilities			
Long-term borrowings	18	1,040,218	808,324
Derivative financial liabilities	19	—	36,530
Deferred subsidy income	20	3,892	4,546
Deferred income tax liabilities	21	86,352	86,352
		1,130,462	935,752
Current liabilities			
Trade and other payables	22	419,606	323,480
Short-term borrowings	23	2,583,575	1,933,961
Current portion of long-term borrowings	18	207,510	129,098
Derivative financial liabilities	19	30,491	—
		3,241,182	2,386,539
Total liabilities		4,371,644	3,322,291
Total equity and liabilities		5,443,943	4,443,963
Net current liabilities		(787,953)	(432,081)
Total assets less current liabilities		2,202,761	2,057,424

Li Weiruo *Director*

Yuan Bai *Director*

The notes on pages 74 to 140 are an integral part of these consolidated financial statements.

Balance Sheet

		As at 31 December	
		2013	**2012**
	Note	*RMB'000*	*RMB'000*
Assets			
Non-current assets			
Interests in subsidiaries	10	750,770	744,902
Loan to subsidiaries	10	116,564	110,992
		867,334	855,894
Current assets			
Trade and other receivables	12	476	476
Cash and cash equivalents	14	85	168
		561	644
Total assets		867,895	856,538
EQUITY			
Capital and reserves attributable to equity holders of the Company			
Share capital	16	138,618	138,618
Reserves	17	609,813	603,201
Total equity		748,431	741,819

		As at 31 December	
		2013	**2012**
	Note	*RMB'000*	*RMB'000*
LIABILITIES			
Non-current liabilities			
Long-term borrowings	18	73,863	65,223
Derivative financial liabilities	19	—	36,530
		73,863	101,753
Current liabilities			
Accruals and other payables	22	461	1,142
Current portion of long-term borrowings	18	14,649	11,824
Derivative financial liabilities	19	30,491	—
		45,601	12,966
Total liabilities		119,464	114,719
Total equity and liabilities		867,895	856,538
Net current liabilities		(45,040)	(12,322)
Total assets less current liabilities		822,294	843,572

Li Weiruo
Director

Yuan Bai
Director

The notes on pages 74 to 140 are an integral part of these consolidated financial statements.

Consolidated Statement of Comprehensive Income

		Year ended 31 December	
		2013	**2012**
	Note	*RMB'000*	*RMB'000*
Turnover	24	1,339,252	1,346,970
Cost of sales	25	(1,202,342)	(1,019,752)
Gross profit		136,910	327,218
Distribution costs	25	(54,134)	(54,463)
Administrative expenses	25	(73,847)	(63,993)
Other income — net	28	9,273	13,340
Operating profit		18,202	222,102
Finance income	29	47,267	26,859
Finance expenses	29	(129,726)	(120,363)
Finance expenses — net	29	(82,459)	(93,504)
(Loss)/Profit before income tax		(64,257)	128,598
Income tax benefit/(expense)	30	6,868	(26,986)
(Loss)/Profit for the year		(57,389)	101,612
Other comprehensive income		—	—
Total comprehensive (loss)/income for the year		(57,389)	101,612
Attributable to:			
Equity holders of the Company		(57,056)	101,612
Non-controlling interests		(333)	—
		(57,389)	101,612
(Loss)/Profit per share attributable to the equity holders of the Company during the year (expressed in RMB per share)			
— Basic	32	(0.0079)	0.0141
— Diluted	32	(0.0079)	0.0141
Dividend	33	—	—

The notes on pages 74 to 140 are an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

		Attributable to equity holders of the Company				
		Share capital	**Reserves**	**Total**	**Non-controlling interests**	**Total equity**
	Note	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Balance at 1 January 2012		138,618	881,442	1,020,060	—	1,020,060
Comprehensive income:						
Profit for the year		—	101,612	101,612	—	101,612
Total comprehensive income		—	101,612	101,612	—	101,612
Transactions with equity holders:						
Transfer of equity interest to non-controlling interests	17	—	(3,600)	(3,600)	3,600	—
		—	(3,600)	(3,600)	3,600	—
Balance at 31 December 2012		138,618	979,454	1,118,072	3,600	1,121,672
Balance at 1 January 2013		138,618	979,454	1,118,072	3,600	1,121,672
Comprehensive income:						
Loss for the year		—	(57,056)	(57,056)	(333)	(57,389)
Total comprehensive loss		—	(57,056)	(57,056)	(333)	(57,389)
Transactions with equity holders:						
Employee share option scheme:						
— Value of employees services	17	—	8,016	8,016	—	8,016
		—	8,016	8,016	—	8,016
Balance at 31 December 2013		138,618	930,414	1,069,032	3,267	1,072,299

The notes on pages 74 to 140 are an integral part of these consolidated financial statements.

Consolidated Cash Flow statement

		Year ended 31 December	
		2013	**2012**
	Note	*RMB'000*	*RMB'000*
Cash (used in)/generated from operating activities	34(a)	(9,412)	286,560
Interest paid		(122,078)	(110,805)
Income tax paid		(3,993)	(27,673)
Net cash (used in)/generated from operating activities		(135,483)	148,082
Cash flows from investing activities			
Purchases of property, plant and equipment and payments for construction-in-progress		(578,494)	(608,714)
Proceeds from disposal of property, plant and equipment	34(b)	350	—
Interest income received		34,732	26,639
Net cash used in investing activities		(543,412)	(582,075)
Cash flows from financing activities			
Increase in pledged bank deposits		(497,451)	(439,838)
Proceeds from borrowings		2,008,270	1,905,625
Repayment of borrowings		(1,065,648)	(813,136)
Net cash generated from financing activities		445,171	652,651
Net (decrease)/increase in cash and cash equivalents		(233,724)	218,658
Cash and cash equivalents at beginning of the year		350,752	132,094
Exchange losses on cash and cash equivalents		(345)	—
Cash and cash equivalents at end of the year	14	116,683	350,752

The notes on pages 74 to 140 are an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1 GENERAL INFORMATION

Ko Yo Chemical (Group) Limited (the "Company") was incorporated in the Cayman Islands on 11 February 2002 as an exempted company with limited liability under the Companies Law Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands. Its shares had been listed on the Growth Enterprise Market (the "GEM") of the Stock Exchange of Hong Kong Limited (the "Stock Exchange") since 10 July 2003 (the "Listing"). On 25 August 2008, the Company transferred the listing of its shares from GEM of the Stock Exchange to the Main Board of the Stock Exchange ("Transfer of Listing").

The address of the registered office of the Company is Cricket Square, Hutchins Drive, P.O. Box 2681, Grand Cayman KY1-1111, Cayman Islands and the principal place of business of the Company is Suite No. 02, 31st Floor, Sino Plaza, 255-257 Gloucester Road, Causeway Bay, Hong Kong.

The Company is an investment holding company. The Company and its subsidiaries (the "Group") are principally engaged in the manufacture and sale of chemical products and chemical fertilisers in Mainland China.

These consolidated financial statements are presented in Renminbi ("RMB"), unless otherwise stated. These consolidated financial statements have been approved for issue by the Board of Directors on 24 March 2014.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

The Group incurred a consolidated net loss of approximately RMB57,389,000 (2012: consolidated net profit of RMB101,612,000) during the year ended 31 December 2013 and had a net operating cash outflows of approximately RMB135,483,000 (2012: net operating cash inflows of RMB148,082,000), and as at that date, the Group's current liabilities exceeded its current assets by approximately RMB787,953,000 (2012: RMB432,081,000). These conditions indicate the existence of a material uncertainty which may cast significant doubt about the Group's ability to continue as a going concern.

The directors of the Company have assessed the appropriateness of adopting the going concern basis for the preparation of the financial statements for the year ended 31 December 2013 in light of the Group's plans and measures described below to improve its financing and operating cash flows:

— As at 31 December 2013, the Group's total borrowings amounted to RMB3,831 million, of which RMB2,791 million will be due within 12 months from 31 December 2013. As at that date, the Group's bank deposits pledged for long-term borrowings and short-term borrowings amounted to RMB301 million and RMB1,414 million, respectively. The Group has not experienced any significant difficulties in renewing its short-term borrowings upon their maturities and there is no indication that the banks will not renew the existing short-term borrowings upon the Group's request. Subsequent to the balance sheet date and up to the date of approval of the financial statements, the Group has renewed short-term borrowings of approximately RMB170 million for another 12 months, and has obtained a new short-term borrowing of RMB80 million with a term of 6 months. In addition, certain banks have advised their intention in writing, though not legally binding, to renew loans to the Group for another 12 months when they fall due in 2014 or to provide new loans, totalling approximately RMB1,101 million which require no pledged bank deposits or other collateral. Therefore, the directors of the Company believe that the Group will be able to renew its existing short-term borrowings upon maturity.

— The Group is expected to generate adequate operating cash inflows in 2014 from its existing production facilities as well as the newly completed production facilities located in GuangAn, Sichuan Province ("GuangAn Project"). As at the date of approval of these financial statements, construction of GuangAn Project has already been completed and it is ready to be put into operation. Subject to the finalisation of certain commercial terms in contract with the Company's natural gas (major raw materials) supplier, the directors of the Company expect that GuangAn Project will commence commercial operation in mid-2014. The directors also expect that sufficient sales orders will be secured in the coming year such that adequate operating cash inflows will be generated by the existing production facilities and GuangAn Project.

In the opinion of the directors, in light of the above, the Group will have sufficient working capital to finance its operations and fulfill its financial obligations as and when they fall due in the coming 12 months from the date of the financial statements. Accordingly, the directors are satisfied that it is appropriate to prepare the financial statements on a going concern basis.

Notwithstanding the above, significant uncertainties exist as to whether management of the Company will be able to achieve its plans and measures as described above. Whether the Group will be able to continue as a going concern would depend upon the Group's ability to generate adequate financing and operating cash inflows through renewal of its current bank loans upon expiry and obtaining additional bank financing as needed, securing the gas supply for its GuangAn Project on time at terms that are acceptable to the Group, and securing adequate sales orders during the coming year for the Group's existing and new production facilities. Should the Group be unable to achieve the above plans and measures such that it would not be able to operate as a going concern, adjustments would have to be made to write down the value of assets to their recoverable amounts, to provide for any future liabilities which might arise, and to reclassify non-current assets and non-current liabilities as current assets and current liabilities, respectively. The effect of these adjustments has not been reflected in the consolidated financial statements.

The consolidated financial statements of the Group have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRS") issued by the Hong Kong Institute of Certified Public Accountants. The consolidated financial statements have been prepared under the historical cost convention, as modified by the financial liabilities (including derivative instruments) at fair value through profit or loss.

The preparation of financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

Changes in accounting policy and disclosures

(a) *New and amended standards adopted by the Group*

There are no new standards or amendments to standards that are effective for the first time for the financial year beginning on 1 January 2013 that would be expected to have a material impact on the Group.

(b) *New standards, amendments and interpretations have been issued but are not effective for the financial year beginning 1 January 2013 and have not been early adopted by the Group*

Other than as disclosed below, there are no new standards or amendments to standards that are effective for the first time for the financial year beginning after 1 January 2013 that would be expected to have a material impact on the Group.

- HKFRS 9, 'Financial instruments' addresses the classification, measurement and recognition of financial assets and financial liabilities. HKFRS 9 was issued in November 2009 and October 2010. It replaces the parts of HKAS 39 that relate to the classification and measurement of financial instruments. HKFRS 9 requires financial assets to be classified into two measurement categories: those measured as at fair value and those measured at amortised cost. The determination is made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument. For financial liabilities, the standard retains most of the HKAS 39 requirements. The main change is that, in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than the income statement, unless this creates an accounting mismatch. The Group is yet to assess HKFRS 9's full impact.

2.2 **Subsidiaries**

2.2.1 ***Consolidation***

A subsidiary is an entity (including a structured entity) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

(a) *Business combinations*

The Group applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The Group recognises any non-controlling interest in the acquiree on an acquisition-by-acquisition basis, either at fair value or at the non-controlling interest's proportionate share of the recognised amounts of acquiree's identifiable net assets.

Acquisition-related costs are expensed as incurred.

If the business combination is achieved in stages, the acquisition date carrying value of the acquirer's previously held equity interest in the acquiree is re-measured to fair value at the acquisition date; any gains or losses arising from such re-measurement are recognised in profit or loss.

Any contingent consideration to be transferred by the Group is recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration that is deemed to be an asset or liability is recognised in accordance with HKAS 39 either in profit or loss or as a change to other comprehensive income. Contingent consideration that is classified as equity is not remeasured, and its subsequent settlement is accounted for within equity.

The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill. If the total of consideration transferred, non-controlling interest recognised and previously held interest measured is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in the income statement (Note 2.11).

Intra-group transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated. When necessary, amounts reported by subsidiaries have been adjusted to conform with the Group's accounting policies.

(b) *Changes in ownership interests in subsidiaries without change of control*

Transactions with non-controlling interests that do not result in loss of control are accounted for as equity transactions — that is, as transactions with the equity holders in their capacity as equity holders. The difference between fair value of any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

(c) *Disposal of subsidiaries*

When the Group ceases to have control, any retained interest in the entity is re-measured to its fair value at the date when control is lost, with the change in carrying amount recognised in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other comprehensive income are reclassified to profit or loss.

2.2.2 ***Separate financial statements***

Investments in subsidiaries are accounted for at cost less impairment. Cost includes direct attributable costs of investment. The results of subsidiaries are accounted for by the Company on the basis of dividend received and receivable.

Impairment testing of the investments in subsidiaries is required upon receiving a dividend from these investments if the dividend exceeds the total comprehensive income of the subsidiary in the period the dividend is declared or if the carrying amount of the investment in the separate financial statements exceeds the carrying amount in the consolidated financial statements of the investee's net assets including goodwill.

2.3 **Segment reporting**

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the steering committee that makes strategic decisions.

2.4 **Foreign currency translation**

(a) ***Functional and presentation currency***

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Renminbi ("RMB"), which is the Company's functional and presentation currency.

(b) ***Transactions and balances***

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in profit or loss.

Foreign exchange gains and losses that relate to borrowings and cash and cash equivalents are presented in profit or loss within 'finance cost, net'. All other foreign exchange gains and losses are presented in profit or loss within 'other income — net'.

2.5 Property, plant and equipment

Property, plant and equipment are stated at historical cost less depreciation and any impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will follow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are expensed in profit or loss during the financial period in which they are incurred.

Depreciation of property, plant and equipment is calculated using the straight-line method to allocate their costs to their residual values over their estimated useful lives, as follows:

— Buildings	35 years
— Plant and machinery	12-14 years
— Motor vehicles	10 years
— Office equipment and others	7 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.11).

Construction in progress represents the direct costs of construction incurred of property, plant and equipment less any impairment losses. No provision for depreciation is made on construction in progress until such time the relevant assets are completed and ready for use. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

Gains and losses on disposals are determined by comparing proceeds with carrying amount and are recognised within 'other income — net' in the consolidated statement of comprehensive income.

2.6 Investment properties

Investment properties are interests in land and buildings that are held for long-term rental yields or for capital appreciation or both, rather than for use in the production or supply of goods or services or for administrative purposes.

Investment properties are initially measured at cost, which is the fair value of the consideration given to acquire them, including transaction costs. Subsequently, all investment properties are stated at cost less accumulated depreciation and accumulated impairment losses.

Depreciation is computed on a straight-line basis, after taking into account the estimated residual value (10% of original cost), over the estimated useful lives. The estimated useful lives of investment properties are 35 years.

The useful life and depreciation methods are reviewed periodically to ensure that the method and period of depreciation are consistent with the expected pattern of economic benefits from the individual investment properties.

Transfers to, or from, investment properties are made when, and only when, there is evidence of a change in use.

2.7 **Mining right**

Mining right is stated at cost less subsequent accumulated amortisation and accumulated impairment losses. Mining right is amortised using the units of production method based on the proven and probable mineral reserves.

2.8 **Land use rights**

Land use rights are up-front payments to acquire a long-term interest in land, which are regarded as operating leases. These payments are stated at cost and amortised over their respective lease terms on a straight-line basis, net of accumulated impairment charge.

The amortisation charge of land use rights on which a construction-in-progress is under development is capitalised during the construction period. Other amortisation charges are expensed.

2.9 **Non-current assets held-for-sale**

Non-current assets are classified as assets held for sale when their carrying amount is to be recovered principally through a sale transaction and a sale is considered highly probable. They are stated at the lower of carrying amount and fair value less costs to sell. Deferred tax assets, even if held for sale, would continue to be measured in accordance with the policies set out elsewhere in Note 2.24.

2.10 **Intangible assets**

(a) ***Goodwill***

Goodwill arises on the acquisition of subsidiaries, associates and joint ventures and represents the excess of the consideration transferred over the Group's interest in net fair value of the net identifiable assets, liabilities and contingent liabilities of the acquiree and the fair value of the non-controlling interest in the acquiree.

For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the cash-generating units ("CGUs"), or groups of CGUs, that is expected to benefit from the synergies of the combination. Each unit or group of units to which the goodwill is allocated represents the lowest level within the entity at which the goodwill is monitored for internal management purposes. Goodwill is monitored at the operating segment level.

Goodwill impairment reviews are undertaken annually or more frequently if events or changes in circumstances indicate a potential impairment. The carrying value of goodwill is compared to the recoverable amount, which is the higher of value in use and the fair value less costs to sell. Any impairment is recognised immediately as an expense and is not subsequently reversed.

(b) ***Construction permits***

Separately acquired construction permits are shown at historical cost. Construction permits have a finite useful life and are carried at cost less accumulated amortisation. Amortisation is calculated using the straight-line method to allocate the cost of construction permits over their estimated useful lives of 10 years.

2.11 **Impairment of interests in subsidiaries and non-financial assets**

Assets that have an indefinite useful life — for example, goodwill or intangible assets — are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered a impairment is reviewed for possible reversal of the impairment at each reporting date.

2.12 **Financial assets**

2.12.1 ***Classification***

The Group classifies its financial assets in the following categories: loans and receivables. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition. During 2012 and 2013, other than loans and receivables, the Group did not hold any financial assets in other categories.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for the amounts that are settled or expected to be settled more than 12 months after the end of the reporting period. These are classified as non-current assets. The Group's loans and receivables comprise 'trade and other receivables' and 'cash and cash equivalents' in the balance sheet (Notes 2.16 and 2.17).

