



上海復旦微電子集團股份有限公司
Shanghai Fudan Microelectronics Group Company Limited*
(a joint stock limited company incorporated in the People's Republic of China)
(Stock Code: 1385)



2016
ANNUAL REPORT



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Chairman's Statement

On behalf of the board of directors (the "Board") of Shanghai Fudan Microelectronics Group Company Limited (the "Company"), I am pleased to present the annual report of the Company and its subsidiaries (the "Group") for the year ended 31 December 2016.

During the year under review, the world economic growth has different paces in various countries, the U.S. economy growth rate was significantly higher; the Europe economy was growing slow due to geopolitical threats; and China was facing economic pressure due to overcapacity in some of its industries. Since the electronics industry in China has fallen far behind the other well developed countries, following implementation of reform, adopting opening policy and the recent rapid economic growth of China, the continuous growth of the electronics industry could be further sustained with the vigorous support by the government policy. Despite the facing of challenges of slowdown in national consumption and export rates, the electronics industry could still maintain a steady annual growth during the year under review.

For the year ended 31 December 2016, the Group recorded a revenue growth of 14.2%, both the revenue of the sales of IC products and the IC testing services have recorded a similar growth. The gross margin of this year has slightly increased to 53.2%. The Company had participated in more government projects this year than before; therefore, the profit for the year has increased by 34.9% and the earnings per share attributable to owners of the parent increased from RMB25.74 cents of last year to RMB34.38 cents. Having considered that more resources will be required for research and development projects in the coming year, the Board does not recommend the payment of final dividend in respect of the year.

The Group has over ten years of stable development, its finance position is getting more strengthen and with focus on core business, its products are well diversified to cover most of the IC application scopes. The major products like city one-cards, financial IC cards, social security and citizen cards, smart meters, electronics payment etc., have already gained considerable market shares and in leading positions in the market. During the year, the Group has achieved satisfactory sales performances in certain product series as well as the IC testing services.

Looking into 2017, the United States will enter into the rate hike cycle and the fiscal policy will boost the economic growth. Eurozone and Asian emerging markets are still suffering from geopolitics; thus, the economies are expected to have slightly increases. The growth of China's economy is expected to slow down as it is adversely affected by factors like adjustments in industrial structure. Products of the Group are well diversified, covering from basic living needs and consumption to high-end government projects. The Group believes focusing in the core business not only can gain advantages in competition, also the upcoming development in other aspects will gain long-term benefits. Marketing strategy has been focusing on the development of social and people's livelihood consumption products with commitments to meet consumer needs. With aggressive attitude in technology researches, more resources will be put into different applications in order to expedite the business development. Due to the fact that the businesses of the Group are concentrated in the domestic market, its products are focusing on basic living needs, and with the participation in various government projects for years, the Board expected its stable income can confront with economic slowdown and remains optimistic for a healthy growth in the Group's business in the year to come.

Taking this opportunity, the Board wishes to thank the management and all staff of the Group for their relentless efforts and dedication, and extend its gratitude to the Company's shareholders and business partners for their valuable support and trust.

Jiang Guoxing
Chairman

Shanghai, the PRC, 28 March 2017

Management Discussion and Analysis

BUSINESS REVIEW

Focusing on its core business and with products under diversified development, the Group is enabled to maintain a favourable position in the market competition, especially in the business environment of ever-changing technologies and with consumer preference in taking the new. The Group's overall revenue recorded approximately RMB1,187,490,000, increased by 14.2% compared to the previous year. Profit margins of certain products decreased due to price reductions against keen competition; however, due to products with higher gross margin have gained more portfolio weight and some products have reductions in production costs following enlarged market shares; thus, the overall gross margin increased slightly from 52.9% of last year to 53.2%.

The Group's business performance by product category during the year is as follows:

Security and Identification IC Chips

In the year ended 31 December 2016, sales of security and identification chips only recorded a growth of around 7% with gross margin decreased by 5.3% compared to last year; its sales still accounted for more than half of the Group's total turnover and taking up a relatively high weighting. The security and identification products include high-end products like public transit cards, resident cards, social security cards, citizen cards, financial IC cards, and electronic payments etc. Due to the high technical threshold and the Group has already entered the industry in a rather early stage, the sales was not affected by competition and has maintained a very steady growth. However, due to the start of keen competition, the prices and the sales of products with lower technical skills such as campus cards, consumer cards, access control systems and low memory public transit cards were greatly affected; moreover, the gradual market saturation has caused price deduction and decrease in sales, which have a negative impact on the gross profit margin. The sales of security chips has decreased by 13.7% due to market change in its applications. Other products such as contactless RF card chip and contactless chips have benefited from the weakened competition, thus, having satisfactory increases in sales.

Smart Meter ASIC Chips

The sales of the smart meter ASIC chips has decreased by 4.2% as compared to last year. As a result of falling behind in technology and having comparatively high production costs, the old products suffered from substantial decrease in the win rate from bidding and have entered the end of their product life cycle, and the sales of this year has decreased by 53%. Since the release of the follow-up products from last year, further improved version has been released during the year; because the new version fulfills the technical specifications and functional requirements, the rate of winning bids has significantly increased and gained around 50% of the market share. The gross margin of this product has a slightly increase due to the better profit generated from the new products.

Non-volatile Memory Chips

The products of this category mainly comprises the EEPROM series and the NOR flash memory series, they are widely applied in consumer class and peripheral electronic products market. The Group's EEPROM and NOR flash memory products cover different memory storages together with remarkably high reliability; due to market expansion, the sales has increased by 47.2%. Since the old products were replaced by the new ones, the gross margin benefited from technical upgrade with lower production costs and increased by 17%.

Management Discussion and Analysis

BUSINESS REVIEW *(continued)*

Specific Analog Circuits

Specific Analog Circuits mainly consist of leakage protection chips, motor vehicle specific chips, communication chips and lighting chips; they are widely applied in leakage protection devices, home appliances, telecommunication equipment and lighting control system etc. The sales of these products has increased by approximately 11.3% during the year, but the gross margin has decreased by around 1.9%; the reason behind was an increase in market share of leakage protection chips, however, gross margin was adversely affected by price deduction due to change in market condition. This type of products contributes only a small portion in the total sales and it does not have a material impact on the Group's performance.

Other Chips

Due to satisfactory performance in the trial stage and benefited from the increasing market demand, the sales of specific proprietary products has increased by approximately 114.9%. As a result of special specifications that required extremely high technological skills and the substantial research and development expenses incurred during the developing stage, the gross margin of these products is higher than other products and has a good contribution to the overall gross margin of the Group.

IC Testing Services

During the year, the IC testing services provided to external customers have achieved a growth of approximately 24.1%. The IC market has continued to grow rapidly which helped the growth of the Group's IC testing services. Moreover, other than adding testing equipment in order to expand the capacity of testing services, this business segment has paid more attention on the research and development of high-end testing platform. The internal transactions on testing services have decreased to about one-third of this segment revenue. Gross margin of IC testing services decreased by 22.9% compared to last year due to price drop for expanding market share and increase in depreciation as a result of equipment expansion.

FINANCE REVIEW

For the year ended 31 December 2016, the Group recorded a total revenue of approximately RMB1,187,490,000 (2015: RMB1,039,725,000), has increased by 14.2% as compared to last year; gross margin has kept at the 50% level and slightly increased over the last year to 53.2%. In addition, substantial increase in other income and gains has neutralized the increases in operating and research and development expenses; thus, this year's profit was RMB240,090,000 (2015: RMB177,990,000) and has increased by 34.9%. The audited net profit attributable to owners of the parent was approximately RMB212,258,000 (2015: RMB158,898,000), with basic earnings per share of RMB34.38 cents (2015: RMB25.74 cents), representing an increase of approximately 33.6% year-on-year. The Board does not recommend the payment of final dividend in respect of the year ended 31 December 2016 (2015: nil).

For the year ended 31 December 2016, the Group recorded an overall sales growth due to both increases in sales of IC chips and IC testing services income. The gross margin was close to last year's and slightly increased from 52.9% to 53.2%. Other income and gains substantially increased by approximately 96.2% compared with last year, or an increased earnings of approximately RMB79,905,000 caused by the conditions or contingencies related to more government grants being fulfilled, provision of external research and development services, and bank interest income increased as a result of timely collection of trade debts.

Management Discussion and Analysis

FINANCE REVIEW *(continued)*

The sales and distribution expenses have increased by approximately 10.6% as a result of the increases in sales and marketing activities during the year. Administrative expenses have increased by approximately 8.3%, this is because of the increase in staff members to overcome business expansion and adjustment in salary affected by the industry level. Other expenses during the year has increased by approximately RMB81,094,000 or 27.2% as compared to last year; as a result of substantial resources applied to research and development projects in recent years, research and development costs as well as written off, impairment and amortisation provided on intangible assets during the year have increased significantly.

With reference to income tax expense, the Group's tax expense for the year increased by approximately RMB4,432,000 over the year and the tax expense provided mainly due to the increased profit before tax amounted to approximately RMB6,458,000. The Company was qualified under "key software enterprise falling within the State's planned arrangement" in its 2015 annual tax return; thus, enjoyed a preferential tax rate of 10%. The adjustment of tax overprovision for prior year has partly set-off the tax expense due to increase in profit.

The Group's non-current assets decreased by approximately RMB39,699,000 over last year, it is because the amount of acquisition of property, plant and equipment was less than the depreciation; in addition, the additions in deferred development costs of intangible assets during the year amounted to approximately RMB72,822,000, which was less than the total of written off, impairment and amortisation provided in respect of the intangible assets of approximately RMB93,920,000; the deferred tax assets has increased by RMB4,708,000. Current assets increased substantially by approximately RMB324,104,000 than last year, where inventories has greatly increased by RMB66,502,000 in order to cope with increasing seasonal sales. Balance of trade and bills receivables was approximately RMB466,616,000, increased by approximately RMB100,599,000 as compared with last year, it was mainly attributable to the increasing sales in the fourth quarter of the year, and most of them are within the normal credit period. Cash and bank deposits increased by approximately RMB154,191,000 than last year due to timely collection of payments. Due to increase in tax and other payables, current liabilities has increased by RMB17,219,000 as compared to last year. Non-current liabilities has increased by RMB6,340,000 due to increase in deferred income.

Equity of non-controlling interests has increased by RMB40,910,000 or 36.6%, this is because the IC testing services provided by the 50.3%-owned Sino IC Technology Co., Ltd. ("Sino IC") has achieved a good performance and attributed more profit to the non-controlling interests.

MATERIAL INVESTMENTS AND ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES

Shanghai Fukong Hualong Micro-system Technology Co., Ltd. ("Fukong Hualong"), which is a non wholly-owned subsidiary of the Group, entered into an agreement to issue new shares and the transaction contemplated under the agreement was deemed as a disposal under the Listing Rules. Upon completion of the share allotment, the Company's equity holding in Fukong Hualong was decreased from 51% to 38.25%. The new equity holder, which holds a 25% equity interest in Fukong Hualong, has agreed to act in concert with the Company over Fukong Hualong's operating, investing and financial decisions. The Directors consider that Fukong Hualong is under the unilateral control of the Group and regarded as a subsidiary of the Company which is consolidated in the Group's financial statements.

Other than above mentioned, the Group had no material investment and there was no acquisition and disposal of subsidiaries during the year.

Management Discussion and Analysis

FUTURE PLANS FOR MATERIAL INVESTMENTS

The Group will focus on its core business development and has no material investment plan at present.

FINANCIAL RESOURCES AND LIQUIDITY

As at 31 December 2016, net assets of the Group amounted to approximately RMB1,374,432,000 (2015: RMB1,113,586,000), an increase of approximately 23.4% over the year; of which current assets amounted to approximately RMB1,311,647,000 (2015: RMB987,543,000), a rise of approximately 32.8% year-on-year, and including cash and bank deposits of approximately RMB540,224,000 (2015: RMB386,033,000), an increase of approximately 39.9% over last year.

As the Group keeps profiting for the past years, profit and internal cash generated have been used to meet the operations and business development needs.

The net cash flows from operating activities for the year was approximately RMB249,660,000 (2015: RMB199,610,000), increased by approximately RMB50,050,000. The net cash flows used in investing activities was approximately RMB105,249,000, a decrease of RMB134,760,000 over the previous year. Besides, deposits with maturity over 3 months decreased by approximately RMB10,860,000, the cash and cash equivalents as at the reporting date was increased by RMB165,051,000.

As at 31 December 2016, the Group has not pledged any of its assets to any third parties (2015: nil).

CAPITAL STRUCTURE

The Company's capital structure has no change during the year and only comprises of ordinary shares.

In 2016, Sino IC, a non wholly-owned subsidiary, increased its share capital from 84,000,000 shares to 126,000,000 shares by transferring RMB42,000,000 out of the retained earnings to the share capital.

During the year, Fukong Hualong entered into an agreement for the allotment of 10,000,000 new shares and increased its share capital from 30,000,000 shares to 40,000,000 shares.

GEARING RATIO

As at 31 December 2016, the Group's current liabilities amounted to approximately RMB416,358,000 (2015: RMB399,139,000), an increase of approximately 4.3% year-on-year. Non-current liabilities amounted to approximately RMB12,078,000 (2015: RMB5,738,000), an increase of approximately 110.5% over the year. Net asset value per share was approximately RMB2.23 (2015: RMB1.80), a growth of approximately 23.4% over last year. The Group's ratio of current liabilities over current assets was approximately 31.7% (2015: 40.4%) and the gearing ratio was approximately 31.2% (2015: 36.4%) on the basis of total liabilities over net assets.

As at 31 December 2016, the Company and the Group had no bank or other borrowings (2015: nil).

PRINCIPAL RISKS AND UNCERTAINTIES

The Directors believe that developing and implementing rigorous risk management practices can efficiently and effectively reduce operational risks. The Board has delegated the responsibilities to relevant departments and will monitor, review and improve the practices from time to time.

Management Discussion and Analysis

PRINCIPAL RISKS AND UNCERTAINTIES *(continued)*

The Directors believe that the Group is not exposed to risks associated with business regulations in view that there is no specific legislative control over the design, development and sales of integrated circuit where Group focuses its business on at present, and national policies are all advantageous to the development of the industry. In addition, the Group's business maintained a stable and healthy growth over the years. With the Group's existing customers and suppliers are all long-term partners, and business of the industry is still in the growth phase driven by national policies and huge market demands in most of its products, the Directors believe there will be no uncertainties.

FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments comprise cash and short term time deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as trade and bills receivables, deposits and other receivables, trade and bills payables and accruals and other payables, which arise directly from its operations.

It is, and has been, throughout the year under review, the Group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are foreign currency risk, credit risk and liquidity risk.

Interest and Foreign Exchange Risk

The Directors believe that the Group is not exposed to any material interest rate risk in view that the Group does not have any debt obligations that are subject to fluctuations in market interest rates.

The Group has transactional currency exposures. Such exposures arise from sales or purchases by operating units in currencies other than the units' functional currency. Approximately 6% (2015: 8%) of the Group's sales are denominated in currencies other than the functional currency of the operating units making the sale, whilst almost 61% (2015: 70%) of costs are denominated in the units' functional currency. The Group keeps monetary items in foreign currencies at a certain level in order to meet the needs of purchases that are denominated in foreign currencies. It is the Group's policy not to enter into forward contracts until a firm commitment is in place. During the reporting period, the fluctuations in foreign exchange had no material influence on the Group's operations and cash flows.

Credit Risk

The Group trades only with recognised and creditworthy third parties and, therefore, no collaterals are required. At the end of the reporting period, the Group has certain concentrations of credit risk as the Group's sales are made to several major customers. 27% (2015: 27%) of the Group's total trade and bills receivables were due from the Group's five largest customers. The Group seeks to maintain strict control over its outstanding receivables and closely monitors the collection of receivables to minimise credit risk.

The credit risk of the Group's other financial assets, which comprise cash and cash equivalents, deposits and other receivables, arises from default of the counterparty, and the maximum exposure is limited to the carrying amount of these instruments.

Liquidity Risk

The Group monitors its risk to a shortage of funds using a recurring liquidity planning tool. This tool considers the maturity of both its financial instruments and financial assets (e.g., trade and bills receivables) and projected cash flows from operations.

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of normal business credit terms obtained from various creditors.

Management Discussion and Analysis

CAPITAL COMMITMENTS

As at 31 December 2016, the Group had capital commitments contracted but not provided for in the amount of approximately RMB7,637,000 (2015: RMB15,950,000), which were related to the acquisition of property, plant and equipment.

CONTINGENT LIABILITIES

As at 31 December 2016, the Group had no contingent liabilities (2015: nil).

USE OF CAPITAL AND FUNDING

The Group has sufficient working capital and a stable financial position, which will be applied to the research and development of new products and the identification of cooperation opportunities.

EMPLOYEES

As at 31 December 2016, the Group has approximately 1,040 (2015: 958) employees. The increase in the number of employees was due to recruitments to meet increasing research and development projects, and this division engages more than half of the total employees. The remuneration of employees was determined in accordance with their performance, qualifications, experience and contribution to the Group with reference to the latest market trend in the industry.

As at 31 December 2016, the employee benefit expense (including directors' remuneration) as recorded in the consolidated statement of profit or loss and comprehensive income was RMB203,670,000 (2015: RMB164,256,000). The significant increase in employee benefit expense was due to the rise in number of employees and adjustment of salaries to concur with the industry's salary level; in addition, due to the expansion of research and development projects, the employee benefit expense of RMB55,601,000 (2015: RMB58,072,000) was capitalized as development costs during the year.

COMPLIANCE WITH LAWS AND REGULATIONS

The Directors deem the compliance with laws and regulations as the cornerstone of a business and attach considerable importance to it. The Group strictly complies with relevant laws and regulations of each country and region where the subsidiary companies perform business activities. Furthermore, as the H shares of the Company are listed on the main board of Stock Exchange of Hong Kong Limited ("SEHK"), the Company shall be bound by the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and the Securities and Futures Ordinance on Chapter 571 of the Laws of Hong Kong. The Group's operating business is not subjected to any specific regulation at the time being.

Management Discussion and Analysis

RELATIONSHIP WITH EMPLOYEES, CUSTOMERS AND SUPPLIERS

The Group provides in service training, technological exchange, series of lectures and group study to staff members and management team; this can deepen their understanding on technological development and the industry's trend, strengthen their professional skills and knowledge, in order to help with the long-term development of the business. Besides, the Group provides suitable employees benefits, arranges regular health checkups, participates in social events, recreational activities and competitions, in favor of the staff's healthy living and their sense of belonging to the Company.

The Group's employee remuneration package is determined with reference to industry standards and individual qualifications and performance. The Group will conduct annual assessment regarding the performance and skill development of employees to adjust salaries and bonuses and develop incentive programs.

Understanding that customer is the key factor for generating revenue and business development, the Group actively maintains close and long term partnerships with customers. With more than ten years of business experience and expertise, the Group strives to fulfill the requirements of customers. The Group has currently one customer whose income arising from transactions accounted for 10% or more of the Group's total revenue. The Group's five largest customers include manufacturers of security IC chips and agents of smart meters ASIC chips, all of which are government authorities and renowned enterprise in the industry with business relationship with the Group for 5 to 10 years. 2 of these customers are trade with 90 days credit, which is the same credit term given by the Group to other customers and the other 3 customers are traded on the payment to delivery basis. As at 31 December 2016, the above-mentioned 2 customers have no record of overdue payment nor doubtful debt provision. In accordance with the risk management policies adopted by the Group, its customers and products are managed in well-balanced portfolios, there is no exposure on heavy reliance on individual products nor these major customers' orders.

The Group sees the suppliers as valued business partners, and is committed to maintain long term relationships with them and protect interests of both sides to ensure reasonable prices and stable supply of the Group. The Group does not rely on any main supplier that might lead to a significant impact on the operation.

Corporate Information

BOARD OF DIRECTORS

Executive Directors

Mr. Jiang Guoxing (*Chairman*)
Mr. Shi Lei (*Managing Director*)
Mr. Yu Jun (*Deputy Managing Director*)
Ms. Cheng Junxia

Non-executive Directors

Ms. Zhang Qianling
Mr. Ma Zhicheng
Mr. Yao Fuli
Ms. Zhang Huajing

Independent Non-executive Directors

Mr. Cheung Wing Keung *FCCA, CPA*
Mr. Guo Li
Mr. Chen Baoying
Mr. Lin Fujiang

COMPANY SECRETARY

Mr. Li Wing Sum, Steven *FCCA, FCPA, FTIHK*

AUTHORISED REPRESENTATIVES

Mr. Shi Lei
Mr. Li Wing Sum, Steven

AUDIT COMMITTEE

Mr. Cheung Wing Keung (*Chairman*)
Mr. Guo Li
Mr. Lin Fujiang

NOMINATION COMMITTEE

Mr. Cheung Wing Keung (*Chairman*)
Mr. Guo Li
Ms. Cheng Junxia

REMUNERATION COMMITTEE

Mr. Cheung Wing Keung (*Chairman*)
Mr. Guo Li
Ms. Cheng Junxia

SUPERVISORS' COMMITTEE

Mr. Li Wei
Mr. Wei Ran
Mr. Xu Zhihan

AUDITORS

Ernst & Young
Certified Public Accountants

REGISTERED OFFICE

No. 220, Handan Road
Shanghai
People's Republic of China

PLACE OF BUSINESS IN HONG KONG

Flat 6, 5/F., East Ocean Centre
98 Granville Road, Tsimshatsui East
Kowloon, Hong Kong

SHARE REGISTRAR AND TRANSFER OFFICE

Tricor Tengis Limited
Level 22, Hopewell Centre
183 Queen's Road East
Wanchai, Hong Kong

PRINCIPAL BANKERS

Industrial and Commercial Bank of China Shanghai branch

China Everbright Bank Co., Ltd.
Shanghai branch

STOCK CODE

1385

Directors and Senior Management Biographies

Biographical details of the directors and the senior management of the Company are set out below:

DIRECTORS

Executive directors

Mr. Jiang Guoxing, aged 63, joined the Company in July 1998, is the Chairman of the Company. Mr. Jiang is a professor grade senior engineer and graduated with a degree in Computer Science from the Fudan University. He is also the vice chairman and general manager of Shanghai Fudan Forward Science and Technology Co., Limited, a company listed on the Shanghai Stock Exchange. He was the supervisor of Industrialisation and Properties Management Office of Fudan University and the non-executive director of Shanghai Fudan-Zhangjiang Bio-Pharmaceutical Co., Ltd., a company listed on the main board of the Stock Exchange.

Mr. Shi Lei, aged 50, joined the Company in July 1998, is the Managing Director of the Company. He is a professor grade senior engineer and was graduated with a Bachelor degree in management from the University of Science and Technology of China (the “USTC”) and a Master degree in management from the Fudan University. Mr. Shi was the deputy manager in the Development Division of Shanghai Agricultural Investments Company and the general manager of Shanghai Pacific Commercial Trust Company Limited.

Mr. Yu Jun, aged 49, joined the Company in July 1998, is the Deputy Managing Director of the Company and a director respectively of the Company’s subsidiaries namely, Shanghai Doublepoint Information Technology Co., Ltd., Shanghai Fukong Hualong Micro-system Technology Co., Ltd. (“Fukong Hualong”) and Sino IC Technology Co., Ltd. (“Sino IC”) He graduated with a Bachelor’s degree in Electronics Engineering and a Master’s degree in Electronics and Information Systems from the Fudan University and is a senior engineer. Mr. Yu was the deputy director and tutor of the Research Institute for Integrated Circuit Designs of the Fudan University as well as the chief engineer of Shanghai Fudan High Tech Company and has extensive knowledge and experience in the design of integrated circuits and systems.

Ms. Cheng Junxia, aged 70, joined the Company in July 1998, is the Chief Engineer of the Company and a director of the Company’s subsidiary namely, Shanghai Fudan Microelectronics (Hong Kong) Limited (“Fudan Hong Kong”). She is also a member of the remuneration committee and the nomination committee. She graduated with a degree in Physics from the Fudan University. She was a professor and a director of the Research Institute for Integrated Circuit Designs of the Fudan University and the general manager of Shanghai Fudan High Tech Company. She has extensive knowledge and experience in the design and manufacture of integrated circuits.

Non-executive directors

Ms. Zhang Qianling, aged 80, joined the Company in July 1998. She was the supervisor of Sino IC She was graduated from the Department of Physics of Fudan University and was a principal professor and tutor to doctorate students at Fudan University. She was a promoter and first director of the ASIC and System State Key Laboratory of the Fudan University and was a director of Shanghai Huahong Integrated Circuit Co. Ltd.

Mr. Ma Zhicheng, aged 56, joined the Company in July 2015, is a qualified senior operating manager. He was awarded the post-graduate degree of Business Administration from the Shanghai Academy of Social Sciences. He is the Deputy General Manager of Shanghai Commerce and Invest (Group) Corporation (“SCI”), which is one of the substantial shareholders of the Company. He is also the Managing Director of Shanghai Fudan Technology Enterprise Holdings Limited, a subsidiary of SCI. Mr. Ma is the Chairman of Shanghai Fudan Digi-medical Technology Co., Ltd. He was the Assistant General Manager of SCI, the General Manager of Shanghai Commercial Investment Venture Capital Co., Ltd., the Chairman of Shanghai Hualong Information Technology Development Center, the Deputy General Manager of Shanghai Xinlian Real Estates Co. and the Office Manager of Shanghai Aeronautic Machinery Co.

Directors and Senior Management Biographies

DIRECTORS *(continued)*

Non-executive directors *(continued)*

Mr. Yao Fuli, aged 42, joined the Company in July 2015. He was awarded Bachelor Degree and Master Degree of Business Administration from Fudan University. He is the General Manager of Shanghai Cyber Galaxy Investment Co., Limited. Mr. Yao was the Deputy General Manager of SCI and Managing Director of Shanghai Commercial Investment Venture Capital Co., Ltd, the Chairman of Shanghai Aijian Capital Management Co., Ltd., the Deputy General Manager of Shanghai Aijian Trustees Co., Ltd. and the Asset Management Manager of Shanghai Aijian Corporation as well as a member of its General Manager Council and Management Committee.

Ms. Zhang Huajing, aged 56, joined the Company in July 2015. She was awarded a Bachelor Degree from Shanghai University of Finance and Economics and is a senior accountant. She is the Deputy Chief Accountant and Finance Manager of SCI. Ms. Zhang was the Assistant Manager of Finance Department and Audit Director of SCI. She was also the Chief Accountant of Yangtze River Economic United Development (Group) Co., Ltd. She was the Chief Accountant of Finance Department of Changfa Group Shanghai Trading and Industrial Holding Co.

Independent non-executive directors

Mr. Cheung Wing Keung, aged 52, joined the Company in May 2004 and is also a member of the audit committee, the remuneration committee and nomination committee of the Company. He is a fellow member of the Association of Chartered Certified Accountants and an associate member of the Hong Kong Institute of Certified Public Accountants. He has over 25 years' working experience in auditing, accounting, taxation, corporate management and consultancy. He has worked in accounting firms and the Hong Kong Inland Revenue Department and has held senior positions in certain Hong Kong's private group companies.

Mr. Guo Li, aged 70, joined the Company in May 2006 and is a member of the audit committee, the remuneration committee and the nomination committee of the Company. He graduated from the Department of Radio Electronics from the USTC and is a professor and doctoral supervisor as well as a senior member of China Electronics Academy and a member of China Image and Graphics Academy. He was the director of the Academic Committee of Department of Science and Technology in the University of Science and Technology of China as well as its Laboratory of Circuit and System. He has been carrying the researches in digital signal processing, digital image processing and IC design etc. and was a visiting scholar in the Department of Computer in the University of Notre Dome of the United States.

Mr. Chen Baoying, aged 87, joined the Company in October 2007, is a part-time professor of Nankai University. He graduated with a Bachelor degree of Trade Finance in the Nankai University and a Master degree in Renmin University of China in Foreign Trade and Economic Development. He has around 40 years working experience in research of international trade and finance. He was the researcher of the Institute of International Trade of the Ministry of Foreign Trade and Economic Cooperation, the PRC, which he worked for 30 years. He was the vice director of the Hong Kong and Macao Research Centre of the Hong Kong and Macao Affairs Office of the State Council since 1986 and retired in 1995, and was primarily responsible for research of economic and finance in these areas. He was appointed member respectively of the Join Working Group of the Mainland and Hong Kong Securities Affairs and the Expert Group on Commodities of the China Securities Regulatory Commission. He was an independent non-executive director of China National Resources Development Holdings Limited, a company listed on the main board of the Stock Exchange.

Directors and Senior Management Biographies

DIRECTORS *(continued)*

Independent non-executive directors *(continued)*

Mr. Lin Fujiang, aged 58, joined the Company in December 2012, is a member of the audit committee. He is currently a professor of the School of Information Science and Technology and an executive director of the Micro-Nano-Electronics System Integration Centre of the USTC. He graduated with degrees of Bachelor and Master in Electronic Engineering and Technology from the USTC and a Doctorate degree in Electrical and Electronic Engineering from the University of Kassel, Germany. Mr. Lin was a national special recruited expert selected under the “One Thousand Talents Plan” in 2009 and has been engaged for a long-term multidisciplinary research of microwave and microelectronics, especially with a series of achievements in advanced radio frequency semi-conductors and circuit integration modeling and simulation, and is also a renowned practical radio frequency modeling expert. He has presented more than a hundred fifty scholarly essays in subscriptions, magazines and conferences and holds several intellectual rights in electronic technology jointly with some famous scholars, and is a well-known scholar in electronics science and technology.

SUPERVISORS

Mr. Li Wei, aged 45, joined the Company in July 1998, is the Technical Officer of the Company and the general manager of Fukong Hualong. He has a Master degree in Semiconductor Physics and Physics of Semiconductor Devices granted by the Department of Electronic Engineering of the Fudan University. Mr. Li is an expert in IC design and has conducted in-depth researches on the mobile payment and satellite navigation system.

Mr. Wei Ran, aged 61, joined the Company in May 2009, holds a master degree and is a senior economist. He is the general manager of SCI and chairman of Shanghai Commercial Investment Enterprise Limited. He was the assistant to general manager and the deputy general manager of SCI. He has substantial experience in corporate merger, restructuring, investment and financing.

Mr. Xu Zhihan, aged 53, joined the Company in October 2015. He is a certified public accountant of the PRC and graduated from School of Management of Fudan University in 1985 with a Bachelor Degree. He was also awarded the Doctor designation from the Faculty of Business Management in Accountancy of Fudan University in 2007. Mr. Xu was the speaker, associate professor and associate director of School of Management of Fudan University. He is currently the associate professor of accountancy in School of Management of Fudan University.

SENIOR MANAGEMENT

Mr. Li Wei, (see personal details set out in the paragraph headed “Supervisors” above).

Mr. Shi Jin, aged 60, joined the Company in October 1999 until March 2002 and re-joined the Company in March 2007. He is the Deputy General Manager of the Company and the chairman of Sino IC. He holds a Master’s degree in business administration and is an assistant research fellow. He was previously the director of the Research Institute of Shanghai Planning Commission, the general manager of Shanghai Industrial Investment Consultation Company, the chairman of Shanghai Industrial Investment Finance and Management Company, the deputy head of the Economics Department of Shanghai Municipal Research Institute and the chief executive of Tian You High Technology Enterprise Investment Ltd.

Ms. Ji Lanhua, aged 66, joined the Company in July 1998 and is the Deputy General Manager of the Company and a director of Sino IC. She holds a Bachelor degree and was previously the sales manager of Fudan High Tech Company. She had engaged in the design and development of the Company’s motorcycle ignition controller circuits and telephone transmission circuits. Ms. Ji is very experienced in the design and sales of IC chips.

Directors and Senior Management Biographies

SENIOR MANAGEMENT *(continued)*

Mr. Da Zhongdong, aged 48, joined the Company in June 2001 and is the Deputy General Manager of the Company and chairman of Fukong Hualong. He holds a Bachelor degree and is a researcher in microelectronics and chief engineer. He had worked for China Academy of Space Technology. He once was the manager of the design department of the Company. He has substantial experience in IC design and specific application management.

Mr. Diao Linshan, aged 51, joined the Company in January 1999, is the Deputy Operation Officer and General Manager of the Sales Department of the Company, and a director of Fudan Hong Kong. He holds a Master degree in business management and administration. He has worked for Oxford and Cambridge International Group as assistant to general manager and Beijing Wantong Industrial Corporation Limited as deputy general manager. He had worked as sales manager in the smart card division after joining the Company and has substantial experience in marketing of IC and operation management.

Mr. Li Wing Sum Steven, aged 60, joined the Company in July 2000 and is the Company Secretary of the Company. He is a fellow member respectively of the Association of Chartered Certified Accountants, the Hong Kong Institute of Certified Public Accountants and the Taxation Institute of Hong Kong and a member of the Hong Kong Institute of Directors. He has over 35 years' experience in auditing, accounting, taxation and financial management. He has worked in an international accounting firm and had been employed as executive director in a listed company in Hong Kong and group financial controller of various companies including a subsidiary of a multi-national corporation. He is the independent non-executive director of Xinjiang Xinxin Mining Industry Co., Ltd. since October 2011 and Wang On Properties Limited since April 2016, both companies are listed on the main board of the Stock Exchange. He is also the company secretary of China National Culture Group Limited, a company listed on the main board of the Stock Exchange since May 2014.

Corporate Governance Report

DIRECTORS' RESPONSIBILITY ON THE FINANCIAL STATEMENTS

The directors of the Company (the "Directors") acknowledge their responsibility for preparing the financial statements for the year ended 31 December 2016, which were prepared in accordance with statutory requirements and applicable accounting standards.

The reporting responsibilities of the external auditors on the financial statements are set out in the "Independent Auditors' Report" on pages 36 to 40.

CORPORATE GOVERNANCE PRACTICES

The Company has adopted the code provisions set out in the Corporate Governance Code (the "CG Code") contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"). In the opinion of the Directors, the Company has complied with the code provisions set out in the CG Code throughout the year ended 31 December 2016, save and except the code provision A.6.7 of the CG Code.

The code provision A.6.7 of the CG Code requires that independent non-executive directors and other non-executive directors should also attend general meetings and develop a balanced understanding of the views of shareholders. The independent non-executive Directors, Mr. Cheung Wing Keung, Mr. Guo Li, and Mr. Chen Baoying, and the non-executive Directors, Mr. Ma Zhicheng and Ms. Zhang Huajing were unable to attend the annual general meeting of the Company held on 27 May 2016 due to their other business engagements.

DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted a code of conduct regarding Directors' securities transactions on terms no less exacting than the required standard of dealings as set out in Appendix 10 of the Listing Rules. Having made specific enquiry to all Directors, the Directors have complied with such code of conduct and the required standard of dealings regarding securities transactions by the Directors throughout the year ended 31 December 2016.

BOARD OF DIRECTORS AND BOARD MEETING

Composition and role

During the year ended 31 December 2016, The Board has 12 members at present and comprises four executive Directors, four non-executive Directors and four independent non-executive Directors. There was no change in the members of the Board during the year. The Board members have no financial, business, family or other material/relevant relationships with each other. The Board's composition is formed to be well balanced to ensure strong independence exists across the Board. The biographies of the Directors are set out on pages 11 to 13, with details of diversity of skills, expertise, experience and qualifications concerning the Directors.

The Board is responsible for the leadership and management of the Group's businesses as well as its strategic planning and performances. The Management was delegated the authority and responsibility by the Board for the management of the Group. In addition, the Board has also delegated various responsibilities to the Board committees. Details of these committees are set out below in this report.

The Board classifies directors into chairman, executive directors, non-executive directors and independent non-executive directors and this has been disclosed in all the Company's announcements, circulars and the websites of the Company and the Stock Exchange.

Corporate Governance Report

BOARD OF DIRECTORS AND BOARD MEETING *(continued)*

Composition and role *(continued)*

For the year ended 31 December 2016, the Company has complied with the Listing Rules that the independent non-executive directors appointed must representing at least one-third of the Board. In addition, the Company has ensured that at least one of the independent non-executive Directors has appropriate professional qualifications, or accounting or related financial management expertise as required by the Listing Rules. The participation of independent non-executive Directors can provide the Board with independent judgements, knowledge and experience to ensure the interests of all shareholders have been duly considered.

The Company has arranged appropriate insurance cover in respect of legal action against the Directors.

Chairman and Managing Director

The Company has, since the early stage of its incorporation in 1998, segregated the duties of the chairman of the Board and the managing director. The Chairman of the Board and the Managing Director are separately held by Mr. Jiang Guoxing and Mr. Shi Lei in order to preserve independence and have a balanced judgement of views. The Chairman of the Board has the responsibilities to lead the Board and make sure it works effectively and discharges its responsibilities and that all key and appropriate issues are discussed by the Board in a timely manner. The Managing Director has the responsibilities to manage and execute the Group's business directions and operation decisions.

Appointment, re-election and removal of Directors

All appointments of Directors have to be first considered by the Nomination Committee and proposed by the Nomination Committee to the full Board for further approval. Subject to article 87 of the Company's articles of association, Directors shall be elected at the shareholders' general meeting each for a term of not more than three years and one-third of the Directors shall retire from office at the annual general meeting. Every Director (including Directors with fixed terms of appointment) shall be subject to retirement by rotation at least once every three years; and that any Director appointed as an addition or to fill a casual vacancy on the Board shall be subject to re-election by shareholders at the first general meeting after his appointment. A retiring Director is eligible for re-election.

Terms of Appointment of Directors

Executive Directors

Each of the four executive Directors has entered into a service contract with the Company for a term of three years which commenced on 19 July 2015 until 18 July 2018 and will continue thereafter unless terminated by a three months' prior written notice to be given by either party without payment of compensation.

Non-executive Directors

Each of the four non-executive Directors has entered into a service contract with the Company for a term of three years which commenced on 19 July 2015 until 18 July 2018 and will continue thereafter unless terminated by a three months' prior written notice to be given by either party without payment of compensation.

Independent Non-executive Directors

Each of the four independent non-executive Directors has signed a letter of appointment with the Company for a period commencing from 27 May 2016 until the conclusion of the forthcoming annual general meeting of the Company to be held in or about May 2017 and is subject to termination by either party giving no less than one month's written notice.

The Company has received written annual confirmation from the four independent non-executive Directors of their independence according to Rule 3.31 under the Listing Rules and recognized their independence.

BOARD OF DIRECTORS AND BOARD MEETING *(continued)*

Board meetings

The Board held four full board meetings in each year and meets as and when required. The Directors will receive details of agenda and related documentary materials for decision and to make sure they have sufficient information in advance of each board meeting.

Board minutes are kept by the company secretary of the Company (the “Company Secretary”) and are sent to the Directors for records and are open for inspection by the Directors.

Committees

The Board strives to maintain excellent corporate governance and has established committees with written terms of reference setting out the powers and duties of the committees:

1. *Audit Committee*

An audit committee has been established with written terms of reference in compliance with Listing Rules and has been published on the websites of the Stock Exchange and the Company. The primary duties of the audit committee are to review and supervise the financial reporting process and internal controls as well as risk management of the Group. The audit committee comprises three independent non-executive Directors, Mr. Cheung Wing Keung (Chairman), Mr. Guo Li and Mr. Lin Fujiang. The audit committee members are well experienced in management, accounting, finance, commercial and electronic industry sectors.