2.12.2 ***Recognition and measurement***

Regular way purchases and sales of financial assets are recognised on the trade-date-the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss are initially recognised at fair value, and transactions costs are expensed in the income statement. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Loans and receivables are subsequently carried at amortised cost using the effective interest method.

2.13 **Offsetting financial instruments**

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

2.14 **Impairment of financial assets carried at amortised cost**

The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation, and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

The Group first assesses whether objective evidence of impairment exists.

For loans and receivables category, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognised in the consolidated statement of comprehensive income. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the reversal of the previously recognised impairment loss is recognised in the consolidated statement of comprehensive income.

2.15 **Inventories**

Inventories comprise raw materials, finished goods and work in progress and are stated at the lower of cost and net realisable value. Cost, calculated on the weighted average basis, comprises materials, direct labour and an appropriate proportion of all production overhead expenditure (based on normal production capacity). It excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable distribution costs.

2.16 Trade and other receivables

Trade receivables are amounts due from customers for merchandise sold in the ordinary course of business. If collection of trade and other receivables is expected in 1 year or less (or in the normal operating cycle of the business if longer), they are classified as current assets. If not, they are presented as non-current assets.

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment.

2.17 Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of 3 months or less.

2.18 Share capital

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

2.19 Derivative financial liabilities

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value.

Warrants issued by the Company that will be settled by the exchange of a fixed amount of cash denominated in a currency other than the functional currency of the Company for a fixed number of the Company's own equity instruments are classified as derivative financial liability (warrant liability) and are initially and subsequently measured at fair value. The changes of fair value of warrant liability are recognised in the statement of comprehensive income within 'other income — net'. The full fair value of the warrant liability is classified as a non-current liability when the remaining maturity of the warrant is more than 12 months, and as a current liability when the remaining maturity of the warrant is less than 12 months. The warrant liability will be transferred to share capital and share premium upon exercise of the warrants.

2.20 Embedded derivatives

An embedded derivative is a component of a hybrid (combined) instrument that also includes a non-derivative host contract with the effect that some of the cash flows of the hybrid (combined) instrument vary in a way similar to a stand-alone derivative.

The Group separates embedded derivatives from the host contract and accounts for these as derivatives, if all of the following three conditions are met:

— The economic characteristics and risks of the embedded derivative are not closely related to those of the host contract;

— A separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and

— The hybrid (combined) instrument is not measured at fair value with changes in fair value recognised in the income statement.

These embedded derivatives separated from the host contract are measured at fair value with changes in fair value recognised in the income statement within "other income-net".

2.21 **Trade payables**

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within 1 year or less (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities.

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

2.22 **Borrowings**

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the consolidated statement of comprehensive income over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the end of reporting period.

2.23 **Borrowings Costs**

General and specific borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

2.24 **Current and deferred income tax**

The tax expense for the period comprises current and deferred tax. Tax is recognised in the profit and loss account, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Company and its subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax liabilities are not recognised if they arise from the initial recognition of goodwill, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit nor loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax liabilities are provided on taxable temporary differences arising on investments in subsidiaries, except for deferred income tax liability where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

2.25 **Employee benefits**

(a) ***Employee leave entitlements***

Employee entitlements to annual leave and long service leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave and long-service leave as a result of services rendered by employees up to the balance sheet date.

(b) ***Pension obligations***

In accordance with the rules and regulations in the Mainland China, the Mainland China based employees of the Group participate in various defined contribution plans organised by the relevant municipal and provincial governments in the Mainland China under which the Group and the Mainland China based employees are required to make monthly contributions to these plans calculated as a percentage of the employees' salaries (subject to a floor and cap).

The municipal and provincial governments undertake to assume the retirement benefit obligations of all existing and future retired Mainland China based employees payable under the plans described above. Other than the monthly contributions, the Group has no further obligation for the payment of retirement and other post-retirement benefits of its employees. The assets of these plans are held separately from those of the Group in independently administrated funds managed by the governments.

The Group also participates in a retirement benefit scheme under the rules and regulations of the Mandatory Provident Fund Scheme Ordinance ("MPF Scheme") for its eligible employees in Hong Kong. The contributions to the MPF Scheme borne by the Group are calculated at 5% of the salaries and wages (monthly contributions is limited to HK$1,000 for each eligible employee) as calculated under the MPF legislation. The assets of this MPF Scheme are held separately from those of the Group in independently administered funds.

The Group's contributions to the defined contribution plans are expensed as incurred.

(c) ***Termination benefits***

Termination benefits are payable when employment is terminated by the Group before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits at the earlier of the following dates: (a) when the Group can no longer withdraw the offer of those benefits; and (b) when the entity recognises costs for a restructuring that is within the scope of HKAS 37 and involves the payment of termination benefits. In the case of an offer made to encourage voluntary redundancy, the termination benefits are measured based on the number of employees expected to accept the offer. Benefits falling due more than 12 months after the end of the reporting period are discounted to their present value.

2.26 Share-based compensation

(a) ***Equity-settled share-based payment transactions***

The Group operates a number of equity-settled, share-based compensation plans, under which the entity receives services from employees as consideration for equity instruments (options) of the Group. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed is determined by reference to the fair value of the options granted:

- including any market performance conditions (for example, an entity's share price);

- excluding the impact of any service and non-market performance vesting conditions (for example, profitability, sales growth targets and remaining an employee of the entity over a specified time period); and

- including the impact of any non-vesting conditions (for example, the requirement for employees to save).

Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied.

In addition, in some circumstances employees may provide services in advance of the grant date and therefore the grant date fair value is estimated for the purposes of recognising the expense during the period between service commencement period and grant date.

At the end of each reporting period, the Group revises its estimates of the number of options that are expected to vest based on the non-marketing performance and service conditions. It recognises the impact of the revision to original estimates, if any, in the profit and loss account, with a corresponding adjustment to equity. The existing share options granted by the Group during the year 2013 were granted for the past services of employees and were vested immediately upon granted, therefore the total expenses were recognised immediately at the grant date.

When the options are exercised, the Company issues new shares. The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

The grant by the Company of options over its equity instruments to the employees of subsidiary undertakings in the Group is treated as a capital contribution. The fair value of employee services received, measured by reference to the grant date fair value, is recognised over the vesting period as an increase to investment in subsidiary undertakings, with a corresponding credit to equity.

2.27 **Provisions**

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

2.28 **Contingent liabilities**

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the consolidated financial statements. When a change in the probability of an outflow occurs so that the outflow becomes probable, it will then be recognised as a provision in the consolidated balance sheet.

2.29 **Revenue recognition**

Revenue is measured at fair value of the consideration received or receivable for the sale of goods in the ordinary course of the Group's activities. Revenue is shown net of value-added tax, returns, rebates and discounts and after eliminating sales within the Group.

The Group recognises revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and when specific criteria have been met for each of the Group's activities as described below. The Group bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

Revenue from the sale of goods is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are delivered to customers and title has passed.

Rental income from investment property is recognised in the income statement on a straight-line basis over the term of the lease.

Interest income is recognised using the effective interest method. When a loan and receivable is impaired, the Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at the original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans and receivables is recognised using the original effective interest rate.

Dividend income is recognised when the right to receive payment is established.

2.30 **Government grants**

Grants from the government are recognised at their fair value where there is a reasonable assurance that the grants will be received and the Group will comply with all attached conditions.

Government grants relating to costs are deferred and recognised in the consolidated statement of comprehensive income over the period necessary to match them with the costs that they are intended to compensate.

Government grants relating to the purchase of property, plant and equipment are included in non-current liabilities as deferred subsidy income and are recognised in the consolidated statement of comprehensive income on a straight-line basis over the expected lives of the related assets.

Government grants are recognised in the consolidated statement of comprehensive income as part of other income.

2.31 Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the consolidated statement of comprehensive income on a straight-line basis over the period of the lease.

2.32 Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Group's and the Company's financial statements in the period in which dividends are approved by the Company's shareholders.

3 FINANCIAL RISK MANAGEMENT

3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: market risk (including foreign exchange risk and cash flow and fair value interest rate risk), credit risk, and liquidity risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

(a) *Foreign exchange risk*

The Group exposes to foreign exchange risks as certain portion of cash and cash equivalent, trade and other receivables, trade and other payables, long-term borrowings, derivative financial liabilities and future commercial transactions are denominated in foreign currencies, primarily with respect to the US dollar ("USD") and Hong Kong dollar ("HKD"). The Group currently does not have a foreign currency hedging policy as the directors are of the opinion that the Group's exposure to foreign exchange risk is insignificant because the Group's transactions, assets and liabilities were mainly denominated in Renminbi (the "RMB"). However, the management monitors foreign exchange exposure and will consider hedging significant foreign currency exposure when it is necessary and appropriate.

As at 31 December 2013, if RMB had weakened/strengthened by 5% against the USD with all other variables held constant, post-tax loss for the year would have been increased/decreased by RMB2,216,000 (2012: post-tax profit for the year would have been decreased/increased by RMB3,019,000), mainly as a result of foreign exchange losses/gains on translation of the USD-denominated long-term borrowings.

As at 31 December 2013, if RMB had weakened/strengthened by 5% against the HKD with all other variables held constant, post-tax loss for the year would have been increased/decreased by RMB2,067,000 (2012: post-tax profit for the year would have been decreased/increased by RMB3,303,000), mainly as a result of foreign exchange losses/gains on translation of the HKD-denominated long-term borrowings.

(b) ***Cash flow and fair value interest rate risk***

The Group's interest rate risk mainly arises from pledged bank deposits and borrowings. Long-term borrowing issued at variable rates expose the Group to cash flow risk which is partially offset by cash held at variable rates. The Group's pledged bank deposits and short-term borrowings were issued at fixed rates and exposed the Group to fair value interest rate risk. During 2013 and 2012, the Group's long-term borrowings at variable rate were denominated in USD, HKD and RMB.

The Group has not used any interest rate swaps to hedge its exposure to interest rate risk.

As at 31 December 2013, if interest rates on long-term borrowings had been increased/decreased by 20 basis points with all other variables held constant, post-tax loss for the year would have been increased/decreased by RMB2,121,000 (2012: post-tax profit for the year would have been decreased/increased by RMB1,595,000), mainly as a result of higher/lower interest expense on floating rate borrowings.

(c) ***Credit risk***

The Group has no significant concentrations of credit risk. Credit risk arises from cash and cash equivalents, pledged bank deposits and trade and other receivables.

For cash and cash equivalents and pledged bank deposits, management manages the credit risk by placing most bank deposits in the state-controlled and other listed banks in Mainland China and other high quality foreign banks without significant credit risk.

For trade and other receivables, the credit quality of the counterparties is assessed by taking into account their financial position, credit history and other factors. Individual credit limits are set based on the assessment of the credit quality. Given the constant repayment history, the directors are of the opinion that the risk of default by these counterparties is low. The Group has no significant concentrations of credit risk, with exposure spread over a large number of counterparties and customers.

(d) ***Liquidity risk***

The Group guarantees a sufficient liquidity by efficient cash management and by keeping adequate committed and uncommitted credit line available.

The table below analyses the Group and the Company's financial liabilities and net-settled derivative financial instruments into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances, as the impact of discounting is not significant.

	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Over 5 years
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Group				
At 31 December 2013				
Trade and other payables	196,762	—	—	—
Short-term borrowings	2,583,575	—	—	—
Derivative financial liabilities	—	30,968	—	—
Long-term borrowings	207,510	346,073	694,145	—
Interest payment on borrowings	116,399	69,560	110,590	—
At 31 December 2012				
Trade and other payables	108,696	—	—	—
Short-term borrowings	1,933,961	—	—	—
Derivative financial liabilities	—	—	31,752	—
Long-term borrowings	129,098	203,928	604,396	—
Interest payment on borrowings	87,883	64,623	76,324	—
Company				
At 31 December 2013				
Accruals and other payables	461	—	—	—
Derivative financial liabilities	—	30,968	—	—
Long-term borrowings	14,649	73,863	—	—
Interest payment on borrowings	7,181	3,401	—	—
At 31 December 2012				
Accruals and other payables	1,142	—	—	—
Derivative financial liabilities	—	—	31,752	—
Long-term borrowings	11,824	15,124	50,099	—
Interest payment on borrowings	15,283	14,146	5,410	—

The Group aims to maintain sufficient cash and cash equivalents and ensure the availability of funding though an adequate amount of available financing, including short-term borrowings, long-term borrowings and capital contribution from investors. Due to the dynamic nature of the underlying businesses, management of the Group maintains flexibility in funding by maintaining adequate amount of cash and cash equivalents and flexibility in funding through having available sources of financing.

The Group has been investing in the construction of new production lines and a significant amount of the financing was obtained from short-term borrowings. As a result, the Group had net current liabilities of approximately RMB787,953,000 as at 31 December 2013 (2012: RMB432,081,000). Nevertheless, the Group has not experienced any difficulties in renewing its short-term borrowings upon their maturities.

The directors, having considered the current operation and business plan of the Group as well as the available funding sources as described below, are of the opinion that the Group will have sufficient working capital to maintain its liquidity:

— As at 31 December 2013, the Group's total borrowings amounted to RMB3,831 million, of which RMB2,791 million will be due within 12 months from 31 December 2013. As at that date, the Group's bank deposits pledged for long-term borrowings and short-term borrowings amounted to RMB301 million and RMB1,414 million, respectively. The Group has not experienced any significant difficulties in renewing its short-term borrowings upon their maturities and there is no indication that the banks will not renew the existing short-term borrowings upon the Group's request. Subsequent to the balance sheet date and up to the date of approval of the financial statements, the Group has renewed short-term borrowings of approximately RMB170 million for another 12 months, and has obtained a new short-term borrowing of RMB80 million with a term of 6 months. In addition, certain banks have advised their intention in writing, though not legally binding, to renew loans to the Group for another 12 months when they fall due in 2014 or to provide new loans, totalling approximately RMB1,101 million which require no pledged bank deposits or other collateral. Therefore, the directors of the Company believe that the Group will be able to renew its existing short-term borrowings upon maturity.

— The Group is expected to generate adequate operating cash inflows in 2014 from its existing production facilities as well as the newly completed production facilities located in GuangAn, Sichuan Province ("GuangAn Project"). As at the date of approval of these financial statements, construction of GuangAn Project has already been completed and it is ready to be put into operation. Subject to the finalisation of certain commercial terms in contract with the Company's natural gas (major raw materials) supplier, the directors of the Company expect that GuangAn Project will commence commercial operation in mid-2014. The directors also expect that sufficient sales orders will be secured in the coming year such that adequate operating cash inflows will be generated by the existing production facilities and GuangAn Project.

3.2 Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Group may issue new shares, borrow or repay debts or adjust the amount of dividends paid to shareholders.

Consistent with others in the industry, the Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings (including short-term borrowings and long-term borrowings as shown in the consolidated balance sheet) less cash and cash equivalents and pledged bank deposits. Total capital is calculated as "equity" as shown in the consolidated balance sheet plus net debt.

The gearing ratio as at 31 December 2013 was as follows:

	2013	**2012**
	RMB'000	*RMB'000*
Short-term borrowings (Note 23)	2,583,575	1,933,961
Long-term borrowings (Note 18)	1,247,728	937,422
Total borrowings	3,831,303	2,871,383
Less: Cash and cash equivalents (Note 14)	(116,683)	(350,752)
Pledged bank deposits (Note 13)	(1,726,298)	(1,228,847)
Net debt	1,988,322	1,291,784
Total equity	1,072,299	1,121,672
Total capital	3,060,621	2,413,456
Gearing ratio	65%	54%

The increase in the gearing ratio from 54% in 2012 to 65% in 2013 is mainly due to the increase of borrowings which are used for the construction of GuangAn project.

3.3 Fair value estimation

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1).

- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2).

- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The following table presents the Group's financial liabilities that are measured at fair value at 31 December 2013.

	Level 1	Level 2	Level 3	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Liabilities				
Financial liabilities at fair value through profit or loss				
— Derivative financial liabilities (Note 19)	—	—	30,491	30,491

The following table presents the Group's financial liabilities that are measured at fair value at 31 December 2012.

	Level 1	Level 2	Level 3	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Liabilities				
Financial liabilities at fair value through profit or loss				
— Derivative financial liabilities (Note 19)	—	—	36,530	36,530

If one or more of the significant inputs is not based on observable market data, the instrument is included in level 3.

The following table presents the changes in level 3 instruments for the year ended 31 December 2013.

	Derivative financial liabilities
	RMB'000
Opening balance	36,530
Addition	—
Gains recognised in profit or loss	(6,039)
Closing balance	30,491
Total gains for the period included in profit or loss for liabilities held at the end of the reporting period	(6,039)

The following table presents the changes in level 3 instruments for the year ended 31 December 2012.

	Derivative financial liabilities
	RMB'000
Opening balance	5,072
Addition	40,978
Gains recognised in profit or loss	(9,520)
Closing balance	36,530
Total gains for the period included in profit or loss for liabilities held at the end of the reporting period	(9,520)

The fair value of long-term borrowings for disclosure purposes is estimated by discounting the future contractual cash flows at a current market interest rate for borrowings with similar credit risk and maturity (Note18).

The carrying values less impairment provision of cash and cash equivalents, pledged bank deposits, trade and other receivables, trade and other payables, and short-term borrowings approximates their fair values due to their short maturities.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgement are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(a) Useful lives of property, plant and equipment

The estimate of useful lives of property, plant and equipment was made by the directors with reference to the established industry practices, technical assessments made on the durability of the assets, as well as the historical magnitude and trend of repair and maintenance expenses incurred by the Group. It could change significantly as a result of technical innovations and competitor actions in responses to severe industry cycles. Management will increase the depreciation charge where useful lives are less than previously estimated lives, or it will write off or write down technically obsolete or non-strategic assets that have been abandoned or sold.

(b) **Provision for impairment of trade receivables**

The Group makes provision for impairment of trade receivables based on the assessment of the recoverability of trade receivables with reference to the extent and duration that the amount will be recovered. Provisions are applied to trade receivables where events or changes in circumstances indicate that the balances may not be collectible. The identification of impairment requires the use of judgement and estimates. Where the expectation is different from the original estimate, such difference will impact the carrying value of receivables and impairment expenses in the period in which such estimate has been changed.

(c) **Fair value of derivative financial liabilities**

The Company has granted warrants to International Finance Corporation ("IFC") in 2009. Management has used the Black-Scholes valuation model to determine the fair value of the warrants granted. The changes of fair value are recognised in profit or loss. Significant judgement, such as risk free rate, dividend yield, expected volatility and option life, is required to be made by management as the parameters for applying the Black-Scholes valuation model.