The Group’s financial statements for the year ended 31 December 2016 have been reviewed by the committee, who were of the opinion that these statements complied with the applicable accounting standards, the Listing Rules and legal requirements, and that adequate disclosures had been made.

The audit committee held four meetings during the year under review. Besides, the committee also held two meetings with the external auditors for the discussions on issues including the accounting policies adopted by the Group, internal control, risk management and financial statements.

2. *Nomination Committee*

The nomination committee now comprises two independent non-executive Directors, Mr. Cheung Wing Keung (Chairman) and Mr. Guo Li and an executive Director, Ms. Cheng Junxia. The nomination committee was established with written terms of reference which has been published on the websites of the Stock Exchange and the Company. The main roles and functions of the nomination committee include periodical review on the structure, number of members and composition of the Board, including their skill, knowledge and experience, and the independence of independent non-executive Directors and to make recommendation as to the changes of Directors. The Committee identifies suitable candidates who can add value to the management through their contributions in the relevant strategic business areas, and makes recommendation to the Board in respect of the appointment and reappointment of Directors which will result on the constitution of a strong and diverse Board. In carrying out its responsibilities, the nomination committee would give adequate consideration to the principles under Rules A.3 and A.4 of Appendix 14 of the Listing Rules.

The Nomination Committee has held one meeting during the year.

Corporate Governance Report

BOARD OF DIRECTORS AND BOARD MEETING *(continued)*

Committees *(continued)*

3. Remuneration Committee

The remuneration committee now consists of two independent non-executive Directors, Mr. Cheung Wing Keung (Chairman) and Mr. Guo Li and an executive Director, Ms. Cheng Junxia. The remuneration committee was established with written terms of reference which has been published on the websites of the Stock Exchange and the Company. The roles and functions of the remuneration committee included the determination of the remuneration packages of all executive Directors, including their benefits in kind, pension rights and compensation payments, any compensation payable for loss or termination of their office or appointment, and make recommendations to the Board for the remuneration of non-executive Directors. The remuneration committee also considers factors such as salaries of comparable companies in the same industry, time commitment and responsibilities of the Directors, employment conditions within the Group and performance.

The remuneration committee of the Company has considered and reviewed the existing terms of employment contracts of the executive Directors and non-executive Directors, and considers that the existing terms of employment contracts of the executive Directors and non-executive Directors as well as the letters of appointment of the independent non-executive Directors are fair and reasonable.

During the year under review, one meeting of the remuneration committee was held.

Record of number of Board and committee meetings and Directors' attendance

During the year ended 31 December 2016, the number of regular Board and committee meetings and Directors' attendance are set out below:

Directors	Annual general meeting	Board of Directors	Audit Committee	Nomination Committee	Remuneration committee
Mr. Jiang Guoxing	1/1	4/4	N/A	N/A	N/A
Mr. Shi Lei	0/1	4/4	N/A	N/A	N/A
Mr. Yu Jun	1/1	4/4	N/A	N/A	N/A
Ms. Cheng Junxia	1/1	4/4	N/A	1/1	1/1
Ms. Zhang Qianling	1/1	4/4	N/A	N/A	N/A
Mr. Ma Zhicheng	0/1	4/4	N/A	N/A	N/A
Mr. Yao Fuli	1/1	4/4	N/A	N/A	N/A
Ms. Zhang Huajing	0/1	3/4	N/A	N/A	N/A
Mr. Cheung Wing Keung	0/1	4/4	4/4	1/1	1/1
Mr. Guo Li	0/1	4/4	4/4	1/1	1/1
Mr. Chen Baoying	0/1	4/4	N/A	N/A	N/A
Mr. Lin Fujiang	1/1	4/4	4/4	N/A	N/A

Directors training

All Directors have participated in continuous professional development to develop and refresh their knowledge and skills. This is to ensure that their contribution to the Board remains informed and relevant. The Company has the responsibility for arranging and funding suitable training, placing an appropriate emphasis on the roles, functions and duties of a listed company director.

Corporate Governance Report

BOARD OF DIRECTORS AND BOARD MEETING *(continued)*

Directors training *(continued)*

During the year ended 31 December 2016, all Directors have received relevant trainings and have provided their training records as follow:

Directors	Training type
Mr. Jiang Guoxing	A,B
Mr. Shi Lei	A,B
Mr. Yu Jun	A,B
Ms. Cheng Junxia	A,B
Ms. Zhang Qianling	A,B
Mr. Ma Zhicheng	B
Mr. Yao Fuli	A,B
Ms. Zhang Huajing	B
Mr. Cheung Wing Keung	A,B
Mr. Guo Li	A,B
Mr. Chen Baoying	B
Mr. Lin Fujiang	A,B

Notes:

- A. Attending conference/forum/seminar/workshop
- B. Reading relevant articles and information relating to the business, economy, directors' duties and corporate governance

COMPANY SECRETARY

During the year, the Company Secretary has undertaken no less than 15 hours of professional training to update his skills and knowledge.

AUDITORS' REMUNERATION

The audit committee of the Company is responsible for considering the appointment of the external auditors and reviewing any non-audit functions performed by the external auditors, including whether such non-audit functions could lead to any potential material adverse effect on the Company. During the year under review, the Group has paid the following fees to the external auditors and which has been reviewed and approved by the audit committee:

	2016 RMB'000	2015 RMB'000
Annual audit	1,576	1,199

Corporate Governance Report

INTERNAL CONTROL AND RISK MANAGEMENT SYSTEM

The Company and each subsidiary have to conduct at least annually to enable the Board to perform a review on the Group's system of internal control and risk management to ensure the effective and adequate internal control system including finance, compliance control, operations and risk management. The reports and findings prepared by the internal audit team and the risk management team have to be circulated to the relevant committee delegated by the Board. If necessary, the internal audit team and the risk management team will submit their findings and the proposed audit plan to the audit committee for its approval. A review of system of internal control and risk management has been undergone during the year under review and the Directors are satisfied that the Group has maintained sound and effective internal controls and risk management.

CONSTITUTIONAL DOCUMENTS

The constitutional documents of the Company have been published both on the Stock Exchange and the Company's websites. For the year ended 31 December 2016, the Company has not amended its articles of association.

SHAREHOLDERS' RIGHT

Shareholders can convene an extraordinary general meeting ("EGM")

Shareholders requesting the convening of an extraordinary shareholders' general meeting or a class meeting of shareholders shall proceed in accordance with the procedures set forth below:

- (1) shareholders separately or aggregately holding a total of 10 percent or more of the shares may sign one or more written counterpart requests requesting the Board to convene an extraordinary shareholders' general meeting or a class meeting of shareholders and stating the subject of the meeting. The Board shall convene the shareholders' general meeting or the meeting of shareholders of different class as soon as possible after having received the above-mentioned written request; and
- (2) if the Board fails to issue a notice of such a meeting within 30 days after having received the above-mentioned written notice, the shareholders who made such request may themselves convene the meeting within four months after the Board received the request. The procedures according to which they convene such meeting shall be, as similar as possible, to the procedures according to which shareholders' meetings are to be convened by the Board.

Forward a proposal at a general meeting

When the Company is to hold an annual shareholders' general meeting, shareholders separately or aggregately holding 3 percent or more of the total number of the Company's shares shall be entitled to propose new notions in writing to the Company. The Company shall include in the agenda for the meeting the matters in the motions that fall within the scope of duties of the shareholders' general meeting.

Procedures for directing Shareholders' enquiries to the Board

Shareholders may at any time send their enquiries and concerns to the Board in writing through the Company Secretary. Shareholders may also make enquiries with the Board at the general meetings of the Company.

Procedure for shareholders to propose a person for election as a director

A written notice of intention to nominate a person for election as Director and a written notice of acceptance of such nomination given by such person shall be give in to the Company 7 days prior to a shareholder's meeting. The written notice shall be given in no earlier than the day after the dispatch of the notice of the meeting appointed for such election and end no later than seven days before the date of such meeting



Corporate Governance Report

SHAREHOLDERS' RELATIONS

The Company has been publishing all of its announcements including annual, interim reports and inside information in time in accordance with the Listing Rules. In addition to the post of spokesman established to liaise with shareholders and institutional investors, the Company also provides the most updated information on its website to maintain a different communication channel with its shareholders. Besides, the executive Directors, the non-executive Directors (including independent non-executive Directors) and the Company's external auditors have presented in the annual general meeting of the Company to communicate and answer to the questions raised by shareholders and significant issues were put as separate proposed resolutions.

Environmental, Social and Governance Report

The Board is pleased to present the Environmental, Social and Governance Report of the Group for the year ended 31 December 2016. This report is prepared in compliance with the relevant Environmental, Social and Governance Reporting Guide set out in Appendix 27 of the Listing Rules. The ESG Report covers the overall environmental, social and governance policy of the Company and its subsidiaries (collectively the “Group”) from 1 January 2016 to 31 December 2016.

ENVIRONMENT

Emissions

The Group’s principal activities consist of designing, developing and selling products of application-specific IC, provision of testing services for IC products; designing, developing and selling specific IC testing software and products; as well as the provision of research and consultancy services of IC technology. The Group operates in a fables model and does not have significant impact to the environment and does not generate pollution nor hazardous waste. At the time being, there are no specific environmental laws or regulations governing the industry for the Group to comply. Nevertheless, the Group places great value on environmental protection and invited Bureau Veritas to conduct an annual verification of the Group’s greenhouse gases emissions per year. By knowing the situation of greenhouse gases emissions, the Group hopes to develop policies that can reduce carbon footprint, achieve the sustainable development targets of energy saving and carbon emissions reduction, and create a green corporate image.

The Group takes initiatives in reducing the consumption of resources and adopting best environmental practice to every possible extent. Reviewing from time to time, the Group not only demonstrates its commitment to environmental protection and improvement by complying with the environmental legislations and enhancing the environmental awareness of all employees, but also by expressing concerns regarding the environmental protection measures taken by the suppliers in production.

Resources Usage

The Group’s business nature does not involve much in consumptions of electricity and water. The Group pursues the principal and practice of recycling and saving. To protect the environment, the Group hires a recycling company to carry out waste reduction with physical crushing method onto unqualified products regularly, by taking this process, metals can be separated and reusable to achieve the aim of recycling.

The Group advocates the concept of green office and implemented measures such as installation of french windows to allow more sunlight in order to reduce the use of lighting, resettlement of old office furniture, encouraging employees to use electronics copies instead of hardcopies, use of recycled papers during printing and copying, promotion of double-sided printing and copying, as well as turning off idle lighting, air conditioning and electricity to reduce energy consumptions.

Environmental and Natural Resources

The Group’s business activities have not had any significant impact on the environment and natural resources. To improve the environment and air quality, the Group advocates the concept of a greened office and takes environmental protection measures in order to reduce any pollutants production from business operations. The Group manages the number of its motor vehicles strictly and properly arranges logistics; moreover, offers free group transportation for our employees, and also encourages our employees to travel in public transits, in order to reduce the emission of pollutants from motor vehicles.

Environmental, Social and Governance Report

SOCIAL

Employment and Labor Practices

Employment

The Group provides a proper working environment conforms with labor regulations to our employees. Therefore, we have set up a human resources management system, which listed out detailed information relating to recruitment, promotion, working hours and other employee benefits, in order to comply with related labour laws and regulations. We also provide our employees with a pleasant and green working environment, follow the anti-discrimination laws, and encourage diversification of skills of working teams. Our equal opportunity policy ensures applicants or employees are treated equally when seeking a job or working in the Group, and will not deprive of their rights because of their sex, age, race, pregnancy, disability, marital or family status. The management takes review from time to time on the salary level within the industry and makes adjustment to the Group's salary policy accordingly.

Health and Safety

In addition to standard employee benefits, the Group also provides regular physical examination, and arranges internal recreation club activities and competitions to ensure the physical and mental health of employees and enhance their sense of belongings to the Group.

Development and Training

The Group provides on-the-job training, technical exchanges, holds seminars and group learning activities for employees and managements to enhance their understanding on the industry trends and technological development and strengthen their professional skills and knowledge. All of which will help to employees' long-term technology and business development.

Labor Standards

The Group strictly abides the Labor Law of the People's Republic of China and any social insurance related laws and regulations; overseas subsidiaries and branch offices also comply with related labor laws and regulations enforced in the countries and regions they operated. The Group sets up a system to state clear guidelines for hiring, salary levels, promotion, benefits, and retirement etc., in order to guarantee the relationship, rights and interest of both employer and employees.

Operating Practices

Supply Chain Management

The Group has a complete supplier selection system, all the suppliers have to pass the assessment on their qualifications and material supplies. All the suppliers of the Group are well-known enterprises in the industry, having large equipment configuration and considerable technical capabilities. The Group assesses the elements of cost, working environment, compliance with labor and social environmental laws and the protection of intellectual property, so as to evaluate and select suitable suppliers comprehensively.

Product Responsibility

The basis for the survival of the Group is to provide satisfactory products and services to the customers; take the development of customers as the Group's foundation of development; and protecting the environment for the survival of the Group and its customers is the premise of sustainable operations. The Group's products completely meet the design of functional specifications; thus, its products provided to the customers are with competitiveness in the international markets. The Group develops relevant management policies, include strict quality control, satisfaction survey and aftersales services, to ensure the Group's products are produced by qualified materials and manufacturing processes in accordance with product safety requirements from related laws and regulations.

Environmental, Social and Governance Report

SOCIAL *(continued)*

Operating Practices *(continued)*

Product Responsibility (continued)

The Group has many self-developed intellectual property rights, and the industry has paid great attention on the protection of intellectual property rights. The Group's operations must involve the use of the intellectual property rights by an autonomous, customer or supplier. Therefore, an extremely rigorous system for the protection of intellectual property rights has been established, includes adding intellectual property protection clauses when entering contracts with customers or suppliers in order to protect the intellectual property rights of all parties, and to ensure the related staff to comply with all relevant laws and regulations.

The Group has established environmental managed material standards, using environmental technology to manufacture and provide environmentally friendly products, and do not use any prohibited raw materials in our products and manufacturing processes.

Anti-corruption

The operations of companies in the Group comply with the laws and regulations in China and the counties and regions they operated, and it is forbidden to use any opportunity or authority to obtain personal benefits or interest, as stated in the employment contract.

The Group has internal monitor system to avoid conflicts of interest and different levels of approvals in its business operations.

Community

Community Investment

The Group promotes its staff to join activities and contribute to the local communities in which the group companies operate. The Group educates and cultivates staff with a review to improve their social responsibility awareness, and actively encourages staff to volunteer their leisure hours to participate in functions for the improving of local communities and environment. The Group will try its best endeavors to increase investment in communities in order to build a better environment.

Report of the Directors

The directors present their report and the audited financial statements of Shanghai Fudan Microelectronics Group Company Limited (the “Company”) and its subsidiaries (collectively referred to as the “Group”) for the year ended 31 December 2016.

PRINCIPAL ACTIVITIES AND BUSINESS REVIEW

The principal activities of the Company consist of designing, developing and selling products of application-specific integrated circuits. There were no significant changes in the nature of the Group’s principal activities during the year.

Further discussion and analysis of these activities as required by Schedule 5 to the Hong Kong Companies Ordinance, including a description of the principal risks and uncertainties facing the Group and an indication of likely future development in the Group’s business, can be found in the Management Discussion and Analysis set out on pages 3 to 9 of this annual report. This discussion forms part of this directors’ report.

RESULTS AND DIVIDENDS

The Group’s profit for the year ended 31 December 2016 and the Group’s financial position at that date are set out in the financial statements on pages 43 to 44.

The directors did not recommend the payment of final dividend in respect of the year to shareholders.

SUMMARY FINANCIAL INFORMATION

A summary of the published results and assets, liabilities and non-controlling interests of the Group for the last five financial years, as extracted from the audited financial statements, is set out on page 108. This summary does not form part of the audited financial statements.

SHARE CAPITAL

There were no movements in either the Company’s authorised or issued share capital during the year.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company’s articles of association or the laws of the People’s Republic of China (the “PRC”) which would oblige the Company to offer new shares on a pro rata basis to existing shareholders.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

Neither the Company, nor any of its subsidiaries purchased, redeemed or sold any of the Company’s listed securities during the year.

Report of the Directors

DISTRIBUTABLE RESERVES

According to the relevant regulations of the PRC, the amount of retained profits available for distribution is the lower of the amount determined under PRC accounting standards and the amount determined under Hong Kong Financial Reporting Standards (“HKFRSs”). At 31 December 2016, the Company’s reserves available for distribution amounted to RMB841,429,000, and no final dividend has been proposed for the year.

MAJOR CUSTOMERS AND SUPPLIERS

In the year under review, sales to the Group’s five largest customers accounted for 30% of the total sales for the year and sales to the largest customer included therein amounted to 10%. Purchases from the Group’s five largest suppliers accounted for 62% of the total purchases for the year and purchase from the largest supplier included therein amounted to 34%.

None of the directors of the Company or any of their associates or any shareholders (which, to the best knowledge of the directors, own more than 5% of the Company’s issued share capital) had any beneficial interest in the Group’s five largest suppliers and customers.

DIRECTORS

The directors of the Company during the year were:

Executive directors:

Mr. Jiang Guoxing
Mr. Shi Lei
Mr. Yu Jun
Ms. Cheng Junxia

Non-executive directors:

Ms. Zhang Qianling
Mr. Ma Zhicheng
Mr. Yao Fuli
Ms. Zhang Huajing

Independent non-executive directors:

Mr. Cheung Wing Keung
Mr. Guo Li
Mr. Chen Baoying
Mr. Lin Fujiang

In accordance with article 87 of the Company’s latest amended articles of association, the directors shall be elected at the general meeting each for a term of not more than three years. One-third of the directors for the time being, or, if their number is not three or a multiple of three, then the number nearest to, but not less than, one-third, shall retire from office at the annual general meeting (the “AGM”). Every director (including directors with fixed terms of appointment) shall be subject to retirement by rotation at least once every three years. Any person appointed as a director either to fill a vacant position or as an addition to the board of directors shall be subject to retirement and re-election by shareholders at the first annual general meeting after the appointment.

DIRECTORS *(continued)*

The Company has received annual confirmations of independence from Mr. Cheung Wing Keung, Mr. Guo Li, Mr. Chen Baoying and Mr. Lin Fujiang, and as at the date of this report, still considers them to be independent.

DIRECTORS' AND SENIOR MANAGEMENT'S BIOGRAPHIES

Biographical details of the directors of the Company and the senior management of the Group are set out in the section headed "Directors' and Senior Management's Biographies" of the annual report.

DIRECTORS' SERVICE CONTRACTS

Each of the executive directors and non-executive directors has entered into a service contract with the Company for a term of three years which commenced on 19 July 2015 and will continue thereafter unless terminated by a three months' prior written notice to be given by either party without payment of compensation.

Mr. Cheung Wing Keung, Mr. Guo Li, Mr. Chen Baoying, and Mr. Lin Fujiang, who are the independent non-executive directors of the Company, have signed letters of appointment with the Company for a period commencing from May 2016, until the forthcoming AGM in or about May 2017 and are subject to termination by either party giving no less than one month's written notice.

No director proposed for re-election at the forthcoming AGM has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

DIRECTORS' REMUNERATION

The directors' fees are subject to shareholders' approval at general meetings. Other emoluments are determined by the Company's board of directors with reference to directors' duties, responsibilities and performance and the results of the Group.

PERMITTED INDEMNITY PROVISION

A permitted indemnity provision for the benefit of the Directors is currently in force and was in force throughout the financial year. The Company has taken out and maintained directors and officers liability insurance which provides appropriate cover for, among others, incurred by Directors to a third party.

DIRECTORS' INTERESTS IN TRANSACTIONS, ARRANGEMENTS OR CONTRACTS

No director nor a connected entity of a director had a material interest, either directly or indirectly, in any transactions, arrangements or contracts of significance to the business of the Group to which the holding company of the Company or any of the Company's subsidiaries was a party during the year.