The Company has granted warrants to Asian Equity Special Opportunities Portfolio Master Fund Ltd ("Asian Equity") and PA International Opportunities VII Limited ("PA International") in 2012. Management has used the Binominal valuation model to determine the fair value of the warrants granted. The changes of fair value are recognised in profit or loss. Significant judgement, such as risk free rate, dividend yield, expected volatility, debt rate and option life, is required to be made by management as the parameters for applying the Binominal valuation model.

(d) **Impairment of goodwill**

The Group tests annually whether goodwill has suffered any impairment in accordance with the accounting policy stated in Note 2.10(a). The recoverable amounts of cash-generating units have been determined based on fair value less costs to sell calculations. These calculations require the use of estimates (Note 9).

(e) **Impairment of non-current assets other than goodwill**

In determining whether a non-current asset is impaired or the event previously causing the impairment no longer exists, management has to exercise judgement in the area of asset impairment, particularly in assessing: (1) whether an event has occurred that may affect the asset value or such event affecting the asset value has not been in existence; (2) whether the carrying value of an asset can be supported by the net present value of future cash flows which are estimated based upon the continued use of the asset or derecognising; and (3) the appropriate key assumptions to be applied in preparing cash flow projections including whether these cash flow projections are discounted using an appropriate rate. Changing the assumptions selected by management to determine the level of impairment, including the discount rates or the growth rate assumptions in the cash flow projections, could materially affect the net present value used in the impairment test.

(f) **Classification of non-current assets held for sale**

As disclosed in Note 15, the Group reclassified the non-current assets of one of its subsidiaries to current assets which are held for sale. In determining whether non-current assets can be classified as assets held for sale, management needs to exercise judgement as to whether a sale is highly probable.

(g) **Income taxes**

The Group is mainly subject to income taxes in the Mainland China. Significant judgement is required in determining the provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the tax losses can be utilised. Recognition of deferred tax assets primarily involves management judgement and estimations regarding the taxable profits of the entities in which the losses arose. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits.

Pursuant to the Corporate Income Tax Law and its implementation rules, effective from 1 January 2008, certain non-resident enterprises (for instance, those without an establishment or place of business in Mainland China or which have an establishment or place of business in Mainland China but whose relevant income is not effectively connected with the establishment or a place of business in the Mainland China) are subject to withholding tax at the rate of 5% or 10% on various types of passive income such as dividends derived from sources within the Mainland China. As at 31 December 2013, the deferred tax liabilities recognised for withholding tax on accumulated earning generated by Mainland China subsidiaries amount to RMB5,485,000 (2012: RMB5,485,000) on the earning of RMB109,700,000 (2012: RMB109,700,000) generated by other Mainland China subsidiaries.

5 LAND USE RIGHTS — GROUP

The Group's land use rights represent prepaid operating lease payments.

	2013	2012
	RMB'000	*RMB'000*
At 1 January	59,289	59,289
Cost		
Accumulated amortisation	(5,073)	(3,888)
Net book amount	54,216	55,401
Opening net book amount	54,216	55,401
Amortisation charge for the year	(1,189)	(1,185)
	53,027	54,216
At 31 December		
Cost	59,289	59,289
Accumulated amortisation	(6,262)	(5,073)
	53,027	54,216

All the Group's land use rights are located in Mainland China. The remaining lease periods of the land use rights are between 3 to 45 years (2012: 4 to 46 years).

As at 31 December 2013, certain land use rights with a total net book value of approximately RMB45,094,000 (2012: RMB45,897,000) were pledged as collateral for the Group's long-term borrowings (Note18(a)(b)).

Amortisation charge of RMB1,189,000 (2012: RMB1,185,000) had been charged in administrative expenses.

6 PROPERTY, PLANT AND EQUIPMENT — GROUP

	Buildings	Plant and machinery	Motor vehicles	office equipment and others	Construction-in-progress	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
At 1 January 2012						
Cost	311,047	847,100	10,085	9,888	459,553	1,637,673
Accumulated depreciation	(10,991)	(96,296)	(4,384)	(4,852)	—	(116,523)
Net book amount	300,056	750,804	5,701	5,036	459,553	1,521,150
Year ended 31 December 2012						
Opening net book amount	300,056	750,804	5,701	5,036	459,553	1,521,150
Additions	—	203	3,306	726	637,610	641,845
Disposals (Note 25 and 34)	—	(799)	(200)	(916)	—	(1,915)
Depreciation	(6,194)	(64,822)	(1,379)	(981)	—	(73,376)
Additions	293,862	685,386	7,428	3,865	1,097,163	2,087,704
At 31 December 2012						
Cost	311,047	846,406	12,541	9,556	1,097,163	2,276,713
Accumulated depreciation	(17,185)	(161,020)	(5,113)	(5,691)	—	(189,009)
Net book amount	293,862	685,386	7,428	3,865	1,097,163	2,087,704
Year ended 31 December 2013						
Opening net book amount	293,862	685,386	7,428	3,865	1,097,163	2,087,704
Additions	23	11	1,294	4,598	564,150	570,076
Transfers	72,122	—	—	8,745	(80,867)	—
Transfers to investment properties (Note 7)	—	—	—	—	(13,862)	(13,862)
Disposals (Note 25 and 34)	—	—	(246)	(201)	—	(447)
Depreciation	(7,208)	(65,244)	(745)	(1,653)	—	(74,850)
Closing net book amount	358,799	620,153	7,731	15,354	1,566,584	2,568,621
At 31 December 2013						
Cost	383,192	846,417	13,381	22,322	1,566,584	2,831,896
Accumulated depreciation	(24,393)	(226,264)	(5,650)	(6,968)	—	(263,275)
Net book amount	358,799	620,153	7,731	15,354	1,566,584	2,568,621

Depreciation expense of RMB64,406,000 (2012: RMB63,305,000) had been charged in cost of sales and RMB10,444,000 (2012: RMB10,071,000) in administrative and distribution costs.

All the Group's buildings are located in Mainland China. As at 31 December 2013, property, plant and equipment with a total net book value of approximately RMB1,390,511,000 (2012: RMB1,447,846,000) were pledged as collateral for the Group's long-term borrowings (Note 18(a)(b)).

Borrowing costs of RMB65,316,000 (2012: RMB36,364,000) have been capitalised in the construction-in-progress at average capitalisation rate of 8.14% (2012: 8.05%) (Note 29).

7 INVESTMENT PROPERTIES — GROUP

	2013	**2012**
Cost		
As at 1 January	—	—
Transfer from property, plant and equipment (Note 6)	13,862	—
As at 31 December	13,862	—
Accumulated depreciation and impairment losses		
As at 1 January	—	—
Charge for the year	(208)	—
As at 31 December	(208)	—
Net book value		
As at 31 December	13,654	—
As at 1 January	—	—
Fair value as at 31 December	24,370	—

The fair values of the investment properties as at 31 December 2013 were estimated by the Group, based on valuation performed by independent valuers. It falls under level 3 in the fair value hierarchy.

The rental income arising from investment properties for the year 2013 amounted to RMB1,312,000 (2012: Nil), which is included in other income — net. Depreciation charge of RMB208,000 (2012: Nil) had been charged in other income — net.

During the year, the Group entered into a lease agreement of certain portions of its building. Accordingly, the relevant carrying amounts of the building as at the date of change usage were transferred to investment properties.

As at 31 December 2013, the Group had no unprovided contractual obligations for future repairs and maintenance (2012: Nil).

As at 31 December 2013, investment properties with a carrying amount of RMB13,654,000 (31 December 2012: Nil) were pledged as collateral for long term borrowings (Note 18(a)) with a carrying amount of RMB15,711,000 (31 December 2012: Nil).

8 MINING RIGHT — GROUP

The mining right represents the right to conduct mining activities in a phosphate mine located in Sichuan, Mainland China, which has a remaining legal life of 26 years, expiring in February 2039.

	Total
	RMB'000
At 1 January 2012, 31 December 2012 and 2013	
Cost	334,306
Accumulated amortisation and impairment	—
Net book amount	334,306

The Group has not commenced any mining activities, therefore no amortisation was charged in this year. The impairment test information of mining right is set out in Note 9.

9 OTHER INTANGIBLE ASSETS — GROUP

	Goodwill	Construction permits	Total
	RMB'000	*RMB'000*	*RMB'000*
At 1 January 2012			
Cost	8,900	2,700	11,600
Accumulated amortisation	—	(432)	(432)
Closing net book amount	8,900	2,268	11,168
At 1 January 2013	8,900	2,268	11,168
Amortisation charge	—	(270)	(270)
Closing net book amount	8,900	1,998	10,898
At 31 December 2013			
Cost	8,900	2,700	11,600
Accumulated amortisation	—	(702)	(702)
Net book amount	8,900	1,998	10,898

Construction permits represent the permissions granted by the government for the construction of GuangAn Project. Amortisation charge of RMB270,000 (2012: RMB270,000) is included in administrative expenses.

Impairment tests for goodwill and mining right

The goodwill and mining right (Note 8) are allocated to the Group's cash-generating unit ("CGU") in relation to the mining activities of the phosphate mine located in Sichuan, Mainland China and its production of phosphoric acid. The recoverable amount of the CGU is determined based on fair value less cost to sell calculations. The fair value less cost to sell is derived by using discounted cash flow approach which incorporates assumptions that market participants would use in estimating the CGU's fair value. It falls under level 3 in the fair value hierarchy.

The key assumptions used for the calculations of fair value less costs to sell are as follows:

	2013	2012
Gross margin	30%	32%
Growth rate	3%	3%
Discount rate (post-tax discount rate applied to the cash flow projections)	17%	17%
Years of cash flows projection (expected mining period of the phosphate mine)	30 years	30 years

Management determined gross margin based on past market prices of the phosphoric acid which are produced from phosphate ore and management's estimation of exploitation and production costs. The discount rate used is post-tax and reflects specific risks relating to the relevant CGU. Expected mining period of the phosphate mine is determined based on extractable reserve of the phosphate mine and the Group's production capacity. Management of the Group determines that there is no impairment of the CGU containing goodwill and mining right.

10 INTERESTS IN SUBSIDIARIES AND LOANS TO SUBSIDIARIES — COMPANY

(a) Interests in subsidiaries

	2013	2012
	RMB'000	*RMB'000*
Unlisted investments, at cost	332,113	332,113
Investment arising from share-based compensation (Note i)	11,378	5,510
Amounts due from subsidiaries (Note ii)	407,279	407,279
	750,770	744,902

(i) The amount represents share-based compensation expenses arising from the granting of share options of the Company to employees of subsidiaries in exchange for their services offered to the subsidiaries.

(ii) The amounts due from subsidiaries which are unsecured, non-interest bearing, denominated in HKD and have no requirement on the repayment in the foreseeable future, is accounted for as quasi-investment.

(b) **Loans to subsidiaries**

	2013	**2012**
	RMB'000	*RMB'000*
Loans to subsidiaries	116,564	110,992

The loans to subsidiaries are unsecured, denominated in HKD, due by 8 July 2015 and bear interest at 9% (2012: 9%) per annum. The fair value of loans to subsidiaries amounted to RMB119,073,000 (2012: RMB113,485,000), which is based on discounted cash flows using a rate based on the borrowing rate of 8.57% (2012: 8.68%). The discount rate equals to LIBOR plus appropriate credit spread. It falls under level 3 in the fair value hierarchy.

The following is a list of the subsidiaries as at 31 December 2013:

Name (Note e)	**Place of incorporation/ establishment and kind of legal entity**	**Principal activities and place of operation**	**Particulars of issued, registered and fully paid up capital**	**Interest held**
Ko Yo Ecological Agrotech (BVI) Limited ("Ko Yo BVI") (Note a)	British Virgin Islands ("BVI"), limited liability company	Investment holding in BVI	100 ordinary shares of USD1 each	100%
Bright Bridge Investments Limited (Note a)	BVI, limited liability company	Investment holding in BVI	1 ordinary share of USD1 each	100%
Ko Yo Development Company Limited ("Ko Yo Hong Kong")	Hong Kong, limited liability company	Investment holding in Hong Kong	3,000,000 non-voting deferred shares and 100 ordinary shares of HKD1 each	100%
Chengdu Ko Yo Chemical Industry Co., Ltd. ("Chengdu Ko Yo Chemical")	Mainland China, wholly foreign owned enterprise	Manufacture and sale of chemical products including sodium carbonate, ammonia, and chemical fertilisers including urea and ammonium chloride in Mainland China	RMB27,000,000	100%

Name (Note e)	Place of incorporation/ establishment and kind of legal entity	Principal activities and place of operation	Particulars of issued, registered and fully paid up capital	Interest held
Chengdu Ko Yo Compound Fertilisers Co., Ltd. ("Chengdu Ko Yo Compound")	Mainland China, wholly foreign owned enterprise	Manufacture, research, development and sale of bulk blended fertilisers in Mainland China	RMB15,000,000	100%
Dazhou Ko Yo Chemical Industry Co., Ltd ("Dazhou Ko Yo Chemical") (Note b)	Mainland China, wholly foreign owned enterprise	Manufacture and sale of chemical products including ammonia, ammonia carbonate and urea in Mainland China	RMB350,000,000	100%
Qingdao Ko Yo Chemical Industry Co., Ltd. ("Qingdao Ko Yo Chemical")	Mainland China, wholly foreign owned enterprise	Manufacture, research, development and sale of bulk blended fertilisers in Mainland China	USD2,100,000	100%
Hong Kong Cuyo Investment Limited ("Hong Kong Cuyo")	Hong Kong, limited liability company	Investment holding in Hong Kong	4,720,000 ordinary shares of HKD1 each	100%
Sichuan Chengyuan Chemical Industry Co., Ltd ("Sichuan Cuyo")	Mainland China, wholly foreign-owned enterprise	Exploration and exploitation of a phosphorous mine in Mainland China	RMB5,000,000	100%
Sichuan Ko Yo Agrochem Co., Ltd ("Ko Yo Agrochem")	Mainland China, wholly foreign owned enterprise	Sale of chemical products including sodium carbonate, ammonia, and chemical fertilisers including urea and ammonium chloride in Mainland China	RMB24,000,000	100%

Name (Note e)	Place of incorporation/ establishment and kind of legal entity	Principal activities and place of operation	Particulars of issued, registered and fully paid up capital	Interest held
Guangan Ko Yo Chemical Industry Co., Ltd ("Ko Yo GuangAn")	Mainland China, wholly foreign-owned enterprise	Manufacture and sale of chemical products including sodium carbonate and ammonia in Mainland China	RMB160,000,000	100%
Chengdu Dayuan Chemical Industry Co., Ltd ("Ko Yo Dayuan")	Mainland China, wholly foreign-owned enterprise	Investment holding in Mainland China	RMB100,000	100%
Chengdu Meiyuan Chemical Industry Co., Ltd ("Ko Yo Meiyuan")	Mainland China, wholly foreign-owned enterprise	Investment holding in Mainland China	RMB100,000	100%
Guangan Lotusan Natural Gas Chemicals Co., Ltd ("Ko Yo Lotusan")	Mainland China, wholly domestic-owned enterprise	Manufacture and sale of chemical products including methanol and ammonia in Mainland China	RMB43,000,000	100%
Sichuan Ko Chang Technology Co., Ltd ("Ko Yo Ko Chang") (Note 17(d))	Mainland China, domestic-owned enterprise	Development of phosphoric acid production technology	RMB10,000,000	64%
Ko Yo Hong Kong New Material Company Limited ("Hong Kong New Material") (Note c)	Hong Kong, limited liability company	Investment holding in Hong Kong	—	100%

Name (Note e)	Place of incorporation/ establishment and kind of legal entity	Principal activities and place of operation	Particulars of issued, registered and fully paid up capital	Interest held
Guangan Ko Yo New Material Co., Ltd ("Guangan New Material") (Note c)	Mainland China, wholly foreign owned enterprise	Manufacture and sale of engineering plastic including Polyphenylene sulphide (PPS) in Mainland China	—	100%

Notes:

(a) Shares held directly by the Company.

(b) 100% equity interest of Ko Yo Hong Kong, Dazhou Ko Yo Chemical, Guangan Ko Yo Chemical and Sichuan Ko Yo Agrochem were pledged as collateral for the Group's borrowings (Note 18(a)). There is no restriction on the subsidiary's ability to transfer funds to its parent in the form of cash dividends or to repay loans or advances.

(c) In 2013, Hong Kong New Material and Guangan New Material were newly established by the Group with registered capital of HKD10,000 and RMB48,600,000, respectively, which have not been paid.

(d) The total non-controlling interest for the year is RMB3,267,000, which is attributed to Ko Yo Ko Chang. The non-controlling interest in respect of Changsha Research Institute of Mining and Metallurgy Co, Ltd is not material.

(e) The English name of certain companies referred in this financial statements represent management's best effort at translating the Chinese names of these companies as no English names have been registered.

11 INVENTORIES — GROUP

	2013	2012
	RMB'000	*RMB'000*
Raw materials	38,353	39,872
Work in progress	—	2,839
Finished goods	4,906	15,920
	43,259	58,631

The cost of inventories recognised as expense and included in "cost of sales" amounted to RMB516,599,000 (2012: RMB317,127,000).

There is no provision for impairment of inventories of the Group as at 31 December 2013 (31 December 2012: Nil).

12 TRADE AND OTHER RECEIVABLES

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Trade receivables	10,448	11,194	—	—
Less: provision for impairment of trade receivables	(5,241)	(5,241)	—	—
Trade receivables — net	5,207	5,953	—	—
Prepayments for raw materials	217,219	67,978	—	—
Prepaid input value-added tax	90,003	8,377	—	—
Notes receivable	3,285	1,800	—	—
Due from employees	5,447	11,413	—	—
Others	39,744	17,387	476	476
	360,905	112,908	476	476

As at 31 December 2013 and 2012, the fair value of trade and other receivables of the Group approximated to their carrying amounts.

The credit terms of trade receivables granted by the Group are normally within 3 months. The ageing analysis of trade receivables is as follows:

	Group	
	2013	**2012**
	RMB'000	*RMB'000*
Less than 3 months	5,207	4,072
More than 3 months but not exceeding 1 year	—	55
More than 1 year but not exceeding 2 years	—	1,826
More than 2 years but not exceeding 3 years	—	133
More than 3 years	5,241	5,108
	10,448	11,194
Less: provision for impairment of trade receivables	(5,241)	(5,241)
	5,207	5,953

As of 31 December 2013, trade receivables of RMB5,207,000 (2012: RMB4,072,000) that are under credit term were fully performing.

As at 31 December 2013, trade receivables of RMB5,241,000 (2012: RMB5,241,000) were impaired and a full provision of RMB5,241,000 (2012: RMB5,241,000) was provided for. The individually impaired receivables mainly relate to wholesalers, which are in unexpected difficult economic situations. The ageing of these receivables is as follows:

	Group	
	2013	**2012**
	RMB'000	*RMB'000*
More than 2 years but not exceeding 3 years	—	133
More than 3 years	5,241	5,108
	5,241	5,241

The carrying amounts of the Group's and the Company's trade and other receivables are denominated in the following currencies:

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
RMB	350,613	108,598	—	—
HKD	10,292	4,310	476	476
	360,905	112,908	476	476

Movements on the provision for impairment of trade receivables are as follows:

	Group	
	2013	**2012**
	RMB'000	*RMB'000*
At 1 January	5,241	5,241
Provision for receivables	—	—
At 31 December	5,241	5,241

Notes receivable represents trade related bank acceptance notes with maturity period within 6 months and non-interest bearing.

The maximum exposure to credit risk at the reporting date is the carrying amount of each class of receivable mentioned above. The Group does not hold any collateral as security.

13 PLEDGED BANK DEPOSITS — GROUP

The carrying amounts of the Group's pledged bank deposits are denominated in RMB.

The deposits are pledged for long-term borrowings (Note 18) and short-term borrowings (Note 23) and notes payable (Note 22) of the Group. The effective interest rates on pledged bank deposits are ranging from 2.60% to 4.75% (2012: 2.87% to 3.30%).

14 CASH AND CASH EQUIVALENTS

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Cash at bank	116,650	350,461	85	168
Cash in hand	33	291	—	—
	116,683	350,752	85	168
Maximum exposure to credit risk	116,650	350,461	85	168

The weighting average effective interest rate on cash at bank at 31 December 2013 is 0.35% (2012: 0.38%).

The carrying amounts of the Group's and the Company's cash and cash equivalents are denominated in the following currencies:

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
RMB	109,264	335,910	—	—
USD	1	280	1	2
HKD	7,385	14,271	84	166
	116,650	350,461	85	168

15 NON-CURRENT ASSETS HELD FOR SALE

Due to municipal planning arrangement, at the request of the People's Government of Chengdu, the original manufacturing business of Ko Yo Chemical (a directly wholly-owned subsidiary of Ko Yo Hong Kong) which is located at Chengdu, Sichuan Province is required to be discontinued. The Group therefore has applied for the change of the usage of Ko Yo Chemical's land use rights from industrial usage to commercial usage and is arranging the disposal of the non-current assets of Ko Yo Chemical to other parties. In accordance with the overall development strategy as planned by the Group, the proceeds from the sale of the non-current assets of Ko Yo Chemical will be invested in the GuangAn Project.

On 16 June 2011, Ko Yo Hong Kong and Chengdu Hexin Real Estate Co, Ltd (the "Purchaser") entered into the Equity Transfer Agreement and the Supplemental Agreement pursuant to which Ko Yo Hong Kong has agreed to sell, and the Purchaser has agreed to purchase the 40% equity interest in Ko Yo Chemical, at a cash consideration of RMB20 million, and the settlement of certain debts of Ko Yo Chemical amounting to RMB49.44 million. The aggregate consideration of approximately RMB69.44 million was received and the registration of transfer of 40% equity interest in Ko Yo Chemical has been completed during 2011. Ko Yo Chemical ceased its business operation before the end of December 2011.

As the Purchaser intends to further acquire the remaining 60% equity interest in Ko Yo Chemical at a consideration of approximately RMB150 million, a deposit of RMB30.66 million has also been received from the Purchaser during 2011.

Moreover, pursuant to the Supplemental Agreement the Group is required to settle remaining liabilities of Ko Yo Chemical and is entitled to dispose of certain machinery being dismantled from Ko Yo Chemical. The Group received the consideration of RMB31 million for such disposal from another independent third party during 2011.

As of 31 December 2011, the completion of the sale of 100% equity interest in Ko Yo Chemical and the disposal of machinery is subject to the fulfilment of certain terms and conditions, and thus all the amounts received in relation to the disposal of Ko Yo Chemical and the assets totalling RMB131.1 million are classified as advances from purchasers (Note 22). As a result, the Group reclassified the non-current assets of Ko Yo Chemical to current assets which are held for sale.

Due to the delay of government's approval on the change of usage of Ko Yo Chemical's land use rights from industrial usage to commercial usage ("Government approval"), the completion of the sale of 100% equity interest in Ko Yo Chemical has not been completed up to the date of approval of these consolidated financial statements. On the basis that the Group is still committed to sell and the Purchaser is still committed to purchase 100% equity interest in Ko Yo Chemical, the Group has been making positive progress in obtaining the Government Approval and there is no legal obstacle which prevents the Group from obtaining Government Approval, the directors consider the above assets should remain being classified as non-current assets held for sale as of 31 December 2012 and 2013.

The details of the non-current assets held for sale are as follows:

	As at 31 December 2012 and 2013
	RMB'000
Non-current assets held for sale	
Property, plant and equipment	151,871
Land use rights	31,030
Deferred tax assets	15,883
	198,784

16 SHARE CAPITAL

Movements of the share capital of the Company are as follows:

	Number of shares of HKD0.02 each		Share capital	
	2013	**2012**	**2013**	**2012**
	'000	*'000*	*HKD'000*	*HKD'000*
Authorised:				
Ordinary shares at beginning and end of year	10,000,000	10,000,000	200,000	200,000

	Notes	Number of shares of HKD0.02 each		share capital	
		2013	**2012**	**2013**	**2012**
		'000	*'000*	*RMB'000*	*RMB'000*
Issued and fully paid:					
Ordinary shares at beginning of year and at end of year		7,195,285	7,195,285	138,618	138,618

(a) **Share options**

All of share options have duration of 10 years from the date of grant and the options can be exercised from the date of grant.

(1) ***GEM share option scheme***

On 10 June 2003, the Company adopted a share option scheme (the "GEM Share Option Scheme"). The purpose of the GEM Share Option Scheme is to recognise the contribution of the eligible participants, and to provide a performance related incentive to them. The eligible participants include the employees (including executive and non-executive directors) and consultants of the Group.

The number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the GEM Share Option Scheme and any other schemes must not exceed 30% of the shares in issue from time to time. The total number of shares which may be issued upon exercise of all options to be granted under the GEM Share Option Scheme and any other schemes must not exceed 210,000,000 shares (on post-subdivision basis), 10% of the shares of the Company at the date of commencement of dealings of the Company's shares on GEM.

Each participant is entitled to a maximum of 21,000,000 share options (on post-subdivision basis), which are valid for a period of 10 years from the date of grant. The subscription price will be determined by the Company's Board of Directors, and will not be less than the highest of (a) the closing price of the shares quoted on the GEM of the Stock Exchange on the date of the offer; (b) the average closing price of the shares quoted on the GEM of the Stock Exchange for the five business days immediately preceding the date of the offer and (c) the nominal value of the shares.

The details of share options outstanding, after adjustment for the effect of share subdivision, are as follows:

Date of grant	**23 September 2003**	**11 April 2006**	**16 May 2006**	**10 September 2007**
Exercise price (HKD per option, on post-subdivision basis)	0.12	0.15	0.15	0.12
Granted to	2 executive directors, 2 independent directors and 6 employees	18 employees	2 executive directors and 1 independent director	7 employees

Exercisable period	10 years from the date of grant	10 years from the date of grant	10 years from the date of grant *(Note i)*	10 years from the date of grant	Total
At 1 January 2012	122,000,000	42,000,000	6,200,000	25,000,000	195,200,000
Forfeited	—	(8,000,000)	—	—	(8,000,000)
At 31 December 2012	122,000,000	34,000,000	6,200,000	25,000,000	187,200,000
At 1 January 2013	122,000,000	34,000,000	6,200,000	25,000,000	187,200,000
Expired	(122,000,000)	—	—	—	(122,000,000)
Forfeited	—	(1,500,000)	—	(2,000,000)	(3,500,000)
At 31 December 2013	—	32,500,000	6,200,000	23,000,000	61,700,000

(i) Share options that were granted on 16 May 2006 and remained outstanding at end of year were held by the following executive and non-executive directors:

Exercisable period	Directors	Number of options 31 December 2013
16 May 2006 to 10 April 2016	Mr. Li Weiruo	2,100,000
16 May 2006 to 10 April 2016	Mr. Yuan Bai	2,000,000
16 May 2006 to 10 April 2016	Mr. Qian Laizhong	2,100,000
		6,200,000

The GEM Share Option Scheme was terminated upon the Transfer of Listing and no further options will be offered or granted under the GEM Share Option Scheme. All the outstanding share options will remain valid and exercisable in accordance with their terms of issue after the Transfer of Listing.

(2) ***New Share Option Scheme***

On 18 September 2008, the Company adopted a new share option scheme (the "New Scheme") pursuant to the resolutions passed by an extraordinary general meeting.

The purpose of the New Scheme is to encourage the participants to perform their best in achieving the goals of the Group and at the same time allow the participants to enjoy the results of the Group attained through their efforts and contributions and to provide the participants with incentives and help the Group in retaining its existing employees and recruiting additional employees.

The New Scheme shall be valid and effective for the period of 10 years commencing from the adoption date, after which period no further options will be granted but the provision of the Scheme shall remain in full force and effect in all other respects.

The maximum number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the New Scheme and any other schemes shall not exceed 30% of the total shares in issue from time to time. The total number of shares which may be issued upon exercise of all options to be granted under the New Scheme and any other schemes must not exceed 10% of the shares of the Company as at the adoption date unless the Company obtains a refresh approval from its shareholders.

The subscription price will be determined by the Company's Board of Directors, and will not be less than the highest of (a) the closing price of the shares as stated in the Stock Exchange's daily quotations sheets on the date of grant, which must be a trade day; (b) the average closing price of the shares as stated in the Stock Exchange's daily quotations sheets for the five trading days immediately preceding the date of the grant and (c) the nominal value of a share.

The details of share options outstanding are as follows:

Date of grant	**14 January 2010**	**23 November 2010**	**28 March 2013**	**15 November 2013**
Exercise price (HKD per option, on post-subdivision basis)	0.23	0.22	0.119	0.096
Granted to	5 executive directors and 8 employees	3 independent directors	4 executive directors and 2 independent directors and 21 employees	1 independent director

Exercisable period	10 years from the date of grant *(Note i)*	10 years from the date of grant *(Note ii)*	10 years from the date of grant *(Note iii)*	10 years from the date of grant *(Note iv)*	Total
At 1 January 2012	56,900,000	12,000,000	—	—	68,900,000
Forfeited	—	—	—	—	—
At 31 December 2012	56,900,000	12,000,000	—	—	68,900,000
At 1 January 2013	56,900,000	12,000,000	—	—	68,900,000
Granted	—	—	163,500,000	6,000,000	169,500,000
Forfeited	(11,000,000)	—	—	—	(11,000,000)
At 31 December 2013	45,900,000	12,000,000	163,500,000	6,000,000	227,400,000

(i) On 14 January 2010, the Company granted share options to eligible persons including directors and employees to subscribe for an aggregate of 56,900,000 shares of the Company with an exercise price of HKD0.23. Among the 56,900,000 Share Options, 45,900,000 Share Options that were granted on 14 January 2010 and remained outstanding at 31 December 2013 were held by the following employees (including executive directors):

exercisable period	Directors	Number of options 31 December 2013
14 January 2010 to 13 January 2020	Mr. Li Wei Ruo	4,400,000
14 January 2010 to 13 January 2020	Mr. Yuan Bai	4,000,000
14 January 2010 to 13 January 2020	Ms. Chi Chuan	2,000,000
14 January 2010 to 13 January 2020	Ms. Man Au Vivian	4,000,000
14 January 2010 to 13 January 2020	Mr. Li Shengdi	4,000,000
		18,400,000
14 January 2010 to 13 January 2020	Other employees	27,500,000
		45,900,000

(ii) On 23 November 2010, the Company granted share options to three non-executive directors to subscribe for an aggregate of 12,000,000 shares of the Company with an exercise price of HKD0.22. These share options that were granted on 23 November 2010 and remained outstanding at the end of the year were held by the following non-executive directors:

Exercisable period	Directors	Number of Options 31 December 2013
23 November 2010 to 22 November 2020	Mr. Hu Xiaoping	4,000,000
23 November 2010 to 22 November 2020	Mr. Woo Che-wor, Alex	4,000,000
23 November 2010 to 22 November 2020	Mr. Qian Laizhong	4,000,000
		12,000,000

(iii) On 28 March 2013, the Company granted share options to eligible persons including directors and employees to subscribe for an aggregate of 163,500,000 shares of the Company with an exercise price of HKD0.119. Share options that were granted on 28 March 2013 and remained outstanding at end of year were held by the following employees (including executive and non-executive directors):

Exercisable period	Directors	Number of options 31 December 2013
28 March 2013 to 27 March 2023	Mr. Yuan Baiaia	11,000,000
28 March 2013 to 27 March 2023	Ms. Chi Chuan	21,000,000
28 March 2013 to 27 March 2023	Ms. Man Au, Vivian	19,000,000
28 March 2013 to 27 March 2023	Mr. Li Shengdi	21,000,000
28 March 2013 to 27 March 2023	Mr. Hu Xiaoping	2,000,000
28 March 2013 to 27 March 2023	Mr. Woo Che-wor, Alex	2,000,000
		76,000,000
28 March 2013 to 27 March 2023	Other employees	87,500,000
		163,500,000

The fair value of options granted during the year, determined using the Black-Scholes valuation model, was HKD9,611,000 (approximately RMB7,768,000). The significant inputs into the model were weighted average share price of HKD0.115 at the grant date, the exercise price shown above, volatility of 41.81%, dividend yield of 0.00%, an expected option life of ten years and an annual risk-free interest rate of 1.12%. The volatility measured at the standard deviation of continuously compounded share returns is based on statistical analysis of daily share prices over the last ten years of comparable companies.

(iv) On 15 November 2013, the Company granted share options to a newly appointed independent non-executive director to subscribe for an aggregate of 6,000,000 shares of the Company with an exercise price of HKD0.096. Share options that were granted on 15 November 2013 and remained outstanding at end of year were held by the following person:

Exercisable period	Director	Number of options 31 December 2013
15 November 2013 to 14 November 2023	Mr. Sun Tongchuan	6,000,000

The fair value of options granted during the year, determined using the Black-Scholes valuation model, was HKD313,000 (approximately RMB248,000). The significant inputs into the model were weighted average share price of HKD0.096 at the grant date, the exercise price shown above, volatility of 41.81%, dividend yield of 0.00%, an expected option life of ten years and an annual risk-free interest rate of 2.04%. The volatility measured at the standard deviation of continuously compounded share returns is based on statistical analysis of daily share prices over the last ten years of comparable companies.

The total number of share options granted in 2013 was 169,500,000, the total fair value at grant date was HKD9,924,000 (approximately RMB8,016,000), which was vested at the grant date and recognised as administrative expense and a corresponding increase in share-based compensation reserve (Note 17 and 26).

17 RESERVES

Movements of the Group's reserves are as follows:

	Share premium	Merger reserve	Share-based compensation reserve	Reserve fund	Enterprise expansion fund	Retained earnings	Transaction with Non-controlling interests ("NCI")	Total
	RMB'000	*RMB'000* *(Note a)*	*RMB'000*	*RMB'000* *(Note b)*	*RMB'000* *(Note b)*	*RMB'000*	*RMB'000* *(Note d)*	*RMB'000*
At 1 January 2012	550,133	(22,041)	14,186	33,304	1,131	304,729	—	881,442
Comprehensive income:								
Profit attributable to the equity holders of the Group	—	—	—	—	—	101,612	—	101,612
Transactions with equity holders:								
Appropriation (Note b)	—	—	—	11,648	—	(11,648)	—	—
Transfer of Equity interest to NCI (Note d)	—	—	—	—	—	—	(3,600)	(3,600)
	—	—	—	11,648	—	(11,648)	(3,600)	(3,600)
At 31 December 2012	550,133	(22,041)	14,186	44,952	1,131	394,693	(3,600)	979,454

	Share premium	Merger reserve	Share-based compensation reserve	Reserve fund	Enterprise expansion fund	Retained earnings	Transaction with NCI	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
	(note a)			*(note b)*	*(note b)*		*(note d)*	
At 1 January 2013	550,133	(22,041)	14,186	44,952	1,131	394,693	(3,600)	979,454
Comprehensive income:								
Loss attributable to the equity holders of the Group	—	—	—	—	—	(57,056)	—	(57,056)
Transactions with equity holders:								
Appropriation (Note b)	—	—	—	321	—	(321)	—	—
Employee share option scheme (Note 16(b))								
— Value of employee services	—	—	8,016	—	—	—	—	8,016
	—	—	8,016	321	—	(321)	—	8,016
At 31 December 2013	550,133	(22,041)	22,202	45,273	1,131	337,316	(3,600)	930,414

Movements of the Company's reserves are as follows:

	Share premium *RMB'000*	Contributed surplus *RMB'000* *(Note c)*	Share-based compensation reserve *RMB'000*	Retained earnings/ (accumulated losses) *RMB'000*	Total *RMB'000*
At 1 January 2012	550,133	37,162	14,186	(4,421)	597,060
Comprehensive income:					
Profit attributable to the equity holders of the Company (Note 31)	—	—	—	6,141	6,141
At 31 December 2012	550,133	37,162	14,186	1,720	603,201
At 1 January 2013	550,133	37,162	14,186	1,720	603,201
Comprehensive income:					
Loss attributable to the equity holders of the Company (Note 31)	—	—	—	(1,404)	(1,404)
Transactions with equity holders:					
Employee share option scheme (Note 16(b)) — Value of employee services	—	—	8,016	—	8,016
At 31 December 2013	550,133	37,162	22,202	316	609,813

(a) **Merger reserve**

Merger reserve of the Group represents the difference between the nominal value of the share capital issued by the Company and share capital and share premium of a subsidiary acquired through an exchange of shares.