MANAGEMENT CONTRACTS

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or were in existence during the year.

Report of the Directors

DIRECTORS' AND SUPERVISORS' INTERESTS IN SHARES AND UNDERLYING SHARES AND DEBENTURES

At 31 December 2016, the interests of the directors and supervisors of the Company in the share capital and underlying shares and debentures of the Company or its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the “SFO”), as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO, or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the “Hong Kong Stock Exchange”) pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers, were as follows:

Long positions in domestic shares of the Company:

	Number of issued shares held, capacity and nature of interest				Percentage of the Company's issued share capital
	Directly beneficially owned	Through spouse or minor children	Through controlled corporation	Total	
Directors					
Mr. Jiang Guoxing	7,210,000	–	–	7,210,000	1.17
Mr. Shi Lei	7,210,000	–	–	7,210,000	1.17
	14,420,000	–	–	14,420,000	

Report of the Directors

DIRECTORS' AND SUPERVISORS' INTERESTS IN SHARES AND UNDERLYING SHARES AND DEBENTURES *(continued)*

Long positions in shares and underlying shares of associated corporations:

	Name of associated corporation	Relationship with the Company	Shares/equity derivatives	Number of shares/equity derivatives held	Capacity and nature of interest	Percentage of the associated corporation's issued share capital
Directors						
Mr. Yu Jun	Shanghai Doublepoint Information Technology Co., Ltd. ("Doublepoint")	Company's subsidiary	Ordinary shares	200,000	Directly beneficially owned	2.062
Supervisors						
Mr. Li Wei	Doublepoint	Company's subsidiary	Ordinary shares	100,000	Directly beneficially owned	1.031
Mr. Li Wei	Sino IC Technology Co., Ltd. ("Sino IC")	Company's subsidiary	Ordinary shares	126,000	Directly beneficially owned	0.100

Save as disclosed above, as at 31 December 2016, none of the directors or supervisors had registered an interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations that was required to be recorded pursuant to section 352 of the SFO, or as otherwise notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers.

At no time during the year were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any director or their respective spouses or minor children, or were any such rights exercised by them; or was the Company or any of its subsidiaries a party to any arrangement to enable the directors to acquire such rights in any other body corporate.

CONTRACT OF SIGNIFICANCE

No contracts of significance in relation to the Group's business in which the Company, any of its subsidiaries, or fellow subsidiaries, or its parent company was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted during or at the end of the year.

Report of the Directors

SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSONS' INTERESTS IN SHARES AND UNDERLYING SHARES

At 31 December 2016, the following interests of 5% or more of the issued share capital of the Company were recorded in the register of interests required to be kept by the Company pursuant to section 336 of the SFO:

Long positions in shares of the Company:

Name	Notes	Capacity and nature of interest	Number of ordinary shares held	Class of shares	Percentage of shareholding on relevant class of shares	Percentage of the Company's issued share capital
Shanghai Fudan High Tech Company ("Fudan High Tech")	(1)	Directly beneficially owned	106,730,000	Domestic shares	28.46	17.29
Shanghai Fudan Asset Management Co., Ltd	(1)	Through a controlled corporation	106,730,000	Domestic shares	28.46	17.29
Fudan University	(1)	Through a controlled corporation	106,730,000	Domestic shares	28.46	17.29
Shanghai Fudan Technology Enterprise Holdings Limited ("Fudan Technology")	(2)	Directly beneficially owned	109,620,000	Domestic shares	29.23	17.76
Shanghai Commerce and Invest (Group) Corporation ("SCI")	(2)	Through a controlled corporation	109,620,000	Domestic shares	29.23	17.76
Bailian (Group) Co., Ltd. ("Bailian Group")	(2)	Through a controlled corporation	109,620,000	Domestic shares	29.23	17.76
Shanghai Zhengben Corporate Management Consultant Partnership Enterprise ("Shanghai Zhengben")	(3)	Directly beneficially owned	52,167,270	Domestic shares	13.91	8.45
Shanghai Yikun Investment Consultant Partnership Enterprise ("Shanghai Yikun")	(3)	Through a controlled corporation	66,845,110	Domestic shares	17.83	10.83
Zhang Yong	(3)	Through a controlled corporation	66,845,110	Domestic shares	17.83	10.83

SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSONS' INTERESTS IN SHARES AND UNDERLYING SHARES *(continued)*

Long positions in shares of the Company: *(continued)*

Name	Notes	Capacity and nature of interest	Number of ordinary shares held	Class of shares	Percentage of shareholding on relevant class of shares	Percentage of the Company's issued share capital
Shanghai Zhenghua Investment Consultant Partnership Enterprise ("Shanghai Zhenghua")	(4)	Directly beneficially owned	47,443,420	Domestic shares	12.65	7.68
Shanghai Shanyao Industrial Limited* ("Shanghai Shanyao")	(4)	Through a controlled corporation	47,443,420	Domestic shares	12.65	7.68
Zhou Yufeng	(4)	Through a controlled corporation	47,443,420	Domestic shares	12.65	7.68
Shanghai Guonian Investment Consultant Partnership Enterprise ("Shanghai Guonian")	(5)	Directly beneficially owned	29,941,470	Domestic shares	7.98	4.85
Shanghai Danruo Investment Management Partnership Enterprise ("Shanghai Danruo")	(5)	Through a controlled corporation	29,941,470	Domestic shares	7.98	4.85
Zhongrong Yicheng Asset Management Limited ("Zhongrong Yicheng")	(5)	Through a controlled corporation	29,941,470	Domestic shares	7.98	4.85
Beijing Zhongrong Dingxin Investment Management Limited ("Zhongrong Dingxin")	(5)	Through a controlled corporation	29,941,470	Domestic shares	7.98	4.85

Report of the Directors

SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSONS' INTERESTS IN SHARES AND UNDERLYING SHARES *(continued)*

Long positions in shares of the Company: *(continued)*

Name	Notes	Capacity and nature of interest	Number of ordinary shares held	Class of shares	Percentage of shareholding on relevant class of shares	Percentage of the Company's issued share capital
Zhongrong International Trust Limited ("Zhongrong International")	(5)	Through a controlled corporation	29,941,470	Domestic shares	7.98	4.85
Jingwei Textile Machinery Co., Ltd. ("Jingwei Textile")	(5)	Through a controlled corporation	29,941,470	Domestic shares	7.98	4.85
Springs China Opportunities Master Fund ("Spring China")	(6)	Directly beneficially owned	19,224,000	H shares	7.93	3.11
Springs China Limited	(6)	Through a controlled corporation	19,224,000	H shares	7.93	3.11
Zhao Jun	(6)	Through a controlled corporation	19,224,000	H shares	7.93	3.11
Chi Rui	(6)	Through a controlled corporation	19,224,000	H shares	7.93	3.11

Notes:

- (1) Fudan High Tech is a state-owned enterprise wholly owned by Shanghai Fudan Asset Management Co., Ltd, and Shanghai Fudan Asset Management Co., Ltd is wholly owned by Fudan University.
- (2) Bailian Group is a state-owned enterprise wholly owned by the Shanghai Municipal Government and wholly owned SCI, and SCI held 70.2% of the equity interest of Fudan Technology. Accordingly, each of SCI and Bailian Group is deemed to be interested in Fudan Technology's interest in the Company.
- (3) Zhang Yong held 95% of the equity interest in Shanghai Yikun, and Shanghai Yikun held 99.81% of the equity interest in Shanghai Zhengben (formerly known as "Shanghai Zhengben Investment Consultant Partnership Enterprise"). Accordingly, each of Shanghai Yikun and Zhang Yong is deemed to be interested in Shanghai Zhengben's interest in the Company. Shanghai Yikun and Zhang Yong further held the Company's interest through another controlled corporation.
- (4) Zhou Yufeng held 99% of the equity interest in Shanghai Shanyao, and Shanghai Shanyao held 99.79% of the equity interest in Shanghai Zhenghua (formerly known as "Shanghai Zhenghua Investment Consultant Partnership Enterprise"). Accordingly, each of Shanghai Shanyao and Zhou Yufeng is deemed to be interested in Shanghai Zhenghua's interest in the Company.

SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSONS' INTERESTS IN SHARES AND UNDERLYING SHARES *(continued)*

Long positions in shares of the Company: *(continued)*

Notes: *(continued)*

- (5) Jingwei Textile held 37.47% of the equity interest in Zhongrong International; Zhongrong International wholly owned Zhongrong Dingxin; Zhongrong Dingxin held 80% of the equity interest in Zhongrong Yicheng; Zhongrong Yicheng held 0.01% of the equity interest in Shanghai Danruo and is the general partner; and Shanghai Danruo held 72.69% of the equity interest in Shanghai Guonian (formerly known as Shanghai Guonian Investment Consultant Partnership Enterprise). Accordingly, each of Shanghai Danruo, Zhongrong Yicheng, Zhongrong Dingxin, Zhongrong International and Jingwei Textile is deemed to be interested in Shanghai Guonian's interest in the Company.
- (6) Spring China is beneficially owned by Spring China Limited, which is beneficially owned by Zhao Jun and Chi Rui. Accordingly, each of Spring China Limited, Zhao Jun and Chi Rui is deemed to be interested in Spring China's interest in the Company.

Save as disclosed above, as at 31 December 2016, no person, other than the directors and supervisors of the Company, whose interests are set out in the section headed "Directors' and supervisors' interests and short positions in shares and underlying shares and debentures" above, had registered an interest or short position in the shares or underlying shares of the Company that was required to be recorded pursuant to section 336 of the SFO.

CONNECTED TRANSACTIONS AND CONTINUING CONNECTED TRANSACTIONS

During the year, the Company and the Group had the following connected and continuing connected transactions, certain details of which are disclosed in compliance with the requirements of Chapter 14A of the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange (the "Listing Rules").

Connected transactions

Except for the continuing connected transactions disclosed below, details of the connected transactions of the Group are set out in note 26 to the financial statements.

Continuing connected transactions

On 12 August 2003, the Company and Fudan University ("SFU") entered into an agreement under which the Company was required to pay a technical and equipment support fee to SFU based on a price mutually agreed by the two parties. The Company expects that the total transaction amount with SFU will be with an annual cap during 2016 of RMB800,000 (2015: RMB800,000), and the Company paid RMB105,000 in 2016 (2015: RMB570,000).

On 18 January 2010, the Company entered into a co-operation agreement with Shanghai Fukong Hualong Micro-system Technology Co., Ltd. ("Fukong Hualong"), a 38.25% owned subsidiary of the Company, for the research and development of electricity meter IC chips ("Smart Meter Agreement") for a co-operation term commencing from the date of signing the agreement up to the termination of product life. The resultant intellectual proprietary rights would be shared equally by both parties. Under the Smart Meter Agreement, after deducting the production costs, revenue derived from the product would be shared by the Company and Fukong Hualong based on two sales volume levels at the ratios of 82% to 18% and 88% to 12%, respectively. As the products contemplated under the Smart Meter Agreement have to be upgraded to a new version due to market changes, on 16 April 2015, the Company entered into a supplementary agreement with Fukong Hualong with a single revised revenue sharing of 88% to 12% for a term of two years. The annual caps for the profit sharing payable to Fukong Hualong for the two years ended 31 December 2015 and 2016 are RMB4,000,000 and RMB3,000,000. During 2016, the Company has paid profit sharing of RMB1,533,000 to Fukong Hualong (2015: RMB3,246,000).

Report of the Directors

CONNECTED TRANSACTIONS AND CONTINUING CONNECTED TRANSACTIONS

(continued)

Continuing connected transactions *(continued)*

On 24 June 2009, the Company entered into a co-operation agreement with Fukong Hualong for the setting up a jointly developed “Chip & System” mode (“Cooperation Agreement”) with a view to explore markets in global positioning system (“GPS”), smart video player and mobile payment. Based on the previous cooperation result, on 23 April 2012, the Company entered into a cooperation agreement with Fukong Hualong for the product development of satellite navigation IC chips (“Satellite Navigation Agreement”) for a term starting from the agreement date up to the end of the estimated product life which is about 3 years. Pursuant to the Satellite Navigation Agreement, the Company and Fukong Hualong will carry out two cooperation modules respectively in project mode and product sales mode. The cooperation agreement expired on 22 April 2015 and because of further function upgrade requirements, on 16 April 2015, the Company renewed the original agreement for another two years.

According to the renewed Satellite Navigation Agreement, under the project mode, the Company will be the primary applicant for the government grants. The Company will use the grants for research and development expenditures of government grant projects, and will pay part of the grants to Fukong Hualong according to Fukong Hualong’s contributions in the projects and negotiations between the parties, with annual caps of RMB4,000,000 and RMB5,000,000 for the years ended 31 December 2015 and 2016. During 2016, the Company has distributed RMB1,920,000 (2015: Nil) of R&D income to Fukong Hualong.

Based on the above-mentioned project sales mode, both parties, having realised that there are prospects in product industrialisation, have entered into cooperation under product sales mode. The Company will be responsible for the production of qualified IC chips and Fukong Hualong will be responsible for product marketing. Both parties will determine a market selling price with reference to the production costs, selling and distribution costs and market conditions (“Market Selling Price”). According to the renewed Satellite Navigation Agreement, the Company will sell products to Fukong Hualong at a price based on production costs plus a gross profit (according to the Satellite Navigation Agreement signed in April 2012: production cost plus 50% gross profit) and with reference to Market Selling Price. The annual caps relating to the Company’s sales of products to Fukong Hualong are RMB5,000,000 and RMB6,000,000 for the years ended 31 December 2015 and 2016. In 2016, the Company sold related products of RMB3,047,000 (2015: RMB3,072,000) to Fukong Hualong.

As the nature of the transactions contemplated under the Smart Meter Agreement and the Satellite Navigation Agreement is similar and will continue, pursuant to rule 14A.81 of the Listing Rules, these transactions should be aggregated. As such, the Company expects that the total transaction amount will be with an annual cap during 2015 and 2016 of RMB13,000,000 and RMB14,000,000, respectively. The Company paid RMB1,533,000 for Smart Meter Agreement (2015: RMB3,246,000) and RMB1,920,000 for Satellite Navigation Agreement (2015: Nil) of R&D expense compensation to Fukong Hualong, while Fukong Hualong paid RMB3,047,000 (2015: RMB3,072,000) to the Company for the purchase of products during 2016.

The independent non-executive directors of the Company have reviewed the continuing connected transactions set out above and have confirmed that these continuing connected transactions were entered into (i) in the ordinary and usual course of business of the Group; (ii) on normal commercial terms or on terms no less favourable to the Group than terms available to independent third parties; and (iii) in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

CONNECTED TRANSACTIONS AND CONTINUING CONNECTED TRANSACTIONS

(continued)

Continuing connected transactions *(continued)*

Ernst & Young, the Company's auditors, were engaged to report on the Group's continuing connected transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information* and with reference to Practice Note 740 *Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules* issued by the Hong Kong Institute of Certified Public Accountants. Ernst & Young have issued their unqualified letter containing their findings and conclusions in respect of the continuing connected transactions disclosed above by the Group in accordance with Listing Rules 14A.56. A copy of the auditors' letter has been provided by the Company to the Hong Kong Stock Exchange.

SUFFICIENCY OF PUBLIC FLOAT

Based on information that is publicly available to the Company and within the knowledge of the directors, at least 25% of the Company's total issued share capital was held by the public as at the date of this report.

DIRECTORS' INTERESTS IN A COMPETING BUSINESS

During the year and up to the date of this report, none of the directors of the Company had an interest in a business which competes or is likely to compete, either directly or indirectly, with the businesses of the Group, as defined in the Listing Rules.

CORPORATE GOVERNANCE CODE

In the opinion of the directors, the Company has complied with the code provisions set out in the Corporate Governance Code (the "CG Code") contained in Appendix 14 of the Listing Rules throughout the accounting period covered by the annual report, save and except the code provision A.6.7 of the CG Code.

A report on the principal corporate governance practices adopted by the Company is set out in the section headed "Corporate Governance Report" of the annual report.

AUDITORS

Ernst & Young retire and a resolution for their reappointment as auditors of the Company will be proposed at the forthcoming AGM.

ON BEHALF OF THE BOARD

Jiang Guoxing

Chairman

Shanghai, the PRC
28 March 2017

Independent Auditor's Report



To the shareholders of Shanghai Fudan Microelectronics Group Company Limited

(Established in the People's Republic of China with limited liability)

OPINION

We have audited the consolidated financial statements of Shanghai Fudan Microelectronics Group Company Limited (the “Company”) and its subsidiaries (the “Group”) set out on pages 41 to 107, which comprise the consolidated statement of financial position as at 31 December 2016, and the consolidated statement of profit or loss, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2016, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards (“HKFRSs”) issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”) and have been properly prepared in compliance with the disclosure requirements of the Hong Kong Companies Ordinance.

BASIS FOR OPINION

We conducted our audit in accordance with Hong Kong Standards on Auditing (“HKSA”) issued by the HKICPA. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the HKICPA's *Code of Ethics for Professional Accountants* (the “Code”), and we have fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

KEY AUDIT MATTERS

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Independent Auditor's Report

KEY AUDIT MATTERS (continued)

Key audit matter	How our audit addressed the key audit matter
<p><i>Deferred development costs</i></p> <p>As at 31 December 2016, the carrying amount of deferred development costs was RMB139,547,000. Expenditure incurred in developing new products is capitalised and deferred upon meeting the criteria as described in Hong Kong Accounting Standard 38 Intangible Assets. The balance and transaction of deferred development costs is material to the consolidated financial statements and management exercised judgement and estimation in determining the eligibility of the costs for capitalisation, the useful economic lives and impairment, if any, of the capitalised development costs. The Group's disclosures about development costs capitalised are included in note 2.4 Summary of Significant Accounting Policies, note 3 Significant Accounting Judgements and Estimates and note 13 Intangible Assets to the financial statements.</p>	<p>Our audit procedures included, among others, evaluating the internal controls identified by management in capitalising the deferred development costs, performing tests on criteria for initial recognition, costs capitalised and assessed the timeliness of the commencement of amortisation when the asset is available for use. We reviewed the assumptions and methodologies used by management in estimating the useful economic lives and performing impairment assessment on development costs focusing on the estimates surrounding future economic cash flows. We involved our valuation specialist in reviewing management's impairment assessment.</p>
<p><i>Provisions for inventories</i></p> <p>As at 31 December 2016, the carrying amount of inventories was RMB280,612,000. The balance of inventories is material to the consolidated financial statements and management exercised estimation in determining the write-down of inventories to net realisable value based on an assessment of the realisability of inventories and the provision for slow-moving inventories based on the analysis of historical and subsequent usage or sales of inventories. The Group's disclosures about inventory are included in note 2.4 Summary of Significant Accounting Policies, note 3 Significant Accounting Judgements and Estimates and note 15 Inventories to the financial statements.</p>	<p>We assessed the process, methods and assumptions used to develop the provision for inventories. This included comparing management's calculations for consistency against those used in the prior year and considering whether there was any indication of management bias.</p> <p>We tested the underlying data used by management to calculate the provision for obsolete inventories, typically an aged inventory analysis, by re-performing the ageing calculation. We compared the historical and subsequent sales and usage information of inventories. We also tested the calculation by assessing the calculation criteria, testing the estimated selling prices and estimated costs to be incurred to completion and disposal, and recalculating the provision for inventories on a sampling basis.</p>

Independent Auditor's Report

OTHER INFORMATION INCLUDED IN THE ANNUAL REPORT

The directors of the Company are responsible for the other information. The other information comprises the information included in the Annual Report, other than the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

RESPONSIBILITIES OF THE DIRECTORS FOR THE CONSOLIDATED FINANCIAL STATEMENTS

The directors of the Company are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with HKFRSs issued by the HKICPA and the disclosure requirements of the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors of the Company are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors of the Company either intend to liquidate the Group or to cease operations or have no realistic alternative but to do so.