(b) **Statutory reserves**

The appropriation represents the profit appropriation to reserve fund and enterprise expansion fund made by the subsidiaries of the Company established in Mainland China. These subsidiaries are governed by the laws and regulations of Mainland China and their articles of association. They are required to provide for certain statutory funds, namely, reserve fund and enterprise expansion fund which are appropriated from net profit after taxation but before dividend distribution based on the local statutory financial statements prepared in accordance with accounting principles and relevant financial regulations applicable to enterprises established in Mainland China. They are required to allocate at least 10% of their net profit to the reserve fund until the balance of such fund has reached 50% of its registered capital. Appropriation of enterprise expansion fund is determined at the discretion of its directors. The reserve fund can only be used, upon approval by the relevant authorities, to offset accumulated losses or increase capital. The enterprise expansion fund can only be used to increase capital upon approval by the relevant authorities.

(c) **Contributed surplus**

Contributed surplus of RMB37,162,000 was resulted from the reorganization prior to the listing, and represents the difference between the nominal value of the shares issued and the underlying assets of the acquired subsidiary.

(d) **Transfer of equity interest to NCI**

Ko Yo Ko Chang was newly established by the Group with fully paid share capital of RMB10,000,000 in May 2012. On 19 October 2012, Ko Yo Hong Kong transferred 36% equity interest in Ko Yo Ko Chang at a cash consideration of RMB1 to Changsha Research Institute of Mining and Metallurgy Co, Ltd, a well-known science and technology institution in China, in order to leverage the know-how owned by the institute in exploiting technology of phosphate mine. The resulting loss of RMB3,600,000 is recorded in equity, as a transaction with NCI in 2012.

18 LONG-TERM BORROWINGS, SECURED

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Bank borrowings (a)	1,107,067	789,333	—	—
Borrowing from IFC (b)	52,149	71,042	—	—
Borrowings from Asian Equity and PA International (c)	88,512	77,047	88,512	77,047
	1,247,728	937,422	88,512	77,047

(a) **Bank borrowings**

The long-term bank borrowings are secured by bank deposits of RMB301,191,000 (2012: RMB16,082,000), certain land use rights with a total net book value of approximately RMB32,895,000 (2012: RMB33,274,000), property, plant and equipment with a total net book value RMB1,242,351,000 (2012: RMB1,334,813,000), investment property with a total net book value of approximately RMB13,654,000 (2012:Nil),100% equity interest in Ko Yo Hong Kong and Dazhou Ko Yo Chemical (Note 10), which were effectively owned by the Company, and guaranteed by Mr. Li Weiruo, a shareholder and director of the Company.

The average effective interest rate of bank borrowings as at 31 December 2013 is 7.83% (2012: 8.1%).

(b) **Borrowing from IFC**

On 16 April 2009, the Group entered into a long-term borrowing agreement and a warrant subscription agreement with IFC, pursuant to which, IFC granted a long-term borrowing of USD20 million (equivalent to RMB132,454,000) to the Group at the coupon interest rate of LIBOR plus 4.5% per annum and the Company issued warrants at nil consideration to IFC to subscribe 500,000,000 ordinary shares of HKD0.02 each from the Company at an exercise price of HKD0.156 per share (Note 19 (a)). The Group has drawn down the long-term borrowings of USD17 million (equivalent to RMB116,147,000) in 2009 and USD3 million (equivalent to RMB19,869,000) in 2011.

The borrowing from IFC was recognised initially at fair value, which is equal to the difference between the face value of the borrowing and the fair value of warrants. The fair value of the borrowing from IFC at initial recognition and amortised cost at subsequent measurement are set out below:

	Group	
	2013	**2012**
	RMB'000	*RMB'000*
Fair value at initial recognition	94,619	94,619
Interest expense accrued	51,896	42,960
Interest paid	(26,538)	(22,079)
Principal paid	(65,815)	(44,458)
Exchange gain	(2,013)	—
Borrowing from IFC at 31 December	52,149	71,042

The effective interest rate of the borrowing from IFC as at 31 December 2013 is 13.19% (2012: 13.52%). The calculation of the effective interest rate has taken into account the deduction of fair value of warrants from the face value of the borrowing.

The borrowing of IFC is secured by certain land use rights with a total net book value of approximately RMB12,199,000 (2012: RMB12,623,000), and property, plant and equipment with a total net book value of RMB148,160,000 (2012: RMB113,033,000).

(c) **Borrowing from Asian equity and PA International**

In order to finance the construction of GuangAn Project, the Company entered into a bonds subscription agreement and a warrant subscription agreement with Asian Equity and PA International on 29 June 2012, pursuant to which, Asian Equity and PA International subscribed for a bond of HKD140 million (equivalent to RMB113 million) issued by the Company at the nominal interest rate of 9% per annum and the Company issued warrants at nil consideration to Asian Equity and PA International to subscribe 875,000,000 ordinary shares of HKD 0.02 each from the Company at an exercise price of HKD0.16 per share (Note 19). The bonds are due by 7 July 2015, subject to an early redemption put options held by Asian Equity and PA International (Note19 (b)), which were guaranteed by Mr. Li Weiruo, a shareholder and director of the Company.

The host bond was recognised initially at fair value, which is equal to the difference between the face value of the bonds and the fair value of warrants and put options embedded in bonds (Note 19). The fair value of bonds at initial recognition and amortised cost at subsequent measurement are set out below:

	Group and Company	
	2013	**2012**
	RMB'000	*RMB'000*
Fair value at initial recognition	72,423	72,423
Interest expense accrued	33,460	9,494
Interest paid	(14,836)	(4,870)
Exchange gain	(2,535)	—
Borrowing from Asian Equity and PA International at 31 December	88,512	77,047

The effective interest rate of the above borrowing from Asian Equity and PA International as at 31 December 2013 is 26.21% (2012: 25.28%).

As at 31 December 2013, the Group's long-term borrowings were repayable as follows:

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Within 1 year	207,510	129,098	14,649	11,824
Between 1 and 2 years	346,073	203,928	73,863	15,124
Between 2 and 3 years	429,476	268,903	—	50,099
Between 3 and 5 years	264,669	335,493	—	—
	1,247,728	937,422	88,512	77,047
Within 1 year included in current liabilities	(207,510)	(129,098)	(14,649)	(11,824)
	1,040,218	808,324	73,863	65,223

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Wholly repayable within 5 years	1,247,728	937,422	88,512	77,047
Wholly repayable after 5 years	—	—	—	—
	1,247,728	937,422	88,512	77,047

An analysis of the carrying amounts of the long-term borrowings by nature and currency is as follows:

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
At floating rates in USD	52,149	71,042	—	—
At floating rates in RMB	1,107,067	789,333	—	—
At fixed rates in HKD	88,512	77,047	88,512	77,047
	1,247,728	937,422	88,512	77,047

The fair value of the borrowings from Asian Equity and PA International at 31 December 2013, which bear fixed interest rate, amounted to HKD117,338,000 (RMB92,697,000). The fair value is calculated using cash flows discounted at a rate of 29.46%. It falls under level 3 in the fair value hierarchy.

Other than the above borrowings from Asian Equity and PA International, the carrying amounts of the long-term borrowings approximate to their fair values as the market borrowing interest rate approximates to their effective interest rates. The weighted average effective interest rate of the long-term borrowings as at 31 December 2013 is 8.10% (2012: 8.14%).

19 DERIVATIVE FINANCIAL LIABILITIES

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
IFC warrants	49	3,217	49	3,217
Warrants and put-option of bonds issued to Asian Equity and PA International	30,442	33,313	30,442	33,313
Total	30,491	36,530	30,491	36,530
Less non-current portion:				
Warrants and put-option of bonds issued to Asian Equity and PA International	—	36,530	—	36,530
Current portion	30,491	—	30,491	—

Derivative financial liabilities comprise warrants issued to IFC (Note a) and warrants and put-option of bonds issued to Asian Equity and PA International (Note b), the movement of which is set out below:

	Group	**Company**
	RMB'000	*RMB'000*
Opening balance at 1 January 2012	5,072	5,072
Addition (Note (b))	40,978	40,978
Fair value change credited to profit or loss (Note 28)	(9,520)	(9,520)
At 31 December 2012	36,530	36,530
Opening balance at 1 January 2013	36,530	36,530
Fair value change credited to profit or loss (Note 28)	(6,039)	(6,039)
At 31 December 2013	30,491	30,491

(a) **Warrants issued to IFC**

On 16 April 2009, the Company issued warrants to IFC at nil consideration (the "IFC Warrants"), which provided IFC the right to subscribe 500,000,000 ordinary shares of HKD0.02 each from the Company at an exercise price of HKD0.156 per share. The subscription rights attaching to the IFC Warrants may be exercised by IFC with expiry date on 28 April 2014.

IFC exercised a portion of the IFC Warrants to subscribe for 149,885,000 new shares of the Company on 31 March 2011. The derivative financial liabilities of RMB5,323,000, representing the fair value of the exercised warrants at the exercise date, were transferred to share premium.

Management has used the Black-Scholes valuation model to determine the fair value of the IFC Warrants, which was recognised as financial liabilities. Significant judgement, such as risk free rate, dividend yield and expected volatility, is required to be made by management as the parameters for applying the Black-Scholes valuation model.

The fair value of the IFC warrants is as follows:

	IFC Warrants
	RMB'000
At 1 January 2012	5,072
Fair value change credited to profit or loss	(1,855)
At 31 December 2012	3,217
At 1 January 2013	3,217
Fair value change credited to profit or loss	(3,168)
At 31 December 2013	49

The fair value of the IFC Warrants as of 31 December 2013, determined using the Black-Scholes valuation model, was HKD0.002 (approximately RMB0.002) per share (2012: HKD0.011, approximately RMB0.009). The significant inputs into the model are as follows:

	31 December 2013	31 December 2012
Share prices at the valuation date (HKD)	0.093	0.118
Volatility	43%	42%
Dividend yield	nil	Nil
Annual risk-free interest rate	0.12%	0.10%

(b) **Warrants and put-option of bonds issued to Asian equity and PA International**

On 29 June 2012, the Company issued warrants to Asian Equity and PA International at nil consideration (the "Warrants"), which provided Asian Equity and PA International the right to subscribe 875,000,000 ordinary shares of HKD0.02 each from the Company at an exercise price of HKD0.16 per share. The subscription rights attaching to the Warrants may be exercised by Asian Equity and PA International with expiry date on 7 July 2015. Pursuant to the warrant subscription agreement, Asian Equity and PA International have the put option, which is exercisable within the last 14 days before the maturity date of Warrants (i.e. 7 July 2015), to require the Company buy back unexercised warrants at a price of HKD0.0448 per warrant.

Pursuant to the bond subscription agreement, Asian Equity and PA International also have a put option ("Put Option of Bonds"), which is exercisable from 7 July 2014 to 7 July 2015, to force early redemption of 50% of the bond principle and the related interest accrued at a nominal interest rate of 9% per annum.

Management has used the binominal valuation model in determining the fair value of the Warrants and Put Option of Bonds.

The fair value of the Warrants and Put Option of Bonds are as follows:

	Warrants	Put option of Bonds	Total
	RMB'000	*RMB'000*	*RMB'000*
Fair value at date of issue	33,519	7,459	40,978
Fair value change credited to profit or loss	(7,654)	(11)	(7,665)
At 31 December 2012	25,865	7,448	33,313
At 1 January 2013	25,865	7,448	33,313
Fair value change credited to profit or loss	(1,586)	(1,285)	(2,871)
At 31 December 2013	24,279	6,163	30,442

The significant inputs into the model are as follows:

	31 December 2013	31 December 2012
Share prices at the valuation date (HKD)	0.093	0.118
Debt rate	23.31%	25.28%
Volatility	46%	41%
Dividend yield	nil	Nil
Annual risk-free interest rate	0.38%	0.12%

20 DEFERRED SUBSIDY INCOME — GROUP

	Government grant for production facilities
	RMB'000
At 1 January 2012	7,476
Amortisation (Note 28)	(2,930)
At 31 December 2012	4,546
At 1 January 2013	4,546
Amortisation (Note 28)	(654)
At 31 December 2013	3,892

21 DEFERRED INCOME TAX — GROUP

There were no offsetting of deferred income tax assets and liabilities in 2013 and 2012.

	2013	2012
	RMB'000	*RMB'000*
Deferred tax assets:		
— To be recovered after more than 12 months	10,156	2,059
— To be recovered within 12 months	52	52
	10,208	2,111
Deferred tax liabilities:		
— To be settled after more than 12 months	(80,867)	(80,867)
— To be settled within 12 months	(5,485)	(5,485)
	(86,352)	(86,352)

The movements in deferred income tax assets and liabilities are as follows:

Deferred income tax assets:

	Tax losses	Impairment of assets	Deferred subsidy income	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
At 1 January 2012	1,012	679	472	2,163
Charged to profit or loss	—	—	(52)	(52)
At 31 December 2012	1,012	679	420	2,111
At 1 January 2013	1,012	679	420	2,111
Charged to profit or loss	8,149	—	(52)	8,097
At 31 December 2013	9,161	679	368	10,208

Deferred income tax liabilities:

	Mining right (note 8)	Withholding tax of the unremitted earnings of PRC subsidiaries	Total
	RMB'000	*RMB'000*	*RMB'000*
At 31 December 2012 and 1 January 2013	(80,867)	(5,485)	(86,352)
Charged to income statement (Note 30)	—	—	—
At 31 December 2013	(80,867)	(5,485)	(86,352)

As at 31 December 2013, the Group had total unused tax losses of approximately RMB154,088,000 (2012: RMB109,200,000). No deferred tax asset has been recognized in respect of tax losses of certain subsidiaries of RMB35,756,000 (2012: RMB45,433,000) due to the unpredictability of future profit streams of these subsidiaries. Deferred tax asset of RMB24,136,000 (2012: RMB15,942,000) has been recognised in respect of the tax losses of certain subsidiaries of RMB118,332,000 (2012: RMB63,767,000) as management considered it is probable that these subsidiaries can generate sufficient taxable profit to utilise the above tax loss of RMB118,332,000.

In accordance with the enterprise income tax laws in Mainland China, a 10% withholding tax will be levied on the dividend declared by the companies established in Mainland China to their foreign investors starting from 1 January 2008. A lower withholding tax rate of 5% is applied to Mainland China subsidiaries of the Company, whose direct foreign investors are incorporated in Hong Kong, because of the treaty arrangement between Mainland China and Hong Kong. As at 31 December 2013, the deferred tax liabilities recognised for withholding tax on accumulated earning generated by Mainland China subsidiaries amount to RMB5,485,000 (2012: RMB5,485,000) on the earning of RMB109,700,000 (2012: RMB109,700,000) generated by other Mainland China subsidiaries. (Note 4(g)).

22 TRADE AND OTHER PAYABLES

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Trade payables (Note a)	20,075	33,084	—	—
Notes payable (Note b)	10,703	—	—	—
Construction payable	101,384	45,622	—	—
Advances from customers	90,590	81,209	—	—
Advances from purchasers (Note 15)	131,100	131,100	—	—
Accrued expenses	41,514	8,024	461	1,142
Deposits from suppliers	885	9,806	—	—
Other taxes payable	1,154	2,475	—	—
Others	22,201	12,160	—	—
	419,606	323,480	461	1,142

The carrying amounts of the Group's and the Company's trade and other payables are denominated in the following currencies:

	Group		Company	
	2013	**2012**	**2013**	**2012**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
RMB	419,145	322,338	—	—
HKD	461	1,142	461	1,142
	419,606	323,480	461	1,142

(a) **Trade payables**

The ageing analysis of trade payables of the Group is as follows:

	2013	**2012**
	RMB'000	*RMB'000*
Aged:		
Less than 1 year	16,681	26,716
More than 1 year but not exceeding 2 years	2,096	2,787
More than 2 years but not exceeding 3 years	1,006	3,070
More than 3 years	292	511
	20,075	33,084

(b) **Notes payable**

Notes payable represented bank acceptance notes issued by the Group and were interest-free and with maturity dates of less than 1 year.

As at 31 December 2013, the Group's cash of RMB10,703,000 (2012: Nil) was deposited in certain banks as guarantee deposits for issuance of notes payables.

23 SHORT-TERM BORROWINGS GROUP

The short-term borrowings are denominated in RMB and were issued at fixed interest rates which range from 5.60% to 8.86% (2012: 5.60% to 8.86%) per annum.

Total short-term borrowings amounted to RMB2,009,905,000 (2012: RMB1,635,571,000) are secured by bank deposits of RMB1,414,404,000 (2012: bank deposit of RMB1,212,765,000) and guaranteed by Mr. Li Weiruo, a shareholder and director of the Company.

The fair value of short-term borrowings approximate to their carrying amounts, as the impact of discounting is not significant. It falls under level 3 in the fair value hierarchy.

The exposure of the short-term borrowings to the contractual repricing dates are as follows:

	2013	**2012**
	RMB'000	*RMB'000*
6 months or less	2,191,575	1,729,961
Between 6 months to 1 year	392,000	204,000
	2,583,575	1,933,961

24 TURNOVER

Turnover represents invoiced value of sale of chemical products and chemical fertilisers to customers in Mainland China, net of goods returned and value-added tax, where applicable.

The Group's sales made in Mainland China are subject to value-added tax ("output value-added tax"). Such output value-added tax is payable after offsetting input value-added tax paid by the Group on purchases. The applicable rates of output value-added tax range from 0% to 17%.

The Group's turnover and profit are generated from one segment, i.e. manufacturing and sale of chemical products and chemical fertilisers in Mainland China, no segment information is therefore presented.

The Group has a number of customers and revenue generated from the top two customers are accounted for 19% and 10% respectively of the Group's turnover during the year.

25 EXPENSES BY NATURE

	2013	2012
	RMB'000	*RMB'000*
Raw materials and consumables used	502,746	330,824
Changes in inventories of finished goods and work in progress	13,853	(13,697)
Power and natural gas consumed	552,643	579,437
Staff costs (Note 26)	68,669	56,321
Depreciation and amortisation charges	76,309	74,831
Transportation expenses	46,373	49,529
Maintenance expenses	29,298	31,285
Legal and professional fees	1,561	3,222
Stamp duty and other tax	6,747	5,143
Advertisement expenses	1,273	1,143
Auditors' remuneration	2,267	2,267
Operating lease payments	1,016	1,278
Loss on disposal of property, plant and equipment (Note 34)	97	1,915
Other expenses	27,471	14,710
Total cost of sales, distribution costs and administrative expenses	1,330,323	1,138,208

26 STAFF COSTS

	2013	2012
	RMB'000	*RMB'000*
Wages and salaries	51,459	47,362
Pension costs — defined contribution plans	2,207	2,124
Social security costs — defined contribution plans	6,987	6,835
Share options granted to directors and employees (Note 16(b))	8,016	—
	68,669	56,321

27 DIRECTORS' AND SENIOR MANAGEMENT'S EMOLUMENTS

(a) Directors' emoluments

The remuneration of every director for the year ended 31 December 2013 is set out below:

Name of director	Fees	Salaries, allowances, and benefits in kind	Contributions to pension schemes	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Executive Directors	1,248	780	17	2,045
Mr. Li Weiruo				
Mr. Yuan Bai (Chief executive) (Note a)	234	942	42	1,218
Ms. Chi Chuan	234	642	—	876
Mr. Li Shengdi	234	642	—	876
Ms. Man Au, Vivian	234	436	10	680
Independent non-executive directors				
Mr. Hu Xiaoping	94	—	—	94
Mr. Woo Che-wor, Alex	94	—	—	94
Mr. Qian Laizhong	94	—	—	94
Mr. Sun Tong Chuan	16	—	—	16
	2,482	3,442	69	5,993

Note:

(a) Mr. Li Feng, who newly joined the Group in 2014, has taken over from Mr. Yuan Bai as the Chief executive of the Group.

The remuneration of every director for the year ended 31 December 2012 is set out below:

Name of director	Fees	Salaries, allowances, and benefits in kind	Contributions to pension schemes	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
Executive Directors				
Mr. Li Weiruo	1,280	1,100	17	2,397
Mr. Yuan Bai (Chief executive)	240	1,102	41	1,383
Ms. Chi Chuan	240	802	—	1,042
Mr. Li Shengdi	240	802	31	1,073
Ms. Man Au, Vivian	240	573	11	824
Independent non-executive directors				
Mr. Hu Xiaoping	112	—	—	112
Mr. Woo Che-wor, Alex	112	—	—	112
Mr. Qian Laizhong	112	—	—	112
	2,576	4,379	100	7,055

(b) **Five highest paid individuals**

The five individuals whose emoluments were the highest in the Group for the year include four (2012: four) directors whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining one individual in 2013 are as follows:

	RMB'000
Basic salaries, housing allowances, other allowances and benefits in kind	967
Contributions to pension schemes	—
	967

The emolument fell within the following bands:

	2013
Emolument bands	
Nil to RMB1,000,000 (approximately HKD1,266,000)	1

During the year, the Group did not pay any amount to the five highest paid individuals nor any other directors of the Company as an inducement to join or upon joining the Group or as compensation for loss of office and no directors waived any emoluments during the year.

28 OTHER INCOME — NET

	2013	2012
	RMB'000	*RMB'000*
Loss of sales of scrap materials, net	—	(643)
Amortisation of deferred subsidy income (Note 20)	654	2,930
Subsidy income	140	1,400
Rental income, net	1,104	—
Fair value change on derivative financial liabilities (Note 19)	6,039	9,520
Others, net	1,336	133
	9,273	13,340

29 FINANCE COSTS — NET

	2013	2012
	RMB'000	*RMB'000*
Interest expense of bank borrowings	158,969	132,094
Interest expense of borrowing from IFC	8,936	10,847
Interest expense of borrowing from Asian Equity and PA International	23,966	9,494
Less: capitalisation in construction-in-progress (Note 6)	(65,316)	(36,364)
	126,555	116,071
Interest income	(44,653)	(26,639)
Exchange gain, net	(2,614)	(220)
Others	3,171	4,292
	82,459	93,504

30 INCOME TAX EXPENSE

No provision for profits tax in the Cayman Islands, British Virgin Islands or Hong Kong has been made, as the Group had no assessable profit arising in or derived from those jurisdictions during the years ended 31 December 2012 and 2013.

Dazhou Ko Yo Chemical qualifies as a foreign investment production enterprise and is located in the western region in Mainland China. As approved by local tax bureau, it is subject to the preferential tax policies for the development of western region with Enterprise Income Tax ("EIT") at the rate of 15% in 2012 and 2013.

The applicable income tax rate of Ko Yo Agrochem, Chengdu Ko Yo Chemical and Chengdu Ko Yo Compound in 2013 and 2012 is 25%.

Other subsidiaries located in Mainland China did not have assessable profit for the year ended 31 December 2013 (2012: Nil).

The amount of taxation charged to the consolidated statement of comprehensive income represents:

	2013	**2012**
	RMB'000	*RMB'000*
Current income tax for Mainland China	1,229	23,137
Deferred income tax	(8,097)	3,849
	(6,868)	26,986

The taxation on the Group's (loss)/profit before income tax differs from the theoretical amount that would arise using the taxation rate of 15%, the tax rate of Dazhou KoYo Chemical, the major subsidiary of the Company. The difference is analysed as follows:

	2013	**2012**
	RMB'000	*RMB'000*
(Loss)/profit before income tax	(64,257)	128,598
Tax calculated at a taxation rate of 15% (2012: 15%)	(9,638)	19,290
Tax rate difference	509	902
Expenses not deductible for tax purposes	177	207
Withholding tax accrued on the earnings expected to be remitted by subsidiaries (Note 21)	—	5,485
Tax losses for which no deferred income tax was recognised	2,990	2,530
Income not subject to tax (Note 19)	(906)	(1,428)
Taxation	(6,868)	26,986

31 (LOSS)/PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

The loss attributable to equity holders of the Company is dealt with in the financial statements of the Company to the extent of RMB1,404,000 (2012: RMB6,141,000 profit).

32 EARNINGS PER SHARE

(a) Basic

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year (Note 16).

	2013	2012
(Loss)/Profit attributable to equity holders of the Company *(RMB'000)*	(57,056)	101,612
Weighted average number of ordinary shares in issue *(thousands)*	7,195,285	7,195,285
Basic (loss)/profit per share *(RMB per share)*	(0.0079)	0.0141

(b) Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Company had two categories of dilutive potential ordinary shares: share options and warrants. For the share options and warrants, a calculation was made in order to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding share options and warrants. The number of shares calculated as above was compared with the number of shares that would have been issued assuming the exercise of the share options and warrants.

	2013	2012
(Loss)/Profit attributable to equity holders of the Company *(RMB'000)*	(57,056)	101,612
Weighted average number of ordinary shares in issue *(thousands)*	7,195,285	7,195,285
Adjustment — warrants and share option *(thousands)*	—	6,156
Weighted average number of ordinary shares for diluted earnings per share *(thousands)*	7,195,285	7,201,441
Diluted (loss)/earnings per share *(RMB per share)*	(0.0079)	0.0141

The calculation of diluted loss per share for the year ended 31 December 2013 has not assumed the exercise of the share options and warrants as these potential ordinary shares are anti-dilutive during the year.

33 DIVIDEND

The directors do not recommend the payment of an interim dividend and a final dividend for the 6 months ended 30 June 2013 (2012: nil) and the year ended 31 December 2013 (2012: nil).

34 CASH GENERATED FROM OPERATIONS

(a) Reconciliation of loss before taxation to cash generated from operating activities

	2013	**2012**
	RMB'000	*RMB'000*
(Loss)/Profit before income tax	(64,257)	128,598
Depreciation of property, plant and equipment	74,850	73,376
Depreciation of investment properties	208	—
Amortisation of land use rights	1,189	1,185
Amortisation of intangible assets	270	270
Loss on disposal of property, plant and equipment (Note 25)	97	1,915
Interest income (Note 29)	(44,653)	(26,639)
Interest expense (Note 29)	126,555	116,071
Fair value of share option granted	8,016	—
Exchange loss	345	—
Fair value change of derivative financial liabilities	(6,039)	(9,520)
Operating profit before working capital changes	96,581	285,256
Decrease/(increase) in inventories	15,372	(15,411)
(Increase)/decrease in trade and other receivables	(151,109)	42,286
Increase/(decrease) in trade and other payables	30,398	(22,641)
Decrease in deferred subsidy income	(654)	(2,930)
Cash (used in)/generated from operating activities	(9,412)	286,560

(b) **In the cash flow statement, proceeds from disposal of property, plant and equipment comprise:**

	2013	2012
	RMB'000	*RMB'000*
Net book amount (Note 6)	447	1,915
Loss on disposal of property, plant and equipment (Note 25)	(97)	(1,915)
Proceeds from disposal of property, plant and equipment	350	—

35 COMMITMENTS — GROUP

(a) **Capital commitments for property, plant and equipment**

	2013	2012
	RMB'000	*RMB'000*
Constructions-in-progress:		
Contracted but not provided for	33,758	278,047

(b) **Commitments under operating leases**

The Group leases offices under non-cancellable operating lease agreements. The lease terms are between 1 and 2 years, and the majority of lease agreements are renewable at the end of the period at market rate.

The Group had future aggregate minimum lease payments under non-cancellable operating leases for land and buildings are as follows:

	2013	2012
	RMB'000	*RMB'000*
Not later than 1 year	135	885
Later than 1 year and not later than 5 years	—	135
	135	1,020

The Company had no capital commitment and no commitments under operating leases as at 31 December 2013 (2012: Nil).

36 RELATED-PARTY TRANSACTIONS

The Group is controlled by Mr. Li Weiruo, who owns approximately 40.7% of the Company's issued shares as at 31 December 2013 (2012: 40.7%). The remaining approximately 59.3% of the issued shares are widely held.

Long-term borrowings of RMB358,512,000 (2012: RMB 247,046,000) and short-term borrowings of RMB121,300,000 (2012: RMB31,300,000) were guaranteed by Mr. Li Weiruo with no charge. In the opinion of the directors of the Company, the fair value of guarantee provided by Mr. Li Weiruo is insignificant to the Group. Such guarantee has not been accounted for by the Group.

37 KEY MANAGEMENT COMPENSATION (EXCLUDING DIRECTORS' EMOLUMENTS)

	2013	**2012**
	RMB'000	*RMB'000*
Salaries and other short-term employee benefits	4,337	3,014

The directors' emoluments are disclosed in Note 27.

38 EVENT AFTER THE BALANCE SHEET DATE

Subsequent to the balance sheet date and up to the date of approval of the financial statements, short-term borrowings of approximately RMB170 million have been rolled over for a further year. New short-term borrowings of RMB80 million have been granted and drawn down with a term of 6 months.

3. LATEST UNAUDITED FINANCIAL STATEMENTS FOR THE SIX MONTHS ENDED 30 JUNE 2014

The board of directors (the "Directors" or the "Board") of Ko Yo Chemical (Group) Limited (the "Company") is pleased to present the unaudited condensed consolidated operating results of the Company and its subsidiaries (collectively, the "Group") for the six months ended 30 June 2014 together with the unaudited comparative figures for the corresponding periods in 2013 are as follows:

UNAUDITED CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT
For the six months ended 30 June 2014

		Six months ended 30 June	
		2014	**2013**
	Notes	*RMB'000*	*RMB'000*
Turnover	3	738,166	680,756
Cost of sales		(686,160)	(570,467)
Gross profit		52,006	110,289
Interest income		22,203	21,343
Distribution costs		(38,094)	(29,464)
Administrative expenses		(26,485)	(33,669)
Other income		690	3,417
Operating profit	4	10,320	71,916
Finance costs		(37,574)	(41,227)
(Loss)/Profit before taxation		(27,254)	30,689
Taxation	5	4,172	(5,259)
(Loss)/Profit attributable to shareholders		(23,082)	25,430
Basic (loss)/earning per share (RMB cents)	6	(0.32)	0.35
Diluted (loss)/earnings per share (RMB cents)	6	(0.32)	0.35
Declared dividends per share (HK cents)	7	Nil	Nil

CONDENSED CONSOLIDATED BALANCE SHEET
As at 30 June 2014 and 31 December 2013

	Notes	(Unaudited) As at 30 June 2014 *RMB'000*	(Audited) As at 31 December 2013 *RMB'000*
ASSETS			
Non-current assets			
Property, plant and equipment		2,723,538	2,568,621
Deferred income tax assets	11	14,454	10,208
Investment properties		13,438	13,654
Mining right		334,306	334,306
Intangible assets		10,547	10,898
Land use rights		153,123	53,027
		3,249,406	2,990,714
Current assets			
Inventories		47,370	43,259
Trade and other receivables	8	310,270	360,905
Prepaid income tax, net		—	7,300
Pledged bank deposits		1,500,530	1,726,298
Cash and bank deposits		117,008	116,683
Non-current assets held for sale		198,784	198,784
		2,173,962	2,453,229
Total assets		5,423,368	5,443,943
EQUITY			
Share capital		138,618	138,618
Reserves Others		907,332	930,414
Shareholders' funds		1,045,950	1,069,032
Non-controlling interest		4,167	3,267
Total equity		1,050,117	1,072,299

	Notes	(Unaudited) As at 30 June 2014 RMB'000	(Audited) As at 31 December 2013 RMB'000
LIABILITIES			
Current liabilities			
Trade and other payables	9	526,250	419,606
Short-term borrowings, secured	10	2,632,151	2,583,575
Current portion of long term borrowings, secured	10	168,031	207,510
Derivative financial liabilities		30,491	30,491
		3,356,923	3,241,182
Non-current liabilities			
Long-term borrowings, secured	10	926,189	1,040,218
Deferred subsidy income		3,787	3,892
Deferred income tax liabilities	11	86,352	86,352
		1,016,328	1,130,462
Total liabilities		4,373,251	4,371,644
Total equity and liabilities		5,423,368	5,443,943
Net current liabilities		(1,182,961)	(787,953)
Total assets less current liabilities		2,066,445	2,202,761

UNAUDITED CONDENSED CONSOLIDATED CASH FLOW STATEMENT
For the six months ended 30 June 2014 and 30 June 2013

	Six months ended 30 June	
	2014	**2013**
	RMB'000	*RMB'000*
Net cash generated from operating activities	180,438	96,652
Interest paid	(37,574)	(41,227)
Net cash inflow from operating activities	142,864	55,425
Investing activities		
Purchases of fixed assets and payments for construction-in-progress	(286,478)	(323,596)
Proceeds from sale of equity interest of a subsidiary	900	—
Interest received	22,203	21,343
Net cash outflow from investing activities	(263,375)	(302,253)
Net cash outflow before financing activities	(120,511)	(246,828)
Financing activities		
Decrease/(Increase) in pledged bank deposits	225,768	(296,400)
New loans payable	2,015,843	934,931
Repayment of bank loans	(2,120,775)	(325,351)
Net cash inflow from financing activities	120,836	313,180
Increase/(Decrease) in cash and cash equivalents	325	66,352
Cash and cash equivalents at 1 January	116,683	350,752
Cash and cash equivalents at 30 June	117,008	417,104

UNAUDITED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
For the six months ended 30 June 2014 and 30 June 2013

	Share Capital	Share Premium	Merger Reserve	Share-based compensation	Reserve Fund	Enterprise Expansion Fund	Retained Earnings	Transaction to NCI	NCI	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
At 1 January 2013 (audited)	138,618	550,133	(22,041)	14,186	44,952	1,131	394,693	—	—	1,121,672
Net Profit for the 6 Months ended 30 June 2013	—	—	—	—	—	—	25,430	—	—	25,430
Fair value of share options granted	—	—	—	6,995	—	—	—	—	—	6,995
Transfer of equity interest to non-controlling interests ("NCI")	—	—	—	—	—	—	—	(3,600)	3,600	—
At 30 June 2013	138,618	550,133	(22,041)	21,181	44,952	1,131	420,123	(3,600)	3,600	1,154,097
At 1 January 2014 (audited)	138,618	550,133	(22,041)	22,202	45,273	1,131	337,316	(3,600)	3,267	1,072,299
Net loss for the 6 Months ended 30 June 2014	—	—	—	—	—	—	(23,082)	—	—	(23,082)
Sales of equity interest to non-controlling interests ("NCI")	—	—	—	—	—	—	—	—	900	900
At 30 June 2014	138,618	550,133	(22,041)	22,202	45,273	1,131	314,234	(3,600)	4,167	1,050,117

NOTES OF FINANCIAL STATEMENTS

1. Basis of Preparation

The Company is an investment holding company. The Group is principally engaged in the manufacture and sale of chemical products and chemical fertilizers in Mainland China.

The unaudited interim financial statements have been prepared in accordance with the Hong Kong Accounting Standard ("HKAS") 34 "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and the disclosure requirements set out in Appendix 16 of the Rules Governing the Listing of the Securities (the "Listing Rules") of The Stock Exchange of Hong Kong Limited (the "Stock Exchange").

2. Principal Accounting Policies

The principal accounting policies used in the unaudited interim financial statements are consistent with those followed in the Group's financial statements for the year ended 31 December 2013. The measurement basis used in the preparation of the unaudited interim financial statements is historical cost, except for certain investment properties and financial investments, which are measured at fair values. All inter-company transactions and balances within the Group have been eliminated on consolidation.

The Group had net current liabilities of RMB1,182,961,000 as at 30 June 2014. The directors of the Company have given due consideration to the liquidity of the Group and have adopted the going concern basis in preparing the consolidated financial statements for the six months ended 30 June 2014 on the basis that the commence production of Guangan plant in lower half of 2014, the proposed transaction on issue of new shares and convertible bonds (details set out on the header Event After the Balance Date), sufficient bank deposit and that it will succeed in negotiating with its bankers to roll over the outstanding bank loans.

The financial statements are unaudited but have been reviewed by the audit committee of the Company.

3. Turnover

Turnover represents the net amounts received and receivables for chemical products and chemical fertilizers sold, less returns and allowances and value-added taxes, if applicable, during the six months period. The Group's revenues are primarily generated in the People's Republic of China (the "PRC").

Turnover consisted of the following products:

	Six months ended 30 June 2014 (unaudited)		Six months ended 30 June 2013 (unaudited)	
	RMB'000	*%*	*RMB'000*	*%*
BB & complex fertilizers	29,973	4.1	33,423	4.9
Urea	337,629	45.7	427,486	62.8
Ammonia	108,062	14.6	105,684	15.5
Others (Note)	262,502	35.6	114,163	16.8
	738,166	100	680,756	100

Note: Others are carbon dioxide and the trading of urea, phosphate fertilizers, potash fertilizers, sodium carbonate, ammonia and methanol.