The directors of the Company are assisted by the Audit Committee in discharging their responsibilities for overseeing the Group's financial reporting process.

AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Our report is made solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

Independent Auditor's Report

AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

As part of an audit in accordance with HKSAs, we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

Independent Auditor's Report

AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

From the matters communicated with the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Ng Cheung.

Ernst & Young

Certified Public Accountants

22/F CITIC Tower

1 Tim Mei Avenue

Central, Hong Kong

28 March 2017

Consolidated Statement of Profit or Loss

Year ended 31 December 2016

	Notes	2016 RMB'000	2015 RMB'000
REVENUE	5	1,187,490	1,039,725
Cost of sales		(556,198)	(489,416)
Gross profit		631,292	550,309
Other income and gains	5	162,985	83,080
Selling and distribution expenses		(68,428)	(61,887)
Administrative expenses		(87,300)	(80,579)
Other expenses		(378,692)	(297,598)
PROFIT BEFORE TAX	6	259,857	193,325
Income tax expense	9(a)	(19,767)	(15,335)
PROFIT FOR THE YEAR		240,090	177,990
Profit attributable to:			
Owners of the parent	11	212,258	158,898
Non-controlling interests		27,832	19,092
		240,090	177,990
EARNINGS PER SHARE			
ATTRIBUTABLE TO ORDINARY			
EQUITY HOLDERS OF THE PARENT			
Basic and diluted			
– For profit for the year	11	RMB34.38 cents	RMB25.74 cents

Consolidated Statement of Comprehensive Income

Year ended 31 December 2016

	2016 RMB'000	2015 RMB'000
PROFIT FOR THE YEAR	240,090	177,990
OTHER COMPREHENSIVE INCOME		
Other comprehensive income to be reclassified to profit or loss in subsequent periods:		
Exchange differences:		
Exchange differences on translation of a foreign operation	756	668
Net other comprehensive income to be reclassified to profit or loss in subsequent periods	756	668
OTHER COMPREHENSIVE INCOME FOR THE YEAR, NET OF TAX	756	668
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	240,846	178,658
Total comprehensive income attributable to:		
Owners of the parent	213,014	159,566
Non-controlling interests	27,832	19,092
	240,846	178,658

Consolidated Statement of Financial Position

31 December 2016

	Notes	2016 RMB'000	2015 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment	12	308,702	332,011
Intangible assets	13	139,547	160,645
Deferred tax assets	9(c)	42,972	38,264
Total non-current assets		491,221	530,920
CURRENT ASSETS			
Inventories	15	280,612	214,110
Trade and bills receivables	16	466,616	366,017
Prepayments, deposits and other receivables	17	24,195	21,383
Cash and bank balance	18	540,224	386,033
Total current assets		1,311,647	987,543
CURRENT LIABILITIES			
Trade and bills payables	19	113,922	124,703
Accruals, other payables and deferred income	20	286,665	261,067
Tax payable	9(b)	15,771	13,369
Total current liabilities		416,358	399,139
NET CURRENT ASSETS		895,289	588,404
TOTAL ASSETS LESS CURRENT LIABILITIES		1,386,510	1,119,324

Consolidated Statement of Financial Position

31 December 2016

	Notes	2016 RMB'000	2015 RMB'000
TOTAL ASSETS LESS CURRENT LIABILITIES		1,386,510	1,119,324
NON-CURRENT LIABILITIES			
Deferred income	20	12,078	5,738
Net assets		1,374,432	1,113,586
EQUITY			
Equity attributable to owners of the parent			
Issued capital	21	61,733	61,733
Reserves	22	1,160,033	940,097
		1,221,766	1,001,830
Non-controlling interests		152,666	111,756
Total equity		1,374,432	1,113,586

Shi Lei
Director

Cheng Junxia
Director

Consolidated Statement of Changes in Equity

Year ended 31 December 2016

	Attributable to owners of the parent									
		Issued	Share	Statutory	Exchange	Other	Retained	Non-	Total	
	Notes	share	premium	surplus	fluctuation	reserves	profits	controlling	equity	
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	
	(Note 21)	(Note 22)	(Note 22)		(Note 22)					
At 1 January 2015		61,733	168,486*	42,701*	(3,476)*	7,821*	564,999	842,264	92,664	934,928
Profit for the year		-	-	-	-	-	158,898	158,898	19,092	177,990
Exchange differences related to foreign operation		-	-	-	668	-	-	668	-	668
Total comprehensive income for the year		-	-	-	668	-	158,898	159,566	19,092	178,658
Transfer	22	-	-	2,016	-	-	(2,016)	-	-	-
At 31 December 2015		61,733	168,486*	44,717*	(2,808)*	7,821*	721,881*	1,001,830	111,756	1,113,586
Profit for the year		-	-	-	-	-	212,258	212,258	27,832	240,090
Exchange differences related to foreign operation		-	-	-	756	-	-	756	-	756
Total comprehensive income for the year		-	-	-	756	-	212,258	213,014	27,832	240,846
Capital contribution from non-controlling interests	22	-	-	-	-	6,922	-	6,922	13,078	20,000
Transfer	22	-	-	3,051	-	-	(3,051)	-	-	-
At 31 December 2016		61,733	168,486*	47,768*	(2,052)*	14,743*	931,088*	1,221,766	152,666	1,374,432

* These reserve accounts comprise the consolidated reserves of RMB1,160,033,000 (2015: RMB940,097,000) in the consolidated statement of financial position.

Consolidated Statement of Cash Flows

Year ended 31 December 2016

	Notes	2016 RMB'000	2015 RMB'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before tax		259,857	193,325
Adjustments for:			
Bank interest income	5, 6	(9,169)	(7,950)
Bank interest expense		116	130
Loss on disposal of items of property, plant and equipment and intangible assets	6	13,553	8,194
Depreciation	12	68,055	40,706
Impairment of intangible assets	13	36,126	16,389
Amortisation of intangible assets	13	44,417	26,042
		412,955	276,836
Increase in inventories		(66,502)	(4,077)
Increase in trade and bills receivables		(100,599)	(125,277)
Decrease in prepayments, deposits and other receivables		2,910	5,038
(Decrease)/increase in trade and bills payables		(10,781)	50,314
Increase in accruals, other payables and deferred income		33,750	15,974
		271,733	218,808
Cash generated from operations		271,733	218,808
Hong Kong profits tax refunded/(paid)	9(b)	205	(112)
PRC taxes paid	9(b)	(22,278)	(19,086)
		249,660	199,610
CASH FLOWS FROM INVESTING ACTIVITIES			
Increase/(decrease) in time deposits with original maturity of over three months when acquired	18	10,860	(79,700)
Bank interest received		7,207	9,100
Purchases of items of property, plant and equipment		(50,610)	(89,996)
Proceeds from disposal of items of property, plant and equipment		116	39
Additions to intangible assets	13	(72,822)	(79,452)
		(105,249)	(240,009)
Net cash flows used in investing activities		(105,249)	(240,009)

Consolidated Statement of Cash Flows

Year ended 31 December 2016

	Notes	2016 RMB'000	2015 RMB'000
Net cash flows used in investing activities		(105,249)	(240,009)
CASH FLOWS FROM FINANCING ACTIVITIES			
New bank loans		35,811	20,206
Repayment of bank loans		(35,811)	(20,206)
Interest paid		(116)	(130)
Capital contribution from non-controlling interests		20,000	–
Net cash flows generated from/(used in) financing activities		19,884	(130)
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS			
Cash and cash equivalents at beginning of year		121,306	161,167
Effect of foreign exchange rate changes, net		756	668
CASH AND CASH EQUIVALENTS AT END OF YEAR		286,357	121,306
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash on hand and demand deposits	18	191,836	98,107
Non-pledged time deposits	18	348,388	287,926
Cash and bank balances as stated in the consolidated statement of financial position	18	540,224	386,033
Time deposits with original maturity of over three months when acquired	18	(253,867)	(264,727)
Cash and cash equivalents as stated in the consolidated statement of cash flows		286,357	121,306

Notes to Financial Statements

31 December 2016

1. CORPORATE AND GROUP INFORMATION

Shanghai Fudan Microelectronics Group Company Limited (the “Company”, formerly known as Shanghai Fudan Microelectronics Company Limited) is a limited liability company established in Shanghai, the People’s Republic of China (the “PRC”). The registered office of the Company is located at No. 220 Handan Road, Shanghai, the PRC. The Company has established a place of business in Hong Kong, which is located at Flat 6, 5/F., East Ocean Centre, 98 Granville Road, Tsimshatsui East, Kowloon.

The principal activities of the subsidiaries are the provision of testing services for integrated circuit (“IC”) products; designing, developing and selling IC testing software and products; the production of probe cards; as well as the provision of research and consultancy services of IC technology.

The Company’s principal activities have not changed during the year and consist of the design and development and sale of products of application-specific IC.

Information about subsidiaries

Particulars of the subsidiaries are as follows:

Name	Place of incorporation/ registration and place of operations	Issued ordinary/ registered share capital	Percentage of equity directly attributable to the Company		Principal activities
			Direct	Indirect	
Sino IC Technology Co., Ltd. (“Sino IC”) *	People’s Republic of China/Mainland China	RMB126,000,000	50.3	–	Provision of testing services for IC products; designing, developing and selling IC testing software; production of probe cards; and the provision of research and consultancy services of IC technology
Shanghai Fudan Micro-electronics (HK) Limited	Hong Kong	HK\$7,000,000	100	–	Developing and selling IC products
Shanghai Fukong Hualong Micro-system Technology Co., Ltd. (“Fukong Hualong”) **	People’s Republic of China/Mainland China	RMB40,000,000	38.25	–	Designing, developing and selling products of MicroSystem and application-specific IC and software; the provision of investment, investment management and consultancy services; as well as the provision of research and consultancy services of MicroSystem technology
Shenzhen Fudan Microelectronics Company Limited (“SZFM”) ***	People’s Republic of China/Mainland China	RMB5,000,000	100	–	Designing, developing and selling IC products
Beijing Fudan Microelectronics Technology Co., Ltd. (“BJFM”) ***	People’s Republic of China/Mainland China	RMB3,000,000	100	–	Designing, developing and selling IC products

Notes to Financial Statements

31 December 2016

1. CORPORATE AND GROUP INFORMATION *(continued)*

Information about subsidiaries *(continued)*

Particulars of the subsidiaries are as follows: *(continued)*

Name	Place of incorporation/ registration and place of operations	Issued ordinary/ registered share capital	Percentage of equity directly attributable to the Company		Principal activities
			Direct	Indirect	
Shanghai Doublepoint Information Technology Co., Ltd. ("Doublepoint")****	People's Republic of China/Mainland China	RMB9,700,000	61.9	-	Provision of research and consultancy services in computer and network technology area; developing and selling hardware and software of computers, electronic products, and communication equipment; designing, manufacturing and agency services for advertising; and electronic commerce
Fudan Microelectronics (USA) Inc.*****	USA	USD100	-	100	Developing and selling IC products

* Sino IC is registered as a contractual joint venture company under PRC law. Sino IC is treated as a subsidiary, as the Company has unilateral control directly over Sino IC. In April 2014, Sino IC increased its issued capital from 31,000,000 shares to 42,000,000 shares, of which the Company subscribed and paid up 1,006,000 shares. Upon completion of the capital injection, the Company's shareholding in the equity interest of Sino IC decreased from 64.9% to 50.3%. In 2016, Sino IC increased its share capital from 84,000,000 shares to 126,000,000 shares by transferring RMB42,000,000 out of the retained earnings to the share capital.

** Fukong Hualong is a subsidiary of the Company acquired during 2008, which is registered as a contractual joint venture company under PRC law. In December 2016, Fukong Hualong increased its issued capital from 30,000,000 shares to 40,000,000 shares, of which the Company subscribed nil shares. Upon completion of the capital injection, the Company's equity holding in Fukong Hualong decreased from 51% to 38.25%. The new equity holder, which holds a 25% equity interest in Fukong Hualong, has agreed to act in concert with the Company over Fukong Hualong's operating, investing and financing decisions. The directors of the Company consider that Fukong Hualong is under the unilateral control of the Group and regarded as a subsidiary of the Company which is consolidated in the Group's financial statements. Fukong Hualong was not audited by Ernst & Young, Hong Kong or another member firm of the Ernst & Young global network.

*** SZFM and BJFM are wholly-owned subsidiaries of the Company established in 2007. Both of them are registered as limited liability companies under PRC law. None of the companies was audited by Ernst & Young, Hong Kong or another member firm of the Ernst & Young global network.

**** Upon completion of the capital injection on 25 January 2013 and change of registration with the authority on 25 February 2013, Doublepoint changed from an associate with 26.4% of equity interests held by the Company into a subsidiary of the Company, as the Group/Company has unilateral control directly over Doublepoint. On 15 March 2017, the shareholders of Doublepoint passed a resolution for the dissolution of Doublepoint. Doublepoint was not audited by Ernst & Young, Hong Kong or another member firm of the Ernst & Young global network.

***** Fudan Microelectronics (USA) Inc. is a wholly owned subsidiary incorporated in 2016.

Notes to Financial Statements

31 December 2016

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards (“HKFRSs”) (which include all Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards (“HKASs”) and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”), accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention. These financial statements are presented in Renminbi (“RMB”) and all values are rounded to the nearest thousand except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries (collectively referred to as the “Group”) for the year ended 31 December 2016. A subsidiary is an entity (including a structured entity), directly or indirectly, controlled by the Company. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee (i.e., existing rights that give the Group the current ability to direct the relevant activities of the investee).

When the Company has, directly or indirectly, less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- (a) the contractual arrangement with the other vote holders of the investee;
- (b) rights arising from other contractual arrangements; and
- (c) the Group’s voting rights and potential voting rights.

The financial statements of the subsidiaries are prepared for the same reporting period as the Company, using consistent accounting policies. The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases.

Profit or loss and each component of other comprehensive income are attributed to the owners of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control described above. A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises (i) the assets (including goodwill) and liabilities of the subsidiary, (ii) the carrying amount of any non-controlling interest and (iii) the cumulative translation differences recorded in equity; and recognises (i) the fair value of the consideration received, (ii) the fair value of any investment retained and (iii) any resulting surplus or deficit in profit or loss. The Group’s share of components previously recognised in other comprehensive income is reclassified to profit or loss or retained profits, as appropriate, on the same basis as would be required if the Group had directly disposed of the related assets or liabilities.

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES

The Group has adopted the following new and revised HKFRSs for the first time for the current year's financial statements.

Amendments to HKFRS 10, HKFRS 12 and HKAS 28 (2011)	<i>Investment Entities: Applying the Consolidation Exception</i>
Amendments to HKFRS 11 HKFRS 14	<i>Accounting for Acquisitions of Interests in Joint Operations</i> <i>Regulatory Deferral Accounts</i>
Amendments to HKAS 1	<i>Disclosure Initiative</i>
Amendments to HKAS 16 and HKAS 38	<i>Clarification of Acceptable Methods of Depreciation and Amortisation</i>
Amendments to HKAS 16 and HKAS 41	<i>Agriculture: Bearer Plants</i>
Amendments to HKAS 27 (2011)	<i>Equity Method in Separate Financial Statements</i>
<i>Annual Improvements 2012-2014 Cycle</i>	Amendments to a number of HKFRSs

Except for the amendments to HKFRS 10, HKFRS 12 and HKAS 28 (2011), amendments to HKFRS 11, HKFRS 14, amendments to HKAS 16 and HKAS 41, amendments to HKAS 27 (2011), and amendments included in the Annual Improvements 2012-2014 Cycle, which are not relevant to the preparation of the Group's financial statements, the nature and the impact of the amendments are described below:

- (a) Amendments to HKAS 1 include narrow-focus improvements in respect of the presentation and disclosure in financial statements. The amendments clarify:
- (i) the materiality requirements in HKAS 1;
 - (ii) that specific line items in the statement of profit or loss and the statement of financial position may be disaggregated;
 - (iii) that entities have flexibility as to the order in which they present the notes to financial statements; and
 - (iv) that the share of other comprehensive income of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statement of profit or loss. The amendments have had no significant impact on the Group's financial statements.

- (b) Amendments to HKAS 16 and HKAS 38 clarify the principle in HKAS 16 and HKAS 38 that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is part) rather than the economic benefits that are consumed through the use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets. The amendments are applied prospectively. The amendments have had no impact on the financial position or performance of the Group as the Group has not used a revenue-based method for the calculation of depreciation of its non-current assets.

Notes to Financial Statements

31 December 2016

2.3 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in these financial statements.

Amendments to HKFRS 2	<i>Classification and Measurement of Share-based Payment Transactions²</i>
Amendments to HKFRS 4	<i>Applying HKFRS 9 Financial Instruments with HKFRS 4 Insurance Contracts²</i>
HKFRS 9	<i>Financial Instruments²</i>
Amendments to HKFRS 10 and HKAS 28 (2011)	<i>Sale or Contribution of Assets between an Investor and its Associate or Joint Venture⁴</i>
HKFRS 15	<i>Revenue from Contracts with Customers²</i>
Amendments to HKFRS 15	<i>Clarifications to HKFRS 15 Revenue from Contracts with Customers²</i>
HKFRS 16	<i>Leases³</i>
Amendments to HKAS 7	<i>Disclosure Initiative¹</i>
Amendments to HKAS 12	<i>Recognition of Deferred Tax Assets for Unrealised Losses¹</i>
Annual Improvements 2014-2016 Cycle	<i>Amendments to HKFRS 12 Disclosure of Interests in Other Entities¹</i>
Annual Improvements 2014-2016 Cycle	<i>Amendments to HKFRS 1 First-time Adoption of Hong Kong Financial Reporting Standards²</i>
Annual Improvements 2014-2016 Cycle	<i>Amendments to HKAS 28 Investments in Associates and Joint Ventures²</i>

¹ Effective for annual periods beginning on or after 1 January 2017

² Effective for annual periods beginning on or after 1 January 2018

³ Effective for annual periods beginning on or after 1 January 2019

⁴ No mandatory effective date yet determined but available for adoption

Further information about those HKFRSs that are expected to be applicable to the Group is as follows:

The HKICPA issued amendments to HKFRS 2 in August 2016 that address three main areas: the effects of vesting conditions on the measurement of a cash-settled share-based payment transaction; the classification of a share-based payment transaction with net settlement features for withholding a certain amount in order to meet the employee's tax obligation associated with the share-based payment; and accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash-settled to equity-settled. The amendments clarify that the approach used to account for vesting conditions when measuring equity-settled share-based payments also applies to cash-settled share-based payments. The amendments introduce an exception so that a share-based payment transaction with net share settlement features for withholding a certain amount in order to meet the employee's tax obligation is classified in its entirety as an equity-settled share-based payment transaction when certain conditions are met. Furthermore, the amendments clarify that if the terms and conditions of a cash-settled share-based payment transaction are modified, with the result that it becomes an equity-settled share-based payment transaction, the transaction is accounted for as an equity-settled transaction from the date of the modification. The Group expects to adopt the amendments from 1 January 2018. The amendments are not expected to have any significant impact on the Group's financial statements.

2.3 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS *(continued)*

In September 2014, the HKICPA issued the final version of HKFRS 9, bringing together all phases of the financial instruments project to replace HKAS 39 and all previous versions of HKFRS 9. The standard introduces new requirements for classification and measurement, impairment and hedge accounting. The Group expects to adopt HKFRS 9 from 1 January 2018. The Group is currently assessing the impact of the standard.

Amendments to HKFRS 10 and HKAS 28 (2011) address an inconsistency between the requirements in HKFRS 10 and in HKAS 28 (2011) in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The amendments require a full recognition of a gain or loss when the sale or contribution of assets between an investor and its associate or joint venture constitutes a business. For a transaction involving assets that do not constitute a business, a gain or loss resulting from the transaction is recognised in the investor's profit or loss only to the extent of the unrelated investor's interest in that associate or joint venture. The amendments are to be applied prospectively. The previous mandatory effective date of amendments to HKFRS 10 and HKAS 28 (2011) was removed by the HKICPA in January 2016 and a new mandatory effective date will be determined after the completion of a broader review of accounting for associates and joint ventures. However, the amendments are available for application now.

HKFRS 15 establishes a new five-step model to account for revenue arising from contracts with customers. Under HKFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The principles in HKFRS 15 provide a more structured approach for measuring and recognising revenue. The standard also introduces extensive qualitative and quantitative disclosure requirements, including disaggregation of total revenue, information about performance obligations, changes in contract asset and liability account balances between periods and key judgements and estimates. The standard will supersede all current revenue recognition requirements under HKFRSs. In June 2016, the HKICPA issued amendments to HKFRS 15 to address the implementation issues on identifying performance obligations, application guidance on principal versus agent and licences of intellectual property, and transition. The amendments are also intended to help ensure a more consistent application when entities adopt HKFRS 15 and decrease the cost and complexity of applying the standard. The Group expects to adopt HKFRS 15 on 1 January 2018 and is currently assessing the impact of HKFRS 15 upon adoption.

HKFRS 16 replaces HKAS 17 *Leases*, HK(IFRIC)-Int 4 *Determining whether an Arrangement contains a Lease*, HK(SIC)-Int 15 *Operating Leases – Incentives* and HK(SIC)-Int 27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. The standard sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to recognise assets and liabilities for most leases. The standard includes two recognition exemptions for lessees – leases of low-value assets and short-term leases. At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). The right-of-use asset is subsequently measured at cost less accumulated depreciation and any impairment losses unless the right-of-use asset meets the definition of investment property in HKAS 40. The lease liability is subsequently increased to reflect the interest on the lease liability and reduced for the lease payments. Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset. Lessees will also be required to remeasure the lease liability upon the occurrence of certain events, such as change in the lease term and change in future lease payments resulting from a change in an index or rate used to determine those payments. Lessees will generally recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset. Lessor accounting under HKFRS 16 is substantially unchanged from the accounting under HKAS 17. Lessors will continue to classify all leases using the same classification principle as in HKAS 17 and distinguish between operating leases and finance leases. The Group expects to adopt HKFRS 16 on 1 January 2019 and is currently assessing the impact of HKFRS 16 upon adoption.

2.3 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS *(continued)*

Amendments to HKAS 7 require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. The amendments will result in additional disclosure to be provided in the financial statements. The Group expects to adopt the amendments from 1 January 2017.

Amendments to HKAS 12 were issued with the purpose of addressing the recognition of deferred tax assets for unrealised losses related to debt instruments measured at fair value, although they also have a broader application for other situations. The amendments clarify that an entity, when assessing whether taxable profits will be available against which it can utilise a deductible temporary difference, needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount. The Group expects to adopt the amendments from 1 January 2017.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business combinations and goodwill

Business combinations are accounted for using the acquisition method. The consideration transferred is measured at the acquisition date fair value which is the sum of the acquisition date fair values of assets transferred by the Group, liabilities assumed by the Group to the former owners of the acquiree and the equity interests issued by the Group in exchange for control of the acquiree. For each business combination, the Group elects whether to measure the non-controlling interests in the acquiree that are present ownership interests and entitle their holders to a proportionate share of net assets in the event of liquidation at fair value or at the proportionate share of the acquiree's identifiable net assets. All other components of non-controlling interests are measured at fair value. Acquisition-related costs are expensed as incurred.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts of the acquiree.

If the business combination is achieved in stages, the previously held equity interest is remeasured at its acquisition date fair value and any resulting gain or loss is recognised in profit or loss.

Any contingent consideration to be transferred by the acquirer is recognised at fair value at the acquisition date. Contingent consideration classified as an asset or liability is measured at fair value with changes in fair value recognised in profit or loss. Contingent consideration that is classified as equity is not remeasured and subsequent settlement is accounted for within equity.

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred, the amount recognised for non-controlling interests and any fair value of the Group's previously held equity interests in the acquiree over the identifiable net assets acquired and liabilities assumed. If the sum of this consideration and other items is lower than the fair value of the net assets acquired, the difference is, after reassessment, recognised in profit or loss as a gain on bargain purchase.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Business combinations and goodwill *(continued)*

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. The Group performs its annual impairment test of goodwill as at 31 December. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised. An impairment loss recognised for goodwill is not reversed in a subsequent period.

Where goodwill has been allocated to a cash-generating unit (or group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on the disposal. Goodwill disposed of in these circumstances is measured based on the relative value of the operation disposed of and the portion of the cash-generating unit retained.

Impairment of non-financial assets

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories, deferred tax assets and financial assets), the asset's recoverable amount is estimated. An asset's recoverable amount is the higher of the asset's or cash-generating unit's value in use and its fair value less costs of disposal, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to profit or loss in the period in which it arises in those expense categories consistent with the function of the impaired asset.

An assessment is made at the end of each reporting period as to whether there is an indication that previously recognised impairment losses may no longer exist or may have decreased. If such an indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, but not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation) had no impairment loss been recognised for the asset in prior years. A reversal of such an impairment loss is credited to the statement of profit or loss in the period in which it arises.

Notes to Financial Statements

31 December 2016

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Related parties

A party is considered to be related to the Group if:

- (a) the party is a person or a close member of that person's family and that person
 - (i) has control or joint control over the Group;
 - (ii) has significant influence over the Group; or
 - (iii) is a member of the key management personnel of the Group or of a parent of the Group; or
- (b) the party is an entity where any of the following conditions applies:
 - (i) the entity and the Group are members of the same group;
 - (ii) one entity is an associate or joint venture of the other entity (or of a parent, subsidiary or fellow subsidiary of the other entity);
 - (iii) the entity and the Group are joint ventures of the same third party;
 - (iv) one entity is a joint venture of a third entity and the other entity is an associate of the third entity;
 - (v) the entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group;
 - (vi) the entity is controlled or jointly controlled by a person identified in (a);
 - (vii) a person identified in (a) (i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity); and
 - (viii) the entity, or any member of a group of which it is a part, provides key management personnel services to the Group or to the parent of the Group.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. When an item of property, plant and equipment is classified as held for sale or when it is part of a disposal group classified as held for sale, it is not depreciated and is accounted for in accordance with HKFRS 5. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to profit or loss in the period in which it is incurred. In situations where the recognition criteria are satisfied, the expenditure for a major inspection is capitalised in the carrying amount of the asset as a replacement. Where significant parts of property, plant and equipment are required to be replaced at intervals, the Group recognises such parts as individual assets with specific useful lives and depreciates them accordingly.

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful life. The principal annual rates used for this purpose are as follows:

Land and buildings	1.9%
Machinery and office equipment	19%-33%
Motor vehicles	19%

Where parts of an item of property, plant and equipment have different useful lives, the cost of that item is allocated on a reasonable basis among the parts and each part is depreciated separately. Residual values, useful lives and the depreciation method are reviewed, and adjusted if appropriate, at least at each financial year end.

An item of property, plant and equipment including any significant part initially recognised is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in profit or loss in the year the asset is derecognised is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress represents machinery and other items of property, plant and equipment under construction or installation, which are stated at cost less any impairment losses, and are not depreciated. Cost comprises the direct costs of construction, installation and testing during the period of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Intangible assets (other than goodwill)

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value at the date of acquisition. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are subsequently amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year end.

Changes in the expected useful life or expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in profit or loss in the expense category consistent with the function of the intangible asset.

Research and development costs

All research costs are charged to the statement of profit or loss as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development. Product development expenditure which does not meet these criteria is expensed when incurred.

Deferred development costs are stated at cost less any impairment losses and are amortised using the straight-line basis over the expected commercial lives of the underlying products not exceeding three years, commencing from the date when the products are put into commercial production.

Operating leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessee, rentals payable under operating leases net of any incentives received from the lessor are charged to profit or loss on the straight-line basis over the lease terms.

Investments and other financial assets

Initial recognition and measurement

Financial assets are classified, at initial recognition, as loans and receivables and available-for-sale financial investments, as appropriate. When financial assets are recognised initially, they are measured at fair value plus transaction costs that are attributable to the acquisition of the financial assets, except in the case of financial assets recorded at fair value through profit or loss.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Investments and other financial assets *(continued)*

Subsequent measurement

The subsequent measurement of financial assets depends on their classification as follows:

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such assets are subsequently measured at amortised cost using the effective interest rate method less any allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and includes fees or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in other income and gains in the statement of profit or loss. The loss arising from impairment is recognised in the statement of profit or loss in finance costs for loans and in other expenses for receivables.

Available-for-sale financial investments

Available-for-sale financial investments are non-derivative financial assets in listed and unlisted equity investments and debt securities. Equity investments classified as available for sale are those which are neither classified as held for trading nor designated as at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in market conditions.

After initial recognition, available-for-sale financial investments are subsequently measured at fair value, with unrealised gains or losses recognised as other comprehensive income in the available-for-sale investment revaluation reserve until the investment is derecognised, at which time the cumulative gain or loss is recognised in the statement of profit or loss in other income, or until the investment is determined to be impaired, when the cumulative gain or loss is reclassified from the available-for-sale investment revaluation reserve to the statement of profit or loss in other gains or losses. Interest and dividends earned whilst holding the available-for-sale financial investments are reported as interest income and dividend income, respectively and are recognised in the statement of profit or loss as other income in accordance with the policies set out for "Revenue recognition" below.

When the fair value of unlisted equity investments cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such investments are stated at cost less any impairment losses.

The Group evaluates whether the ability and intention to sell its available-for-sale financial assets in the near term are still appropriate. When, in rare circumstances, the Group is unable to trade these financial assets due to inactive markets, the Group may elect to reclassify these financial assets if management has the ability and intention to hold the assets for the foreseeable future or until maturity.

For a financial asset reclassified from the available-for-sale category, the fair value carrying amount at the date of reclassification becomes its new amortised cost and any previous gain or loss on that asset that has been recognised in equity is amortised to profit or loss over the remaining life of the investment using the effective interest rate. Any difference between the new amortised cost and the maturity amount is also amortised over the remaining life of the asset using the effective interest rate. If the asset is subsequently determined to be impaired, then the amount recorded in equity is reclassified to the statement of profit or loss.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e., removed from the Group's consolidated statement of financial position) when:

- the rights to receive cash flows from the asset have expired; or
- the Group has transferred its rights to receive cash flows from the asset, or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a "pass-through" arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if and to what extent it has retained the risk and rewards of ownership of the asset. When it has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the Group continues to recognise the transferred asset to the extent of the Group's continuing involvement. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Impairment of financial assets

The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. An impairment exists if one or more events that occurred after the initial recognition of the asset have an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that a debtor 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 observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial assets carried at amortised cost

For financial assets carried at amortised cost, the Group first assesses whether impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Impairment of financial assets *(continued)*

Financial assets carried at amortised cost (continued)

The amount of any impairment loss identified 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 yet been incurred). The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition).

The carrying amount of the asset is reduced through the use of an allowance account and the loss is recognised in the statement of profit or loss. Interest income continues to be accrued on the reduced carrying amount using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Loans and receivables together with any associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group.

If, in a subsequent period, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a write-off is later recovered, the recovery is credited to other expenses in the statement of profit or loss.

Assets carried at cost

If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument, 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 discounted at the current market rate of return for a similar financial asset. Impairment losses on these assets are not reversed.

Available-for-sale financial investments

For available-for-sale financial investments, the Group assesses at the end of each reporting period whether there is objective evidence that an investment or a group of investments is impaired.

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the statement of profit or loss, is removed from other comprehensive income and recognised in the statement of profit or loss.

In the case of equity investments classified as available for sale, objective evidence would include a significant or prolonged decline in the fair value of an investment below its cost. "Significant" is evaluated against the original cost of the investment and "prolonged" against the period in which the fair value has been below its original cost. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of profit or loss – is removed from other comprehensive income and recognised in the statement of profit or loss. Impairment losses on equity instruments classified as available for sale are not reversed through the statement of profit or loss. Increases in their fair value after impairment are recognised directly in other comprehensive income.

Notes to Financial Statements

31 December 2016

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Impairment of financial assets *(continued)*

Available-for-sale financial investments (continued)

The determination of what is “significant” or “prolonged” requires judgement. In making this judgement, the Group evaluates, among other factors, the duration or extent to which the fair value of an investment is less than its cost.

In the case of debt instruments classified as available for sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of profit or loss. Future interest income continues to be accrued based on the reduced carrying amount of the asset and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of finance income. Impairment losses on debt instruments are reversed through the statement of profit or loss if the subsequent increase in fair value of the instruments can be objectively related to an event occurring after the impairment loss was recognised in the statement of profit or loss.

Financial liabilities

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as loans and borrowings or other financial liabilities, as appropriate.

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings, net of directly attributable transaction costs.

The Group’s financial liabilities include trade and other payables and interest-bearing bank and other borrowings.

The subsequent measurement of financial liabilities depends on their classification as follows:

Loans and borrowings

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost, using the effective interest rate method unless the effect of discounting would be immaterial, in which case they are stated at cost. Gains and losses are recognised in the statement of profit or loss when the liabilities are derecognised as well as through the effective interest rate amortisation process.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in finance costs in the statement of profit or loss.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled, or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognised in the statement of profit or loss.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Cash and cash equivalents

For the purpose of the consolidated statement of cash flows, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments that are readily convertible into known amounts of cash, are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the consolidated statement of financial position, cash and bank balances comprise cash on hand and at banks, including term deposits and assets similar in nature to cash, which are not restricted as to use.

Income tax

Income tax comprises current and deferred tax. Income tax relating to items recognised outside profit or loss is recognised outside profit or loss, either in other comprehensive income or directly in equity.

Current tax assets and liabilities are measured at the amount expected to be recovered from or paid to the taxation authorities, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period, taking into consideration interpretations and practices prevailing in the countries in which the Group operates.

Deferred tax is provided, using the liability method, on all temporary differences at the end of the reporting period between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Notes to Financial Statements

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2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Income tax *(continued)*

Deferred tax liabilities are recognised for all taxable temporary differences, except:

- when the deferred tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, the carryforward of unused tax credits and any unused tax losses. Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, the carryforward of unused tax credits and unused tax losses can be utilised, except:

- when the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at the end of each reporting period and are recognised to the extent that it has become probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income on a systematic basis over the periods that the costs, which it is intended to compensate, are expensed.

Where the grant relates to an asset, the fair value is credited to a deferred income account and is released to the statement of profit or loss over the expected useful life of the relevant asset by equal annual instalments or deducted from the carrying amount of the asset and released to the statement of profit or loss by way of a reduced depreciation charge.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

- (a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;
- (b) from the rendering of services, in the period in which the services are rendered;
- (c) interest income, on an accrual basis using the effective interest method by applying the rate that exactly discounts the estimated future cash receipts over the expected life of the financial instrument or a shorter period, when appropriate, to the net carrying amount of the financial asset; and
- (d) dividend income, when the shareholders' right to receive payment has been established.

Pension schemes

The employees of the Company and its subsidiaries which operate in Mainland China are required to participate in a central pension scheme operated by the local municipal government. The Company and these subsidiaries are required to contribute 22% of their payroll costs to the central pension scheme. The contributions are charged to the statement of profit or loss as they become payable in accordance with the rules of the central pension scheme.

The Group's subsidiary in Hong Kong operates a defined contribution Mandatory Provident Fund retirement benefit scheme (the "MPF Scheme") under the Mandatory Provident Fund Schemes Ordinance for those employees who are eligible to participate in the MPF Scheme. Contributions are made based on a percentage of the employees' basic salaries and are charged to profit or loss as they become payable in accordance with the rules of the MPF Scheme. The assets of the MPF Scheme are held separately from those of the Group in an independently administered fund. The subsidiary's employer contributions vest fully with the employees when contributed into the MPF Scheme.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Dividends

Final dividends are recognised as a liability when they are approved by the shareholders in a general meeting.

Interim dividends are simultaneously proposed and declared, because the Company's memorandum and articles of association grant the directors the authority to declare interim dividends. Consequently, interim dividends are recognised immediately as a liability when they are proposed and declared.

Foreign currencies

These financial statements are presented in RMB, which is the Company's functional currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions recorded by the entities in the Group are initially recorded using their respective functional currency rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rates of exchange ruling at the end of the reporting period. Differences arising on settlement or translation of monetary items are recognised in the statement of profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was measured. The gain or loss arising on translation of a non-monetary item measured at fair value is treated in line with the recognition of the gain or loss on change in fair value of the item. (i.e., translation difference on the item whose fair value gain or loss is recognised in other comprehensive income or profit or loss is also recognised in other comprehensive income or profit or loss, respectively).

The functional currency of the Group's subsidiary in Hong Kong is the Hong Kong dollar. As at the end of the reporting period, the assets and liabilities of the entity are translated into RMB at the exchange rate prevailing at the end of the reporting period and its statement of profit and loss is translated into RMB at the weighted average exchange rate for the year. The resulting exchange differences are recognised in other comprehensive income and accumulated in the exchange fluctuation reserve. On disposal of a foreign operation, the component of other comprehensive income relating to that particular foreign operation is recognised in the statement of profit or loss.

For the purpose of the consolidated statement of cash flows, the cash flows of the overseas subsidiary are translated into RMB at the exchange rates prevailing at the dates of the cash flows. Frequently recurring cash flows of the overseas subsidiary which arise throughout the year are translated into RMB at the weighted average exchange rate for the year.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and their accompanying disclosures, and the disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amounts of the assets or liabilities affected in the future.

Judgements

In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect on the amounts recognised in the financial statements.

Research and development costs

The Group determines whether costs of research and development qualify for capitalisation, and has developed criteria in making that judgement. Therefore, the Group considers whether costs of research and development to be capitalised generates future cash flows, and whether the Group has the technical feasibility of completing the development so that the item under research and development will be available for use or sale and the Group has the intention to complete the development. The Group also considers the ability in measuring development expenditure during the development.

Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below.

Deferred tax assets

Deferred tax assets are recognised for unused tax losses and other temporary differences to the extent that it is probable that taxable profit will be available against which the losses and differences can be utilised. 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 together with future tax planning strategies. The amount of unrecognised tax losses at 31 December 2016 was RMB24,658,000 (2015: RMB24,820,000). Further details are contained in note 9 to the financial statements.

Impairment of financial assets carried at cost

The unquoted equity instrument that is not carried at fair value because of its fair value cannot be reliably measured is stated at cost less any impairment losses. The amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. This evaluation requires the Group to make estimates about expected future cash flows and discount rates, and hence they are subject to uncertainty. Further details are included in note 14 to the financial statements.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES *(continued)*

Estimation uncertainty *(continued)*

Impairment of non-financial assets

The Group assesses whether there are any indicators of impairment for all non-financial assets at the end of each reporting period. Non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable. An impairment exists when the carrying value of an asset or a cash-generating unit exceeds its recoverable amount, which is the higher of its fair value less costs of disposal and its value in use. The calculation of the fair value less costs of disposal is based on available data from binding sales transactions in an arm's length transaction of similar assets or observable market prices less incremental costs for disposing of the asset. When value in use calculations are undertaken, management must estimate the expected future cash flows from the asset or cash-generating unit and choose a suitable discount rate in order to calculate the present value of those cash flows.

Impairment of trade receivables

The Group records impairment of trade receivables based on an assessment of the recoverability of trade and bills receivables. The identification of doubtful debts requires directors' estimates. Where the expectation is different from the original estimate, such difference will impact the carrying values of the trade receivables and doubtful debt expenses in the period in which such estimates have been changed. Further details are contained in note 16 to the financial statements.