4. **Operating Profit**

Operating profit is stated after crediting and charging the following:

	Six months ended 30 June	
	2014	**2013**
	RMB'000	*RMB'000*
Charging:		
Staff costs (including directors' emoluments)		
— Salaries, wages and other benefits	29,053	27,074
— Contributions to retirement scheme	3,957	4,634
Cost of inventories	686,160	570,467
Loss on disposal of fixed assets	11	245
Operating leases for buildings	415	719
Depreciation and amortization charges	32,022	35,107
Fair value of share options granted	—	6,995
Auditors' remuneration	1,089	1,159

5. **Taxation**

No provision for profits tax in the Cayman Islands, the British Virgin Islands or Hong Kong has been made, as the Group had no assessable profit arising in or derived from those jurisdictions during the six months ended 30 June 2014.

The applicable income tax rate of Chengdu Ko Yo Chemical Industry Co., Ltd. ("Chengdu Ko Yo Chemical"), Chengdu Ko Yo Compound Fertilisers Co., Ltd. ("Chengdu Ko Yo Compound") and Sichuan Ko Yo Agrochem Co., Ltd. ("Ko Yo Agrochem") in 2013 are 25%.

Dazhou Koyo Chemical Industry Co., Ltd. ("Dazhou Ko Yo") qualifies as a foreign investment production enterprise and is located in the western region in Mainland China. As approved by local tax bureau, it is subject to the preferential tax policies for the development of western region with Enterprises Income Tax ("EIT") at the rate of 15%.

Accordingly, current income tax provision made for Ko Yo Agrochem for the six months ended 30 June 2014 was approximately RMB74,000. The income tax benefit made for Dazhou Ko Yo for the six months ended 30 June 2014 was approximately RMB4,272,000.

Chengdu Ko Yo Compound, Chengdu Ko Yo Chemical and Qingdao Ko Yo Chemical Co., Ltd. did not have current income tax provision for the six months ended 30 June 2014.

The amount of taxation charged to the unaudited condensed consolidated profit and loss account represents:

	Six months ended 30 June	
	2014	**2013**
	RMB'000	*RMB'000*
Current tax in the PRC	74	5,233
Deferred income tax (Note 11)	(4,246)	(26)
	(4,172)	5,259

6. **Earnings per Share**

The calculation of the basic and diluted earnings per share for the six months ended 30 June 2014 and 2013 were based on:

	Six months ended 30 June	
	2014	**2013**
	RMB'000	*RMB'000*
(Loss)/Profit for the period	(23,082)	25,430
Weighted average number of shares for calculation of basic earnings per share	7,195,284,615	7,195,284,615
Effect of dilutive potential shares on the outstanding share options	—	56,511
Weighted average number of shares for calculation of diluted earnings per share	7,195,284,615	7,195,341,126

7. Dividend

The Board does not recommend the payment of any dividend for the six months ended 2014.

8. Trade and Other Receivables

	(Unaudited) As at 30 June 2014 *RMB'000*	(Audited) As at 31 December 2013 *RMB'000*
Trade receivables	6,927	5,207
Prepayments, purchase deposits and other deposits	110,666	217,219
Notes receivable	—	3,285
Other receivables	192,677	135,194
	310,270	360,905

In general, the credit terms granted by the Group ranged from 0 to 3 months. The aging analysis of trade receivables is as follows:

	(Unaudited) As at 30 June 2014 *RMB'000*	(Audited) As at 31 December 2013 *RMB'000*
Aged:		
Less than 3 months	5,297	5,207
More than 3 months but not exceeding 1 year	1,630	—
More than 1 year but not exceeding 2 years	—	—
More than 2 years but not exceeding 3 years	—	—
More than 3 years	5,241	5,241
	12,168	10,448
Less: provision for doubtful receivables	(5,241)	(5,241)
	6,927	5,207

9. **Trade and Other Payables**

	(Unaudited) As at 30 June 2014 *RMB'000*	(Audited) As at 31 December 2013 *RMB'000*
Trade payables	79,807	20,075
Construction payable	123,818	101,384
Deposits from customers	164,599	91,475
Accruals and other payables	158,026	206,672
	526,250	419,606

The aging analysis of trade payables is as follows:

	(Unaudited) As at 30 June 2014 *RMB'000*	(Audited) As at 31 December 2013 *RMB'000*
Aged:		
Less than 1 year	78,974	16,681
More than 1 year but not exceeding 2 years	833	2,096
More than 2 years but not exceeding 3 years	—	1,006
More than 3 years	—	292
	79,807	20,075

10. **Borrowings**

	(Unaudited) As at 30 June 2014 *RMB'000*	(Audited) As at 31 December 2013 *RMB'000*
Short-term borrowings, secured	2,632,151	2,583,575
Long-term borrowings repayable:		
Less than 1 year	168,031	207,510
Between 1 and 2 years	234,351	346,073
Between 2 and 5 years	691,838	694,145
Over 5 years	—	—
	1,094,220	1,247,728
Within 1 year included in current liabilities	(168,031)	(207,510)
	926,189	1,040,218

As at 30 June 2014, the borrowings of the Group were generally secured by certain fixed assets and pledged cash deposits of the Group. These borrowings bear interest at the rate of 4.85% to 9.00% (2013: 4.96% to 9.00%) per annum.

11. **Deferred Income Tax**

There were no offsetting of deferred income tax assets and liabilities in 2013 and in six months period ended 2014.

Deferred income tax assets:

	Loss available for offsetting future taxable profits *RMB'000*	Impairment of assets *RMB'000*	Deferred subsidy income *RMB'000*	Total *RMB'000*
At 31 December 2013	9,161	679	368	10,208
Charged to income statement	4,272	—	(26)	4,246
At 30 June 2014	13,433	679	342	14,454

Deferred income tax liabilities:

	Evaluation and exploration assets	Withholding tax	Total
	RMB'000	*RMB'000*	*RMB'000*
At 31 December 2013	(80,867)	(5,485)	(86,352)
At 30 June 2014	(80,867)	(5,485)	(86,352)

4. STATEMENT OF INDEBTEDNESS

As at 30 June 2014, the Group had current liabilities comprised short-term borrowings of approximately RMB2,632,151,000, short-term portion for long-term borrowings of approximately RMB168,031,000, trade and notes payables of approximately RMB203,625,000, advances from customers of approximately RMB164,599,000 and accrued charges and other payables of approximately RMB158,026,000 and, outstanding capital commitments of approximately RMB129,000,000.

Save as aforesaid and apart from intra-group liabilities and normal trade payables, the Group did not have any mortgages, charges, debentures, loan capital, bank loan and overdrafts, debt securities or other similar indebtedness, finance leases or hire purchase commitments, liabilities under acceptances or acceptance creditors, or any guarantees, or other material contingent liabilities outstanding at the close of business on 30 June 2014.

The Directors have confirmed that there have been no material changes in the indebtedness and contingent liabilities of the Group since 30 June 2014 up to and including the Latest Practicable Date.

5. MATERIAL CHANGE

The Directors confirm that, save and except for the following, there has been no material change in the financial or trading position or outlook of the Group since 31 December 2013, being the date to which the latest published audited consolidated financial statements of the Group were made up to, and including the Latest Practicable Date:

1. the entering into of the Subscription Agreement and the Loan Agreement, which are expected to improve the financial position and liquidity of the Group;

2. the publication of the Group's unaudited interim result announcement for the six months ended 30 June 2014 on 26 August 2014 where it was disclosed that, among other things, (a) the Group recorded a loss attributable to the shareholders of the Company for the six

months ended 30 June 2014 as compared to a profit attributable to the shareholders of the Company for the corresponding period in 2013, and (b) a decrease in the Group's gross profit margin for the six months ended 30 June 2014 as compared to that of the corresponding period in 2013; and

3. the exercise of 875,000,000 Warrants and 16,500,000 Share Options up to the Latest Practicable Date which have been converted into a total of 704,000,000 Existing Shares as at the Latest Practicable Date which resulted in the enlargement of the Company's capital base and asset value and improvement in the Company's cash flow position.

1. RESPONSIBILITY STATEMENT

This circular, for which the Directors collectively and individually accept full responsibility, includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that to the best of their knowledge and belief the information contained in this circular is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement herein or this circular misleading.

This circular includes particulars given in compliance with the Takeovers Code. The Directors jointly and severally accept full responsibility for the accuracy of the information contained in this circular and confirm, having made all reasonable enquiries, that to the best of their knowledge, opinions expressed in this circular have been arrived at after due and careful consideration and there are no other facts not contained in this circular, the omission of which would make any statement in this circular misleading.

The director of the Subscriber accepts full responsibility for the accuracy of the information contained in this circular relating to the Subscriber and persons acting in concert with it and confirm, having made all reasonable enquiries, that to the best of his knowledge, opinions expressed in this circular have been arrived at after due and careful consideration and there are no other facts not contained in this circular, the omission of which would make any statement in this circular misleading.

2. SHARE CAPITAL, OPTIONS, WARRANTS AND CONVERTIBLE SECURITIES

(a) Share capital

Set forth below is the authorised share capital of the Company as at the Latest Practicable Date, upon the Share Consolidation, and following the completion of the proposed increase in the authorised share capital of the Company:

Authorised share capital:		*HK$*
20,000,000,000	Existing Shares of HK$0.02 each	400,000,000
4,000,000,000	Consolidated Shares of HK$0.10 each upon the Effective Date	400,000,000
8,000,000,000	Consolidated Shares of HK$0.10 each upon completion of the proposed increase in the authorised share capital of the Company	800,000,000

The issued share capital of the Company as at the Latest Practicable Date, upon the Share Consolidation, and following the completion of the issue of the New Shares and the Conversion Shares:

Issued and fully paid or credited as fully paid:		*HK$*
7,899,284,615	Existing Shares of HK$0.02 each	157,985,692.3
Upon the Share Consolidation, and following the completion of the issue of the New Shares and the Conversion Shares:		
579,856,923	Consolidated Shares of HK$0.10 each	157,985,692.3
800,000,000	New Shares to be allotted and issued pursuant to the Subscription Agreement	80,000,000
2,600,000,000	new Consolidated Shares to be issued upon full exercise of the conversion rights attached to the Convertible Bonds	260,000,000
5,979,856,923	Consolidated Shares	497,985,692.3

All of the Existing Shares, the Consolidated Shares, the New Shares, and the Conversion Shares to be issued upon full exercise of the conversion rights attached to the Convertible Bonds will rank pari passu in all aspects, including rights as to dividend and voting. No part of the share capital of the Company is listed or dealt in on any other stock exchange other than the Stock Exchange.

704,000,000 Existing Shares have been issued since 31 December 2013, being the date to which the latest published audited consolidated financial statements of the Group were made up, and to the Latest Practicable Date.

(b) **Options, warrants and convertible securities**

As at the Latest Practicable Date, there are:

(a) outstanding Warrants which can be convertible into 187,500,000 Existing Shares (37,500,000 Consolidated Shares upon the Share Consolidation becoming effective) upon the exercise of the subscription rights attaching thereto. On 18 September 2014, the Company received a notice of exercise from PAG whereby PAG exercised the subscription rights attaching to the Warrants to subscribe for 187,500,000 Existing Shares, which are to be allotted and issued on 23 September 2014; and

(b) outstanding 272,600,000 Share Options which are convertible into 272,600,000 Existing Shares (54,520,000 Consolidated Shares upon the Share Consolidation becoming effective) upon the exercise of the subscription rights attaching thereto.

Warrants

On 29 June 2012, the Company issued the Warrants to Asian Equity and PA International at nil consideration, which provided Asian Equity and PA International the right to subscribe 875,000,000 ordinary shares of HK$0.02 each from the Company at an exercise price of HK$0.16 per share. The subscription rights attaching to the Warrants may be exercised by Asian Equity and PA International with expiry date on 7 July 2015. Pursuant to the warrant subscription agreement, Asian Equity and PA International have the put option, which is exercisable within the last 14 days before the maturity date of Warrants (i.e. 7 July 2015), to require the Company buy back unexercised warrants at a price of HK$0.0448 per Warrant. As at the Latest Practicable Date, Asia Equity and PA International had exercised the subscription rights attaching to the Warrants to subscribe for 687,500,000 Existing Shares.

Pursuant to the bond subscription agreement dated 29 June 2012, Asian Equity and PA International also have a put option ("Put Option of Bonds"), which is exercisable from 7 July 2014 to 7 July 2015, to force early redemption of 50% of the bond principle and the related interest accrued at a nominal interest rate of 9% per annum. As at the Latest Practicable Date, all of the outstanding amount of the bond were settled.

Share Options

The table below set forth the details of the outstanding Share Options:

Holders	**Date of grant**	**Exercise price per Existing Share** *HK$*	**Exercise period**	**Number of share options as of the Latest Practicable Date**
Directors				
Li Weiruo	16 May 2006	0.150	16 May 2006 to 10 April 2016	2,100,000
	14 January 2010	0.230	14 January 2010 to 13 January 2020	4,400,000
				6,500,000
Yuan Bai	16 May 2006	0.150	16 May 2006 to 10 April 2016	2,000,000
	14 January 2010	0.230	14 January 2010 to 13 January 2020	4,000,000
	28 March 2013	0.119	28 March 2013 to 27 March 2023	11,000,000
				17,000,000

Holders	Date of grant	Exercise price per Existing Share *HK$*	Exercise period	Number of share options as of the Latest Practicable Date
Chi Chuan	14 January 2010	0.230	14 January 2010 to 13 January 2020	2,000,000
	28 March 2013	0.119	28 March 2013 to 27 March 2023	21,000,000
				23,000,000
Man Au Vivian	14 January 2010	0.230	14 January 2010 to 13 January 2020	4,000,000
	28 March 2013	0.119	28 March 2013 to 27 March 2023	19,000,000
				23,000,000
Li Shengdi	14 January 2010	0.230	14 January 2010 to 13 January 2020	4,000,000
	28 March 2013	0.119	28 March 2013 to 27 March 2023	21,000,000
				25,000,000
Li Ciping	14 January 2010	0.23	14 January 2010 to 13 January 2020	12,000,000
Hu Xiaoping	23 November 2010	0.220	23 November 2010 to 22 November 2020	4,000,000
	28 March 2013	0.119	28 March 2013 to 27 March 2023	2,000,000
				6,000,000
Woo Che-wor Alex	23 November 2010	0.220	23 November 2010 to 22 November 2020	4,000,000
	28 March 2013	0.119	28 March 2013 to 27 March 2023	2,000,000
				6,000,000

Holders	Date of grant	Exercise price per Existing Share *HK$*	Exercise period	Number of share options as of the Latest Practicable Date
Qian Laizhong	16 May 2006	0.150	16 May 2006 to 10 April 2016	2,100,000
	23 November 2010	0.220	23 November 2010 to 22 November 2020	4,000,000
				6,100,000
Sun Tongchuan	15 November 2013	0.095	15 November 2013 to 14 November 2023	6,000,000
Employees	11 April 2006	0.150	11 April 2006 to 10 April 2016	32,500,000
	10 September 2007	0.116	10 September 2007 to 9 September 2017	23,000,000
	14 January 2010	0.230	14 January 2010 to 13 January 2020	15,500,000
	28 March 2013	0.119	28 March 2013 to 27 March 2023	71,000,000
				142,000,000
				272,600,000

Save as aforesaid, the Company has no other outstanding convertible securities, options or warrants in issue which confer any right to subscribe for, convert or exchange into the Existing Shares as at the Latest Practicable Date.

3. DISCLOSURE OF INTERESTS

(a) Interest in the Company

*i. **Director's interest in the Company***

As at the Latest Practicable Date, the interests and short positions of the Directors and chief executives in the shares, underlying shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO), which are required (a) to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they are taken or deemed to have under such provisions of the SFO); or (b) to be recorded in the register required to be kept under section 352 of the SFO; or (c) to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers contained in Listing Rules were as follows:

(i) *Long positions in the shares and the underlying shares of the Company*

Directors	Personal long position in shares (beneficial owner)	Personal long position in share options (beneficial owner)	Aggregate long position in shares and underlying shares	Total interests in the issued share capital
Li Weiruo	2,924,440,000	6,500,000	2,930,940,000	37.02%
Yuan Bai	366,464,000	17,000,000	383,464,000	4.85%
Chi Chuan	62,640,000	23,000,000	85,640,000	1.08%
Man Au Vivian	31,320,000	23,000,000	54,320,000	0.69%
Li Shengdi	—	25,000,000	25,000,000	0.32%
Li Ciping	—	12,000,000	12,000,000	0.15%
Hu Xiaoping	—	6,000,000	6,000,000	0.08%
Woo Che-wor, Alex	—	6,000,000	6,000,000	0.08%
Qian Laizhong	—	6,100,000	6,100,000	0.08%
Sun Tongchuan	—	6,000,000	6,000,000	0.08%

(ii) *Interests in shares of an associated corporation of the Company*

Name of Director	Name of company	Number of non-voting deferred shares	Capacity	Type of interests	Approximate interest in holding
Li Weiruo	Ko Yo Development Co., Ltd ("Ko Yo Hong Kong") *(Note)*	2,100,000	Beneficial Owner	Personal	70%
Yuan Bai	Ko Yo Hong Kong	420,000	Beneficial Owner	Personal	14%
Chi Chuan	Ko Yo Hong Kong	120,000	Beneficial Owner	Personal	4%
Man Au Vivian	Ko Yo Hong Kong	60,000	Beneficial Owner	Personal	2%

Note: a wholly-owned subsidiary of the Company

(iii) *Short positions in the shares of an associated corporation of the Company*

Name of Director	Name of company	Number of non-voting deferred shares	Capacity	Type of interest	Approximate interests in holding of such class
Li Weiruo	Ko Yo Hong Kong	2,100,000	Beneficial Owner	Personal	70%
Yuan Bai	Ko Yo Hong Kong	420,000	Beneficial Owner	Personal	14%
Chi Chuan	Ko Yo Hong Kong	120,000	Beneficial Owner	Personal	4%
Man Au Vivian	Ko Yo Hong Kong	60,000	Beneficial Owner	Personal	2%

ii. ***Substantial shareholders' and other persons' interests in the Existing Shares and underlying shares***

As at the Latest Practicable Date, so far as is known to any Director or chief executive of the Company, no person (not being a director or a Chief Executive of the Company) had an interest or short positions in the shares or underlying shares of the Company which are required to be notified to the Company and the Stock Exchange under Divisions 2 and 3 of Part XV of the SFO and recorded in the register required to be kept under section 336 of the SFO, and who were directly or indirectly deemed to be interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the Company.

iii. ***Other persons' interests in the Existing Shares and underlying shares***

(i) *Interest in the shares or underlying shares of the Company*

As at the Latest Practicable Date, so far as is known to any Director or Chief Executive of the Company and save as disclosed above, the following person (not being a director or a Chief Executive of the Company) had an interest or short positions in the shares or underlying shares of the Company which are required to be notified to the Company and the Stock Exchange under Divisions 2 and 3 of Part XV of the SFO and recorded in the register required to be kept under section 336 of the SFO, and who were directly or indirectly deemed to be interested in 5% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the Company.