Useful lives of property, plant and equipment

The Group determines the useful lives of property, plant and equipment based on an assessment of the expected useful lives or expected pattern of consumption of future economic benefits embodied in the assets. The determination of a reasonable useful life requires directors' estimates. Where the expectation is different from the original estimate, such difference will impact on the carrying value of the property, plant and equipment and the depreciation expenses in the period in which such estimates have been changed.

Useful lives of intangible assets

The Group determines the useful lives of intangible assets based on an assessment of the expected useful lives or expected pattern of consumption of future economic benefits embodied in the assets. The determination of a reasonable useful life requires directors' estimates. Where the expectation is different from the original estimate, such difference will impact on the carrying value of the intangible assets and the amortisation expenses in the period in which such estimates have been changed.

Provisions for inventories to net realisable value and slow-moving

The Group writes down inventories to net realisable value based on an assessment of the realisability of inventories and makes provision for slow-moving inventories based on the analysis of inventories turnover and their historical and subsequent usage or sales. The assessment of write-down and provision for slow-moving inventories requires directors' estimates. Where the expectation is different from the original estimate, such difference will impact on the carrying value of the inventories and write-down of inventories in the period in which such estimates have been changed. Further details are contained in note 15 to the financial statements.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES *(continued)*

Estimation uncertainty *(continued)*

Deferred development cost

Development costs are capitalised in accordance with the accounting policy for research and development costs in note 2.4 to the financial statements. Determining the amounts to be capitalised requires management to make assumptions regarding the expected future cash flows generated from the assets, discount rates to be applied and the expected period of benefits. Further details are contained in note 13 to the financial statements.

4. OPERATING SEGMENT INFORMATION

For management purposes, the Group is organised into business units based on their products and services and has two reportable operating segments as follows:

- the design, development and sale of IC products segment (“Design, development and sale of IC products”); and
- the provision of testing services for IC products segment (“Testing services for IC products”).

Management monitors the results of the Group’s operating segments separately for the purpose of making decisions about resources allocation and performance assessment. Segment performance is evaluated based on reportable segment profit before tax. The segment profit before tax is measured consistently with the Group’s profit before tax except that interest income and other unallocated income and gains are excluded from such measurement.

Segment assets exclude deferred tax assets, corporate and other unallocated assets as these assets are managed on a group basis.

Segment liabilities exclude deferred tax liabilities, corporate and other unallocated liabilities as these liabilities are managed on a group basis.

Intersegment sales and transfers are transacted with reference to the selling prices used for sales made to third parties at the then prevailing market prices.

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4. OPERATING SEGMENT INFORMATION (continued)

Year ended 31 December 2016	Design, development and sale of IC products RMB'000	Testing services for IC products RMB'000	Total RMB'000
Segment revenue:			
Sales to external customers	1,104,382	83,108	1,187,490
Intersegment sales	–	41,943	41,943
	1,104,382	125,051	1,229,433
<i>Reconciliation:</i>			
Elimination of intersegment sales			(41,943)
Revenue			1,187,490
Segment results	177,676	69,806	247,482
<i>Reconciliation:</i>			
Elimination of intersegment results			(10,038)
Interest income			9,169
Unallocated other income and gains			13,244
Profit before tax			259,857
Segment assets	1,401,681	366,083	1,767,764
<i>Reconciliation:</i>			
Elimination of intersegment receivables			(7,868)
Corporate and other unallocated assets			42,972
Total assets			1,802,868
Segment liabilities	335,031	101,273	436,304
<i>Reconciliation:</i>			
Elimination of intersegment payables			(7,868)
Total liabilities			428,436
Other segment information:			
Impairment loss recognised in the statement of profit or loss	52,500	288	52,788
Impairment loss reversed in the statement of profit or loss	(7,322)	(166)	(7,488)
Depreciation	24,250	43,805	68,055
Amortisation of intangible assets	44,417	–	44,417
Capital expenditure*	97,590	20,270	117,860

* Capital expenditure consists of additions to property, plant and equipment and intangible assets.

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4. OPERATING SEGMENT INFORMATION (continued)

Year ended 31 December 2015	Design, development and sale of IC products RMB'000	Testing services for IC products RMB'000	Total RMB'000
Segment revenue:			
Sales to external customers	972,782	66,943	1,039,725
Intersegment sales	–	41,056	41,056
	972,782	107,999	1,080,781
<i>Reconciliation:</i>			
Elimination of intersegment sales			(41,056)
Revenue			1,039,725
Segment results	140,534	43,732	184,266
<i>Reconciliation:</i>			
Elimination of intersegment results			(9,632)
Interest income			7,950
Unallocated other income and gains			10,741
Profit before tax			193,325
Segment assets	1,190,448	298,227	1,488,675
<i>Reconciliation:</i>			
Elimination of intersegment receivables			(8,476)
Corporate and other unallocated assets			38,264
Total assets			1,518,463
Segment liabilities	319,466	93,887	413,353
<i>Reconciliation:</i>			
Elimination of intersegment payables			(8,476)
Total liabilities			404,877
Other segment information:			
Impairment loss recognised in the statement of profit or loss	28,734	433	29,167
Impairment loss reversed in the statement of profit or loss	(1,191)	(86)	(1,277)
Depreciation	20,082	20,624	40,706
Amortisation of intangible assets	26,042	–	26,042
Capital expenditure*	103,519	53,109	156,628

* Capital expenditure consists of additions to property, plant and equipment and intangible assets.

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4. OPERATING SEGMENT INFORMATION *(continued)*

Geographical information

(a) Revenue from external customers

	2016 RMB'000	2015 RMB'000
Mainland China	1,136,058	1,020,367
Asia Pacific (excluding Mainland China)	38,163	13,865
Others	13,269	5,493
	1,187,490	1,039,725

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

(b) Non-current assets

	2016 RMB'000	2015 RMB'000
Mainland China	448,240	492,651
Asia Pacific (excluding Mainland China)	9	5
	448,249	492,656

The non-current asset information above is based on the locations of the assets and excludes deferred tax assets.

Information about a major customer

In 2016, revenue of approximately RMB164,651,000 was derived from sales by the design, development and sale of IC products segment to a single customer, which contributed 10% or more to the Group's revenue.

In 2015, revenue of approximately RMB187,465,000 was derived from sales by the design, development and sale of IC products segment to a single customer, which contributed 10% or more to the Group's revenue.

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5. REVENUE, OTHER INCOME AND GAINS

Revenue represents the net invoiced value of goods sold, after allowances for returns and trade discounts, and the value of services rendered during the year.

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

	2016 RMB'000	2015 RMB'000
Revenue		
Sale of goods	1,104,382	972,782
Rendering of services	83,108	66,943
	1,187,490	1,039,725
Other income and gains		
Bank interest income (note 6)	9,169	7,950
Government grants received for research activities (note 6)	93,966	61,733
Other government grants (note 6)	13,244	10,741
Others	46,606	2,656
	162,985	83,080

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6. PROFIT BEFORE TAX

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

	2016 RMB'000	2015 RMB'000
Cost of inventories sold	519,095	468,911
Cost of services provided	37,103	20,505
Depreciation (note 12)	68,055	40,706
Research and development costs:		
Deferred development costs amortised* (note 13)	44,417	26,042
Current year expenditure	345,284	248,739
Less: Government grants received for research activities** (note 5)	(93,966)	(61,733)
	295,735	213,048
Minimum lease payments under operating leases	12,454	11,631
Auditor's remuneration	1,576	1,199
Employee benefit expense (excluding directors' and chief executive's remuneration (note 7)):		
Wages and salaries	225,885	193,809
Pension scheme contributions	25,787	23,204
	251,672	217,013
Less: Amounts capitalised as development costs	(55,601)	(58,072)
	196,071	158,941
Foreign exchange differences, net	477	2,265
Impairment of intangible assets (note 13)	36,126	16,389
Impairment/(reversal) of impairment of trade and bills receivables (note 16)	(3,621)	3,540
Write-down of inventories to net realisable value	12,795	7,912
Write off/loss on disposal of items of property, plant and equipment and intangible assets	13,553	8,194
Bank interest income (note 5)	(9,169)	(7,950)
Other government grants (note 5)	(13,244)	(10,741)

* The amortisation of deferred development costs for the year is included in "Other expenses" on the face of the consolidated statement of profit or loss.

** Various government grants have been received for setting up research activities in Shanghai, Mainland China, to support domestic technology development. Conditions or contingencies relating to these grants are fulfilled and they are not deducted from the related costs which they are intended to compensate, but recorded in other income. Government grants received for which related expenditure has not yet been incurred or to which there were unfulfilled conditions are included in "Accruals, other payables and deferred income" in the consolidated statement of financial position.

7. DIRECTORS' AND CHIEF EXECUTIVE'S REMUNERATION

Directors' and chief executive's remuneration for the year, disclosed pursuant to the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "Listing Rules"), section 383(1)(a), (b), (c) and (f) of the Hong Kong Companies Ordinance and Part 2 of the Companies (Disclosure of Information about Benefits of Directors) Regulation, is as follows:

	2016 RMB'000	2015 RMB'000
Fees	78	74
Other emoluments:		
Salaries, allowances and benefits in kind	7,371	5,093
Other benefits	108	108
Pension scheme contributions	42	40
	7,521	5,241
	7,599	5,315

(a) Independent non-executive directors

The fees and other benefits paid to independent non-executive directors during the year were as follows:

	Fees RMB'000	Other benefits received RMB'000	Total RMB'000
2016			
Mr. Cheung Wing Keung	78	–	78
Mr. Guo Li	–	36	36
Mr. Chen Baoying	–	36	36
Mr. Lin Fujiang	–	36	36
Total	78	108	186
2015			
Mr. Cheung Wing Keung	74	–	74
Mr. Guo Li	–	36	36
Mr. Chen Baoying	–	36	36
Mr. Lin Fujiang	–	36	36
Total	74	108	182

There were no other emoluments payable to the independent non-executive directors during the year (2015: Nil).

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7. DIRECTORS' AND CHIEF EXECUTIVE'S REMUNERATION *(continued)*

(b) Executive directors, non-executive directors and the chief executive

	Salaries, allowances and benefits in kind RMB'000	Pension scheme contributions RMB'000	Other benefits received RMB'000	Total remuneration RMB'000
2016				
Executive directors:				
Mr. Jiang Guoxing	300	—	—	300
Mr. Shi Lei	3,045	42	—	3,087
Mr. Yu Jun	2,697	—	—	2,697
Ms. Cheng Junxia	1,329	—	—	1,329
	7,371	42	—	7,413
Non-executive directors:				
Ms. Zhang Qianling	—	—	—	—
Mr. Ma Zhicheng	—	—	—	—
Mr. Yao Fuli	—	—	—	—
Ms. Zhang Huajing	—	—	—	—
	—	—	—	—
	7,371	42	—	7,413

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7. DIRECTORS' AND CHIEF EXECUTIVE'S REMUNERATION (continued)

(b) Executive directors, non-executive directors and the chief executive (continued)

	Salaries, allowances and benefits in kind RMB'000	Pension scheme contributions RMB'000	Other benefits received RMB'000	Total remuneration RMB'000
2015				
Executive directors:				
Mr. Jiang Guoxing	300	–	–	300
Mr. Shi Lei	1,887	40	–	1,927
Mr. Yu Jun	1,935	–	–	1,935
Ms. Cheng Junxia	971	–	–	971
	5,093	40		5,133
Non-executive directors:				
Ms. Zhang Qianling	–	–	–	–
Mr. He Lixing	–	–	–	–
Mr. Shen Xiaozu	–	–	–	–
Mr. Ma Zhicheng	–	–	–	–
Mr. Yao Fuli	–	–	–	–
Ms. Zhang Huajing	–	–	–	–
	–	–	–	–
	5,093	40	–	5,133

The Group and the Company's chief executive is Mr. Shi Lei, who is also an executive director of the Group and the Company.

There was no arrangement under which a director or the chief executive waived or agreed to waive any remuneration during the year.

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8. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included two directors and one chief executive (2015: one director and one chief executive), details of whose remuneration are set out in note 7 above. Details of the remuneration for the year of the remaining two (2015: three) highest paid employees who is neither a director nor chief executive of the Group are as follows:

	2016 RMB'000	2015 RMB'000
Salaries, allowances and benefits in kind	2,700	4,189
Pension scheme contributions	–	40
	2,700	4,229

The number of non-director and non-chief executive highest paid employees whose remuneration fell within the following bands is as follows:

	Number of employees	
	2016	2015
HK\$1,000,001 to HK\$1,500,000	–	–
HK\$1,500,001 to HK\$2,000,000	2	3
	2	3

During the year, no emoluments were paid by the Group to the directors and the chief executive or the non-director and non-chief executive highest paid employee either as an inducement to join the Group, or as compensation for loss of office.

9. INCOME TAX

Under the PRC Corporate Income Tax Law (the “CIT Law”), which became effective on 1 January 2008, the Company is subject to income tax at a base rate of 25%. The Company is eligible to a preferential income tax rate of 15% as a High New Technology Enterprise (“HNT Enterprise”). For the year ended 31 December 2015, income tax provision on assessable income of the Company was made at the rate of 15%. Pursuant to the notice of the State Council on “Issuing Several Policies on Further Encouraging the Development of the Software and Integrated Circuit Industries” (Guo Fa (2011) No. 4) and “Notice Concerning Several Policies on Enterprise Income Tax of Software and Integrated Circuit Industries” (Cai Shui (2016) No. 49) issued by the Ministry of Finance of the PRC, the Company was subsequently qualified as “key software enterprise falling within the State’s planned arrangement” for its 2015 annual tax filing. Accordingly, the Company enjoyed a preferential tax rate of 10% and received a tax refund which represented the difference between the paid amount according to original 15% corporate income tax rate and the aforesaid preferential tax rate of 10%. For the year ended 31 December 2016, income tax on assessable income of the Company has been provided at the rate of 15% as an HNT Enterprise.

Under the CIT Law, the Company’s subsidiary, Sino IC is subject to income tax at a base rate of 25%. Sino IC is entitled to a preferential income tax rate of 15% as an HNT Enterprise. For the financial year ended 31 December 2016, income tax on assessable income of Sino IC has been provided at the rate of 15% (2015: 15%).

Under the CIT Law, the Company’s subsidiary, Fukong Hualong is subject to income tax at a base rate of 25%. For the year ended 31 December 2016, Fukong Hualong is entitled to a preferential income tax rate of 15% as an HNT Enterprise, and therefore, income tax on assessable income of Fukong Hualong has been provided at the rate of 15% (2015: 15%).

Under the CIT Law, three of the Company’s subsidiaries, SZFM, BJFM and Doublepoint, are subject to income taxes at a base rate of 25%. For the year ended 31 December 2016, income taxes on assessable income of these subsidiaries have been provided at the rate of 25% (2015: 25%).

Hong Kong profits tax has been provided at the rate of 16.5% (2015: 16.5%) on the estimated assessable profits arising in Hong Kong during the year.

	2016 RMB'000	2015 RMB'000
Current – Hong Kong		
Charge for the year	–	(83)
Overprovision in prior years	(7)	–
Current – Mainland China		
Charge for the year	26,425	19,967
Overprovision in prior years	(1,943)	(22)
Deferred (note 9(c))	(4,708)	(4,527)
Total tax charge for the year	19,767	15,335

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9. INCOME TAX (continued)

(a) Income tax expense

A reconciliation of the tax expense applicable to profit before tax at the statutory rates for the countries/ jurisdictions in which the Company and the majority of its subsidiaries are domiciled to the tax expense at the effective tax rates, and a reconciliation of the applicable rates (i.e., the statutory tax rates) to the effective tax rates, are as follows:

2016

	Mainland China		Hong Kong		Total	
	RMB'000	%	RMB'000	%	RMB'000	%
Profit before tax	260,420		(563)		259,857	
Tax at the statutory tax rates	65,105	25.0	(93)	16.5	65,012	25.0
Lower tax rates enacted by local authority	(26,102)	(10.0)	-	-	(26,102)	(10.0)
Adjustment in respect of current tax of previous years						
– overprovisions	(1,943)	(0.7)	(7)	1.2	(1,950)	(0.8)
Accelerated deduction for research and development activities	(19,034)	(7.3)	-	-	(19,034)	(7.3)
Expenses not deductible for tax	1,289	0.5	-	-	1,289	0.5
Tax losses and temporary differences not recognised	459	0.1	93	(16.5)	552	0.2
Tax charge at the Group's effective rate	19,774	7.6	(7)	1.2	19,767	7.6

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9. INCOME TAX (continued)

(a) Income tax expense (continued)

2015

	Mainland China		Hong Kong		Total	
	RMB'000	%	RMB'000	%	RMB'000	%
Profit before tax	193,828		(503)		193,325	
Tax at the statutory tax rates	48,457	25.0	(83)	16.5	48,374	25.0
Lower tax rates enacted by local authority	(19,442)	(10.0)	-	-	(19,442)	(10.0)
Adjustment in respect of current tax of previous years						
– overprovisions	(22)	-	-	-	(22)	-
Accelerated deduction for research and development activities	(14,583)	(7.5)	-	-	(14,583)	(7.5)
Expenses not deductible for tax	770	0.4	-	-	770	0.4
Tax losses and temporary differences not recognised	155	-	83	(16.5)	238	-
Tax charge at the Group's effective rate	15,335	7.9	-	-	15,335	7.9

(b) Income tax payable in the consolidated statement of financial position represents:

	2016 RMB'000	2015 RMB'000
At beginning of year	13,369	12,705
Provision for the year	24,475	19,862
Hong Kong tax refunded/(paid) during the year	205	(112)
PRC tax paid during the year	(22,278)	(19,086)
At end of year	15,771	13,369

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9. INCOME TAX (continued)

(c) Deferred tax

The movements in deferred tax assets and liabilities during the year are as follows:

2016

Deferred tax assets

	At 1 January 2016 RMB'000	Deferred tax (charged)/ credited to the statement of profit or loss during the year RMB'000	Deferred tax assets at 31 December 2016 RMB'000
Inventories	294	(37)	257
Impairment of assets	10,686	4,621	15,307
Depreciation of property, plant and equipment, and amortisation of intangible assets	3,722	3,330	7,052
Government grants	20,363	(4,862)	15,501
Temporary differences related to accruals and other payables	3,709	1,146	4,855
Total	38,774	4,198	42,972

Deferred tax liabilities

	At 1 January 2016 RMB'000	Deferred tax credited to the statement of profit or loss during the year RMB'000	Deferred tax liabilities at 31 December 2016 RMB'000
Depreciation of property, plant and equipment	510	(510)	–

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9. INCOME TAX (continued)

(c) Deferred tax (continued)

The movements in deferred tax assets and liabilities during the year are as follows: (continued)

2016 (continued)

For presentation purposes, certain deferred tax assets and liabilities have been offset in the statement of financial position. The following is an analysis of the deferred tax balances of the Group for financial reporting purposes:

	RMB'000
Net deferred tax assets recognised in the consolidated statement of financial position	42,972
Net deferred tax liabilities recognised in the consolidated statement of financial position	-

2015

Deferred tax assets

	At 1 January 2015 RMB'000	Deferred tax (charged)/ credited to the statement of profit or loss during the year RMB'000	Deferred tax assets at 31 December 2015 RMB'000
Inventories	445	(151)	294
Impairment of assets	6,289	4,397	10,686
Depreciation of property, plant and equipment, and amortisation of intangible assets	2,921	801	3,722
Government grants	13,528	6,835	20,363
Temporary differences related to accruals and other payables	10,645	(6,936)	3,709
Total	33,828	4,946	38,774

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9. INCOME TAX (continued)

(c) Deferred tax (continued)

The movements in deferred tax assets and liabilities during the year are as follows: (continued)

2015 (continued)

Deferred tax liabilities

	At 1 January 2015 RMB'000	Deferred tax charged/ (credited) to the statement of profit or loss during the year RMB'000	Deferred tax liabilities at 31 December 2015 RMB'000
Deferred development costs	23	(23)	–
Depreciation of property, plant and equipment	68	442	510
Total	91	419	510

For presentation purposes, certain deferred tax assets and liabilities have been offset in the statement of financial position. The following is an analysis of the deferred tax balances of the Group for financial reporting purposes:

	RMB'000
Net deferred tax assets recognised in the consolidated statement of financial position	38,264
Net deferred tax liabilities recognised in the consolidated statement of financial position	–

9. INCOME TAX (continued)

(c) Deferred tax (continued)

Deferred tax assets have not been recognised in respect of the following items:

	2016 RMB'000	2015 RMB'000
Tax losses	4,518	4,354
Deductible temporary differences	527	139
	5,045	4,493

The Group has tax losses arising in Hong Kong of HK\$737,000 (2015: Nil) that are available indefinitely for offsetting against future taxable profits of the companies in which the losses arose. The Group has tax losses arising in Mainland China of RMB24,658,000 (2015: RMB24,820,000) that will expire in one to five years for offsetting against future taxable profits. Deferred tax assets have not been recognised in respect of the above items as they have arisen in subsidiaries that have been loss-making for some time and it is not considered probable that taxable profits will be available against which the tax losses and deductible temporary differences can be utilised.