Name	**Capacity**	**Number of shares**	**Approximate shareholding percentage**
International Finance Corporation	Beneficial Owner	414,724,615	5.25%

(ii) *Interests in shares of an associated corporation of the Company*

Name	**Name of company**	**Number and description of shares**	**Capacity**	**Type of interest**	**Approximate percentage of holding**
Tang Shiguo *(Note)*	Ko Yo Hong Kong	300,000 non-voting deferred shares	Beneficial owner	Personal	10%

Note: Mr. Tang Shiguo ceased to be a director of the Company with effect from 29th April 2004.

(iii) *Short positions in the shares of an associated corporation of the Company*

Name	**Capacity**	**Name of company**	**Number and description of shares**
Tang Shiguo	Beneficial owner	Ko Yo Hong Kong	300,000 non-voting deferred shares

Save as disclosed above, as at the Latest Practicable Date, the Directors and chief executive of the Company are not aware of any other persons (other than the Directors and the chief executive of the Company) who had, or was deemed to have, an interest and/or short position in the Shares or underlying shares of the Company which is required to be disclosed to the Company and the Stock Exchange under the provisions of Division 2 and 3 of Part XV of the SFO, or as recorded in the register required to be kept under Section 336 of the SFO, or who was, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the Company or any other member of the Group.

iv. ***The Subscriber, its ultimate beneficial owners and parties acting in concert with any of them***

Save for the entering into of the Subscription Agreement and the holding of 3,180,000 Existing Shares, none of the Subscriber, its ultimate beneficial owners and parties acting in concert with any of them has dealt in the Shares, outstanding options, derivatives, warrants or other securities convertible or exchangeable into the Shares during the Relevant Period. As at the Latest Practicable Date, the Subscriber, its ultimate beneficial owners and parties acting in concert with any of them do not hold any Shares or other securities of the Company.

v. ***Others***

During the Relevant Period:

i. none of the subsidiaries of the Company, nor any pension funds of the Company or of any of its subsidiaries, nor the Independent Financial Adviser nor any other advisers to the Company as specified in class (2) of the definition of "associate" under the Takeovers Code owned or controlled any Shares, convertible securities, warrants, options or derivatives of the Company.

ii. no person had any arrangement of the kind referred to in Note 8 to Rule 22 of the Takeovers Code with the Company or any person who is an associate of the Company by virtue of clauses (1), (2), (3) and (4) of the definition of associate under the Takeovers Code, and with the Subscriber, its ultimate beneficial owners or any party acting in concert with any of them.

iii. no shareholding in the Company was managed on a discretionary basis by fund managers connected with the Company.

(b) **Dealings in securities**

i. ***Directors***

None of the Directors or parties acting in concert with any of them had dealt in any Existing Shares, convertible securities, warrants, options or derivatives of the Company during the Relevant Period.

ii. ***Others***

During the Relevant Period, none of the subsidiaries of the Company, nor any pension fund of the Company or any of its subsidiaries, nor the Independent Financial Advisers nor any other advisers to the Company as specified in class (2) of the definition of "associate" under the Takeovers Code had dealt for value in any Existing Shares, convertible securities, warrants, options or derivatives of the Company.

During the Relevant Period, no fund managers who managed funds on a discretionary basis connected with the Company had dealt for value in any Shares, convertible securities, warrants, options and derivatives of the Company.

During the Relevant Period, none of the Company or the Directors has borrowed or lent any Existing Shares.

(c) **Interests and dealings in the Subscriber**

None of the Directors or the Company had any interest in the shares, convertible securities, options, warrants or derivatives of the Subscriber and none of them had dealt for value in any shares, convertible securities, options, warrants or derivatives of the Subscriber during the Relevant Period.

4. DIRECTORS' SERVICE CONTRACTS

Each of the executive Directors has entered into a service contract with the Company for initial fixed term of three years, and will continue thereafter for successive terms of one year until terminated by not less than three months' notice in writing served by either party on the other. Each of the executive Directors is entitled to a basic salary and director's fee subject to an annual review by the Board. In addition, the executive Directors are also entitled to a discretionary bonus, which may not exceed 3% of the audited consolidated net profit of the Group attributable to shareholders in respect of that financial year of the Company. The percentage rate of discretionary bonus is subject to annual review by the Board.

The independent non-executive Directors are appointed with specific terms inside the letter of appointment for initial fixed terms of two years.

As at the Latest Practicable Date:

(a) none of the Directors had entered or proposed to enter into a service contract with the Company or any of its subsidiaries or associated companies which is not determinable by the Company within one year without payment of compensation, other than statutory compensation;

(b) none of the Directors had entered into or amended any service contracts (including both continuous and fixed term contracts) with the Company or any of its subsidiaries or any of its associated companies within six months before the date of the Announcement;

(c) none of the Directors had any continuous service contracts with the Company or any of its subsidiaries or associated companies with a notice period of 12 months or more; and

(d) none of the Directors had any fixed term service contracts with the Company or any of its subsidiaries or associated companies with more than 12 months to run irrespective of the notice period.

5. DIRECTORS' COMPETING INTERESTS

As at the Latest Practicable Date, none of the Directors or the management shareholders of the Company and their respective associates (as defined under the Listing Rules) had any interest in a business which competes or may compete, directly or indirectly with the business of the Company.

6. NO MATERIAL LITIGATION

As at the Latest Practicable Date, neither the Company nor any of its subsidiaries was involved in any litigation or arbitration of material importance and no litigation or claim of material importance known to the Directors to be pending or threatened by or against the Company or any of its subsidiaries.

7. QUALIFICATION AND CONSENT OF EXPERT

The following is the name and qualification of the expert who has given opinion or advice which is contained in this circular:

Name	Qualification
Octal Capital Limited	a corporation licensed to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities under the SFO and the independent financial adviser to the Independent Board Committee and the Independent Shareholders in respect of, among other things, the Subscription Agreement and the Whitewash Waiver

As at the Latest Practicable Date, the expert named above was not beneficially interested in the share capital of any member of the Group nor did it have any right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for any Shares, convertible securities, warrants, options or derivatives which carry voting rights in any member of the Group nor did it have any interest, either direct or indirect, in any assets which have been acquired or disposed of by or leased to or are proposed to be acquired or disposed of by or leased to any member of the Group since 31 December 2013, being the date to which the latest published audited financial statements of the Group were made up.

The expert has given and has not withdrawn its written consent to the issue of this circular with the inclusion of its letter and/or references to its name in the form and context in which they respectively appear.

8. MATERIAL CONTRACTS

The following contracts have been entered into by the Group (not being contracts entered into in the ordinary course of business carried out or intended to be carried out by the Company or any of its subsidiaries) within the two years immediately preceding 31 July 2014 and up to the date of this circular, which are or may be material:

(a) the Subscription Agreement;

(b) the supplemental agreement dated 29 August 2014 to the Subscription Agreement;

(c) the Loan Agreement;

(d) the Placing Agreement; and

(e) the share charge dated 30 July 2014 entered into by Ko Yo Development Company Limited (the "**Chargor**"), a subsidiary of the Company, in favour of the Subscriber whereby the Chargor agreed to charge the 100% equity interest in Sichuan Ko Yo as security for the loan granted under the Loan Agreement.

9. MARKET PRICE

The table below sets forth the closing prices of the Existing Shares on the Stock Exchange (i) at the end of each of the six calendar months immediately preceding 31 July 2014 and ending on the Latest Practicable Date; (ii) on the Last Trading Day; and (iii) on the Latest Practicable Date:

Date	**Closing Price of the Existing Share** *HK$*
30 January 2014	0.093
28 February 2014	0.090
31 March 2014	0.079
30 April 2014	0.081
30 May 2014	0.071
30 June 2014	0.078
28 July 2014 (being the Last Trading Day)	0.110
31 July 2014	Trading suspended
29 August 2014	0.285
Latest Practicable Date	0.37

The lowest and highest closing market prices of the Shares recorded on the Stock Exchange during the Relevant Period were HK$0.07 on 15 May, 16 May, 21 May and 27 May 2014 and HK$0.44 on 18 August 2014, respectively.

10. MISCELLANEOUS

(a) The qualified accountant and the secretary of the Company is Mr. Chung Tin Ming, HKICPA, FCCA.

(b) The registered office of the Company is Cricket Square, Hutchins Drive, P.O. Box 2681, Grand Cayman KY1-1111, Cayman Islands.

(c) The head office and principal place of business of the Company in Hong Kong is Suite No. 02, 31st Floor, Sino Plaza, 255-257 Gloucester Road, Causeway Bay, Hong Kong.

(d) The registered office of the Subscriber is P.O. Box 957, Offshore Incorporation Centre, Road Town Tortola, British Virgin Islands.

(e) The share registrar of the Company in Hong Kong is Union Registrars Limited at 18th Floor, Fook Lee Commercial Centre, Town Place, 33 Lockhart Road, Wanchai, Hong Kong.

(f) The registered office of the Independent Financial Adviser is 801-805, Nan Fung Tower, 88 Connaught Road Central, Hong Kong.

(g) As at the Latest Practicable Date, the board of directors comprises seven executive directors, being Mr. Li Weiruo, Mr. Yuan Bai, Ms. Chi Chuan, Ms. Man Au Vivian, Mr. Li Shengdi, Mr. Li Feng and Mr. Li Ciping and four independent non-executive directors being, Mr. Hu Xiaoping, Mr. Woo Che-Wor, Alex, Mr. Qian Laizhong and Mr. Sun Tongchuan.

(h) As at the Latest Practicable Date, Mr. KM Cheng is the sole director of the Subscriber.

(i) As at the Latest Practicable Date, none of the Independent Shareholders had irrevocably committed themselves to vote for or against the Subscription and/or the Whitewash Waiver.

(j) Save and except Mr. Li's undertaking as referred to in the sub-section headed "Undertaking by Mr. Li" in the section headed "Letter from the Board" of this circular, there is no agreement, arrangement or understanding (including any compensation arrangement) between the Subscriber or any person acting in concert with it and any of the Directors, recent Directors, Shareholders and recent Shareholders having any connection with or dependence upon the outcome of the subscription of the New Shares and the Convertible Bonds and/or the Whitewash Waiver.

(k) There are no benefits to be given to any Directors as compensation for loss of office or otherwise in connection with the Subscription and the Whitewash Waiver.

(l) Save and except Mr. Li's undertaking as referred to in the sub-section headed "Undertaking by Mr. Li" in the section headed "Letter from the Board" of this circular, there is no agreement or arrangement between any Directors and any other person which is conditional on or dependent upon the outcome of the subscription of the New Shares and the Convertible Bonds and the Whitewash Waiver or otherwise connected therewith.

(m) The Subscriber, the Directors and any parties acting in concert with it have not borrowed or lent any relevant securities (as defined in note 4 to Rule 22 of the Takeovers Code) in the Company.

(n) There is no material contract entered into by the Subscriber in which any Director has a material personal interest.

(o) None of the Directors has any interest, direct or indirect, in any assets which had been, since 31 December 2013, being the date of the latest published audited consolidated financial statements of the Company were made up, acquired or disposed of by or leased to any member of the Group, or were proposed to be acquired or disposed of by or leased to any member of the Group.

(p) The Subscriber, Mr. Li and Mr. Yuan Bai and their respective concert parties will abstain from voting on the resolutions in relation to the Subscription Agreement, the transactions contemplated thereunder, the Specific Mandate and the Whitewash Waiver.

(q) There is no agreement, arrangement or understanding to transfer, charge or pledge any voting rights over the New Shares and the Conversion Shares.

(r) The English text of this circular and form of proxy shall prevail over the Chinese text in the case of inconsistency.

DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents are available for inspection (i) during normal business hours from 9:30 a.m. to 5:30 p.m. (other than Saturday, Sunday and public holidays) at the principal place of business of the Company in Hong Kong, (ii) on the website of the Company at *www.koyochem.com*, and (iii) on the website of the SFC at *www.sfc.hk* from the date of this circular up to and including the date of the EGM:

(a) the memorandum and articles of association of the Company;

(b) the memorandum and articles of association of the Subscriber;

(c) the material contract referred to in the section headed "Material Contract" in this appendix;

(d) the annual reports of the Company for the two years ended 31 December 2013;

(e) the letter of consent referred to in the section headed "Qualification and Consent of Expert" in this appendix;

(f) the letter from the Board, the text of which is set out on pages 8 to 28 of this circular;

(g) the letter from the Independent Board Committee, the text of which is set out on pages 29 to 30 of this circular;

(h) the letter from the Independent Financial Adviser, the text of which is set out on pages 31 to 65 of this circular; and

(i) a copy of this circular.

Ko Yo Chemical (Group) Limited
玖源化工(集團)有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 827)

NOTICE OF EXTRAORDINARY GENERAL MEETING

NOTICE IS HEREBY GIVEN THAT the extraordinary general meeting (the "**EGM**") of Ko Yo Chemical (Group) Limited (the "**Company**") will be held at 11:00 a.m. on Monday, 13 October 2014 at Suite No. 02, 31st Floor, Sino Plaza, 255-257 Gloucester Road, Causeway Bay, Hong Kong for the purpose of considering and, if thought fit, passing with or without amendment, the following resolutions of the Company:

ORDINARY RESOLUTIONS

1. "**THAT** the five (5) issued and unissued shares of HK$0.02 each in the share capital of the Company will be consolidated into one (1) share of HK$0.10 each (the "**Consolidated Shares**") (the "**Share Consolidation**"). The board of directors of the Company (the "**Board**") shall at its absolute discretion sell any aggregated fractional Consolidated Shares arising upon the Share Consolidation at any time within one month from the effective date of the Share Consolidation, being 14 October 2014 and on such terms as it considers appropriate."

2. "**THAT** conditional and immediately up the Share Consolidation becoming effective, the board lot size for trading in the Consolidated Shares be changed to 4,000 Consolidated Shares."

3. "**THAT** the authorised share capital of the Company be increased from HK$400,000,000 divided into 4,000,000,000 shares of par value HK$0.10 each to HK$800,000,000 divided into 8,000,000,000 shares of par value HK$0.1 each by the creation of an additional 4,000,000,000 shares of par value HK$0.10 each."

4. "**THAT:**

   (a) the subscription agreement (the "**Subscription Agreement**") dated 30 July 2014 (as supplemented by a supplemental agreement dated 29 August 2014) entered into between the Company and Asia Pacific Resources Development Investment Limited (the "**Subscriber**") pursuant to which the Company will allot and issue to the Subscriber (a) 800,000,000 new shares of HK$0.10 each (the "**New Shares**") at HK$0.32 per New Share; and (b) the 7% coupon convertible bonds due 2024 (the "**Convertible Bonds**") in an aggregate principal amount of HK$832,000,000 (the principal terms of which are set out in the circular of the

Company dated 22 September 2014 (the "**Circular**"), and a copy of which having been produced to this meeting and marked "**A**" and initialed by the chairman of this meeting for the purpose of identification), and the transaction contemplated thereby be and hereby approved, confirmed and ratified;

(b) the allotment and issue of the New Shares and the Convertible Bonds to the Subscriber pursuant to the terms of the Subscription Agreement be and hereby approved;

(c) the directors of the Company be and are hereby granted a specific mandate to exercise all the powers of the Company to allot and issue up to 2,600,000,000 new shares of HK$0.10 each (or such greater number as may be required to be issued as a result of an adjustment to the conversion price as provided for in accordance with the terms of the terms and conditions of the Convertible Bonds) in the capital of the Company as may be required to be allotted and issued upon exercise of the conversion rights attaching to the Convertible Bonds, subject to and in accordance with the terms and conditions set out in the Subscription Agreement and the Convertible Bonds; and

(d) any one or more directors of the Company be and hereby authorised to allot and issue the New Shares and the Convertible Bonds in accordance with the terms of the Subscription Agreement and to do all such acts and things as they consider necessary or expedient for the purpose of giving effect to the Subscription Agreement and completing the transactions contemplated thereby."

5. "**THAT** subject to the granting of the whitewash waiver by the Executive Director of the Corporate Finance Division of the Securities and Futures Commission of Hong Kong and any delegate of such Executive Director pursuant to Note 1 on dispensations from Rule 26 of the Hong Kong Code on Takeovers and Mergers in respect of the obligation on the part of the Subscriber and parties acting in concert with it to make a mandatory general offer to the shareholders of the Company for all issued Shares not already owned by the Subscriber or parties acting in concert with it under Rule 26 of the Hong Kong Code on Takeovers and Mergers as a result of the allotment and issue of the New Shares and the new Consolidated Shares which may fall to be allotted and issued upon exercise of the conversion rights attaching to the Convertible Bonds, such whitewash waiver be and is hereby approved."

By Order of the Board
Ko Yo Chemical (Group) Limited
Li Wei Ruo
Chairman

Hong Kong, 22 September 2014

Registered office:-
Cricket Square
Hutchins Drive
P.O. Box 2681
Grand Cayman KY1-1111
Cayman Islands

Principal place of business in Hong Kong:-
Suite No. 02, 31st Floor, Sino Plaza
255—257 Gloucester Road
Causeway Bay
Hong Kong

Notes:

1. Any shareholder entitled to attend and vote at the meeting is entitled to appoint one or, if he is holder of more than one share, more proxies to attend and vote instead of him. A proxy need not be a shareholder of the Company.

2. In order to be valid, a form of proxy in the prescribed form together with the power of attorney or other authority (if any) under which it is signed must be deposited at the branch share registrar of the Company, Union Registrars Limited, 18th Floor, Fook Lee Commercial Centre, Town Place, 33 Lockhart Road, Wanchai, Hong Kong not less than 48 hours before the time appointed for holding the meeting (or any adjournment thereof).

3. The instrument appointing a proxy shall be in writing under the hand of the appointor or of his attorney duly authorised in writing or, if the appointor is a corporation, either under its common seal or under the hand of an officer or attorney or other person duly authorised.

4. Delivery of the form of proxy will not preclude a member from attending and voting in person at the meeting convened and in such event, the form of proxy shall be deemed to be revoked.