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

10. DIVIDENDS

The board of directors did not propose any final dividend for the year.

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11. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The calculation of the basic earnings per share amount is based on the profit for the year attributable to ordinary equity holders of the parent, and the weighted average number of ordinary shares of 617,330,000 (2015: 617,330,000) in issue during the year.

The calculation of the basic earnings per share is based on:

	2016 RMB'000	2015 RMB'000
Earnings		
Profit attributable to ordinary equity holders of the parent, used in the basic earnings per share calculation	212,258	158,898
	Number of shares '000	
	2016	2015
Shares		
Weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculation	617,330	617,330

The Group had no potentially dilutive ordinary shares in issue during the two years ended 31 December 2016 and 2015. The diluted earnings per share amount is the same as the basic earnings per share amount.

12. PROPERTY, PLANT AND EQUIPMENT

31 December 2016

	Land and buildings RMB'000	Machinery and office equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
At 31 December 2015 and at 1 January 2016:					
Cost	79,608	296,086	7,544	139,407	522,645
Accumulated depreciation	(24,356)	(162,276)	(4,002)	–	(190,634)
Net carrying amount	55,252	133,810	3,542	139,407	332,011
At 1 January 2016, net of accumulated depreciation	55,252	133,810	3,542	139,407	332,011
Additions	554	20,991	2,069	21,424	45,038
Transfers	–	25,670	–	(25,670)	–
Disposals	–	(223)	(69)	–	(292)
Depreciation provided during the year	(4,999)	(62,166)	(890)	–	(68,055)
At 31 December 2016, net of accumulated depreciation	50,807	118,082	4,652	135,161	308,702
At 31 December 2016:					
Cost	80,162	338,394	9,430	135,161	563,147
Accumulated depreciation	(29,355)	(220,312)	(4,778)	–	(254,445)
Net carrying amount	50,807	118,082	4,652	135,161	308,702

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12. PROPERTY, PLANT AND EQUIPMENT *(continued)*

31 December 2015

	Land and buildings RMB'000	Machinery and office equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
At 1 January 2015:					
Cost	81,267	213,375	5,210	149,729	449,581
Accumulated depreciation	(22,370)	(127,625)	(3,951)	–	(153,946)
Net carrying amount	58,897	85,750	1,259	149,729	295,635
At 1 January 2015, net of accumulated depreciation					
Additions	1,305	10,129	2,997	62,745	77,176
Transfers	–	73,067	–	(73,067)	–
Disposals	–	(53)	(41)	–	(94)
Depreciation provided during the year	(4,950)	(35,083)	(673)	–	(40,706)
At 31 December 2015, net of accumulated depreciation	55,252	133,810	3,542	139,407	332,011
At 31 December 2015:					
Cost	79,608	296,086	7,544	139,407	522,645
Accumulated depreciation	(24,356)	(162,276)	(4,002)	–	(190,634)
Net carrying amount	55,252	133,810	3,542	139,407	332,011

13. INTANGIBLE ASSETS

	Deferred development costs RMB'000
31 December 2016	
Cost at 31 December 2015 and 1 January 2016, net of accumulated amortisation and impairment	160,645
Additions – internal development	72,822
Write-off – internal development	(13,377)
Impairment during the year	(36,126)
Amortisation provided during the year	(44,417)
At 31 December 2016	139,547
At 31 December 2016:	
Cost	321,169
Accumulated amortisation and impairment	(181,622)
Net carrying amount	139,547
31 December 2015	
Cost at 1 January 2015, net of accumulated amortisation and impairment	131,763
Additions – internal development	79,452
Write-off – internal development	(8,139)
Impairment during the year	(16,389)
Amortisation provided during the year	(26,042)
At 31 December 2015	160,645
At 31 December 2015:	
Cost	263,543
Accumulated amortisation and impairment	(102,898)
Net carrying amount	160,645

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14. AVAILABLE-FOR-SALE INVESTMENTS

	2016 RMB'000	2015 RMB'000
Unlisted equity investments, at cost	13,443	13,443
Impairment provision	(13,443)	(13,443)
	-	-

As at 31 December 2016, the unlisted equity investments with a carrying amount of RMB13,443,000 (2015: RMB13,443,000) were stated at cost less impairment, because the directors are of the opinion that the information to be applied in the valuation techniques cannot be obtained on a continuous basis so that their fair value cannot be measured reliably. The Group does not intend to dispose of them in the near future.

Included in the above impairment of available-for-sale investments is a provision for individually impaired available-for-sale investments of RMB13,443,000 (2015: RMB13,443,000) with a carrying amount before provision of RMB13,443,000 (2015: RMB13,443,000). The individually impaired available-for-sale investments related to investments from which a measurable decrease in estimated future cash flows is evidenced. The Group does not hold any collateral as security over these investments.

15. INVENTORIES

	2016 RMB'000	2015 RMB'000
Raw materials	123,458	92,922
Work in progress	72,999	58,139
Finished goods	84,155	63,049
	280,612	214,110

16. TRADE AND BILLS RECEIVABLES

	2016 RMB'000	2015 RMB'000
Trade and bills receivables	480,265	384,161
Impairment	(13,649)	(18,144)
	466,616	366,017

The Group's trading terms with its customers are mainly on credit, except for new customers, where payment in advance is normally required. The credit period is generally between 30 and 90 days. The Group's sales are made to several major customers and there is a concentration of credit risk. The Group seeks to maintain strict control over its outstanding receivables and closely monitors the collection to minimise credit risk. Overdue balances are reviewed regularly by senior management. The Group does not hold any collateral or other credit enhancements over these balances. Trade receivables are non-interest-bearing.

An aged analysis of the trade and bills receivables as at the end of the reporting period, based on the invoice date and net of provisions, is as follows:

	2016 RMB'000	2015 RMB'000
Within 3 months	379,442	291,858
3 to 6 months	74,466	48,152
6 to 12 months	10,448	3,397
Over 12 months	2,260	22,610
	466,616	366,017

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16. TRADE AND BILLS RECEIVABLES (continued)

The movements in provision for impairment of trade and bills receivables are as follows:

	2016 RMB'000	2015 RMB'000
At 1 January	18,144	14,629
Impairment losses recognised (note 6)	3,867	4,817
Impairment losses reversed (note 6)	(7,488)	(1,277)
Amount written off as uncollectible	(874)	(25)
	13,649	18,144

Included in the above provision for impairment of trade and bills receivables is a provision for individually impaired trade receivables of RMB1,628,000 (2015: RMB5,830,000) with a carrying amount before provision of RMB1,628,000 (2015: RMB5,830,000). The individually impaired trade and bills receivables relate to customers that were in financial difficulties and are not expected to be recovered.

The aged analysis of the trade and bills receivables that are not individually nor collectively considered to be impaired is as follows:

	2016 RMB'000	2015 RMB'000
Neither past due nor impaired	374,100	128,134
Less than 1 month past due	32,170	67,228
1 to 3 months past due	30,406	15,056
	436,676	210,418

Receivables that were neither past due nor impaired relate to certain major customers and a number of diversified customers for whom there was no recent history of default.

Receivables that were past due but not impaired relate to a number of independent customers that have a good track record with the Group. Based on past experience, the directors of the Company are of the opinion that no provision for impairment is necessary in respect of these balances as there has not been a significant change in credit quality and the balances are still considered fully recoverable.

16. TRADE AND BILLS RECEIVABLES *(continued)*

At 31 December 2016, the Group endorsed certain bills receivable accepted by banks in Mainland China (the “Derecognised Bills”) to certain of its suppliers in order to settle the trade payables due to such suppliers with a carrying amount in aggregate of RMB5,629,000 (2015: RMB10,464,000). The Derecognised Bills had a maturity of within one month at the end of the reporting period. In accordance with the Law of Negotiable Instruments in the PRC, the holders of the Derecognised Bills have a right of recourse against the Group if the PRC banks default (the “Continuing Involvement”). In the opinion of the directors, the Group has transferred substantially all risks and rewards relating to the Derecognised Bills. Accordingly, it has derecognised the full carrying amounts of the Derecognised Bills and the associated trade payables. The maximum exposure to loss from the Group’s Continuing Involvement in the Derecognised Bills and the undiscounted cash flows to repurchase these Derecognised Bills is equal to their carrying amounts. In the opinion of the directors, the fair values of the Group’s Continuing Involvement in the Derecognised Bills are not significant.

During the reporting period, the Group has not recognised any gain or loss on the date of transfer of the Derecognised Bills. No gains or losses were recognised from the Continuing Involvement, both during the year or cumulatively. The endorsement has been made evenly throughout the reporting period.

17. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

	2016 RMB'000	2015 RMB'000
Prepayments	7,263	8,308
Deposits and other receivables (note 27)	16,932	13,075
	24,195	21,383

None of the above assets is either past due or impaired. The financial assets included in the above balances relate to receivables for which there was no recent history of default.

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18. CASH AND BANK BALANCES

	2016 RMB'000	2015 RMB'000
Cash and cash equivalents	286,357	121,306
Including: Time deposits with original maturity of less than three months when acquired	94,521	23,199
Cash on hand and demand deposits	191,836	98,107
Time deposits with original maturity of over three months when acquired	253,867	264,727
Cash and bank balances	540,224	386,033

At the end of the reporting period, the cash and bank balances of the Group denominated in RMB amounted to RMB500,266,000 (2015: RMB364,760,000). The RMB is not freely convertible into other currencies, however, under Mainland China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.

Cash at banks earns interest at floating rates based on daily bank deposit rates. Short term time deposits are made for varying periods of between one day and six months depending on the immediate cash requirements of the Group, and earn interest at the respective short term time deposit rates. The bank balances are deposited with creditworthy banks with no recent history of default.

19. TRADE AND BILLS PAYABLES

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

	2016 RMB'000	2015 RMB'000
Within 3 months	112,699	122,751
3 to 6 months	604	68
6 to 12 months	–	815
Over 12 months	619	1,069
	113,922	124,703

The trade and bills payables are non-interest-bearing and are normally settled on 90-day terms.

A maturity analysis of the above financial liabilities is set out in note 29 to the financial statements.

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20. ACCRUALS, OTHER PAYABLES AND DEFERRED INCOME

	2016 RMB'000	2015 RMB'000
Current liabilities:		
Payable for the purchase of software	5,671	928
Accruals	9,267	5,852
Deferred income	138,018	159,647
Advance from customers	6,094	5,979
Other payables	127,615	88,661
	286,665	261,067
Non-current liability:		
Deferred income	12,078	5,738

Deferred income represents the government grants received, which are related to assets and should be recorded as deferred income that was recognised in profit or loss on a systematic basis over the useful lives of the assets, and which are related to expenses to be incurred in subsequent periods or to which there were unfulfilled conditions, and should be recorded as deferred income that was recognised in profit or loss over the periods in which the related costs are recognised or conditions are fulfilled.

Other payables are unsecured, non-interest-bearing and have an average term of three months.

21. SHARE CAPITAL

	2016 RMB'000	2015 RMB'000
Authorised, issued and fully paid:		
375,000,000 (2015: 375,000,000) unlisted domestic shares of RMB0.10 each	37,500	37,500
242,330,000 (2015: 242,330,000) H shares of RMB0.10 each	24,233	24,233
	61,733	61,733

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22. RESERVES

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity on page 45 of the financial statements.

(i) Share premium

At 31 December 2016, in accordance with the Company Law of the PRC, the Company's share premium account of approximately RMB168,486,000 (2015: RMB168,486,000) was available for distribution by way of a future capitalisation issue.

(ii) Statutory surplus reserve

In accordance with the Company Law of the PRC and the articles of association of the Company and its subsidiaries in Mainland China, the Company and the subsidiaries are required to allocate 10% of their profits after tax (after deducting accumulated losses incurred in previous years), as determined in accordance with the applicable PRC accounting standards and regulations (the "PRC accounting standards"), to the statutory surplus reserve (the "SSR") until such reserve reaches 50% of the registered capital of the respective companies. Subject to certain restrictions set out in the Company Law of the PRC and the articles of association of the Company and its PRC subsidiaries, the SSR may be capitalised as share capital, provided that the remaining balance after the capitalisation is not less than 25% of the registered capital.

As the SSR had reached 50% of the registered capital of the Company before 31 December 2012, the directors of the Company has not proposed any transfer of profit after tax to the SSR since 31 December 2012.

The directors of the Company's PRC subsidiaries have proposed to transfer RMB3,051,000 (2015: RMB2,016,000) in total to the SSR. The transfer represents 10% of the Company's PRC subsidiaries' profit after tax, as determined in accordance with the PRC accounting standards, and attributable to the owners of the parent. The transfer has been incorporated in these financial statements.

(iii) Other reserves

In April 2014, Sino IC increased its issued shares from 31,000,000 shares to 42,000,000 shares. The issue price was RMB5 per share. The Company and the non-controlling shareholders subscribed 1,006,000 shares and 9,994,000 shares, respectively. The excess of the consideration contributed by the non-controlling interests over the net asset value of Sino IC shared by the non-controlling interests upon completion of the capital injection, amounting to RMB7,821,000, was recognised directly in the other reserves account.

In December 2016, Fukong Hualong increased its issued shares from 30,000,000 shares to 40,000,000 shares. The issue price was RMB2 per share. The Company subscribed nil shares in the transaction. The excess of the consideration contributed by the non-controlling interests over the net asset value of Fukong Hualong shared by the non-controlling interests upon completion of the capital injection, amounting to RMB6,922,000, was recognised directly in the other reserves account.

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23. A PARTLY-OWNED SUBSIDIARY WITH MATERIAL NON-CONTROLLING INTERESTS

Details of the Group's subsidiary that has material non-controlling interests are set out below:

	2016	2015
Percentage of equity interest held by non-controlling interests		
Sino IC	49.7%	49.7%
	2016	2015
	RMB'000	RMB'000
Profit for the year allocated to non-controlling interests		
Sino IC	30,131	19,122
Accumulated balances of non-controlling interests at the reporting dates:		
Sino IC	134,842	104,711

The following tables illustrate the summarised information of the above subsidiary. The amounts disclosed are before any inter-company eliminations:

Sino IC	2016	2015
	RMB'000	RMB'000
Revenue	125,051	107,999
Other income	86,621	30,295
Total costs and expenses	(136,622)	(91,019)
Income tax	(14,376)	(7,178)
Profit for the year	60,674	40,097
Total comprehensive for the year	60,674	40,097
Current assets	281,145	187,603
Non-current assets	93,100	118,592
Current liabilities	(91,102)	(91,855)
Non-current liabilities	(10,168)	(2,032)
Net cash flows from operating activities	109,932	75,153
Net cash flows used in investing activities	(78,322)	(58,179)
Net cash flows from financing activities	–	–
Net increase in cash and cash equivalents	31,610	16,974

The profit or loss and net assets of the other subsidiaries attributable to the non-controlling interests are not material to the Group.

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24. CONTINGENT LIABILITIES

As at 31 December 2016, the Group had no significant contingent liabilities.

25. COMMITMENTS

The Group had the following commitments at the end of the reporting period:

(a) Capital commitments

	2016 RMB'000	2015 RMB'000
Contracted, but not provided for:		
Property, plant and equipment	7,637	15,950

(b) The Group leases certain of its office properties under operating lease arrangements, with leases negotiated for terms ranging from one to five years.

At 31 December 2016, the Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

As lessee

	2016 RMB'000	2015 RMB'000
Within one year	9,777	9,849
In the second to fifth years, inclusive	12,228	12,070
	22,005	21,919

26. RELATED PARTY TRANSACTIONS

- (a) In addition to the transactions and balances detailed elsewhere in these financial statements, the Group had the following transactions with related parties during the year:

	Notes	2016 RMB'000	2015 RMB'000
Technical and equipment support fee paid to the owner of one of the shareholders of the Company	(i)	105	570
Rental expense paid to the owner of one of the shareholders of the Company	(ii)	–	283
Testing fee paid to the owner of one of the shareholders of the Company	(iii)	–	171

Notes:

- (i) On 12 August 2003, the Company and Shanghai Fudan University (“SFU”), a substantial shareholder of the Company, entered into an agreement under which the Company was required to pay a technical and equipment support fee to SFU based on a price mutually agreed by the two parties. The annual technical support fee payable to SFU for the year ended 31 December 2016 amounted to RMB105,000 (2015: RMB570,000).
- (ii) Rental expense paid to SFU was made according to the terms and conditions agreed between the related parties through lease agreement.
- (iii) Testing fee paid to SFU was made according to the terms and conditions agreed between the related parties.

The related party transaction in respect of item(i) above also constitutes connected transaction or continuing connected transaction as defined in Chapter 14A of the Listing Rules.

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26. RELATED PARTY TRANSACTIONS (continued)

(b) Compensation of key management team of the Group:

	2016 RMB'000	2015 RMB'000
Directors' and chief executive's remuneration	7,599	5,315
Salaries, allowances and benefits in kind-other key management team members	4,217	4,111
Total compensation paid to key management team	11,816	9,426

Further details of directors' and the chief executive's emoluments are included in note 7 to the financial statements.

- (c) In December 2016, Fukong Hualong issued 10,000,000 shares of RMB1 each at a subscription price of RMB2 each to Zhoushanshi Kangxin Investment Partners Enterprise ("Kangxin Investment"), a limited partnership enterprise established in the PRC. Mr. Li Wei, a supervisor of the Company, Mr. Dai Zhongdong, the assistant general manager of the Company, and Kangxin Investment Zhoushanshi Dongwei Investment Consultancy Limited, in which Mr. Li Wei and Mr. Dai Zhongdong hold a 50% interest each, hold 24.8%, 29.8% and 0.4%, respectively, of the capital contributions in Kangxin Investment.

27. FINANCIAL INSTRUMENTS BY CATEGORY

The carrying amounts of each of the categories of financial instruments as at the end of the reporting period are as follows:

Financial assets

	Loans and receivables RMB'000
31 December 2016	
Trade and bills receivables	466,616
Financial assets included in prepayments, deposits and other receivables (note 17)	16,932
Cash and bank balances	540,224
	1,023,772

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27. FINANCIAL INSTRUMENTS BY CATEGORY (continued)

The carrying amounts of each of the categories of financial instruments as at the end of the reporting period are as follows: (continued)

Financial assets (continued)

	Loans and receivables RMB'000
31 December 2015	
Trade and bills receivables	366,017
Financial assets included in prepayments, deposits and other receivables (note 17)	13,075
Cash and bank balances	386,033
	765,125

Financial liabilities

	Financial liabilities at amortised cost RMB'000
31 December 2016	
Trade and bills payables	113,922
Financial liabilities included in accruals, other payables and deferred income (note 20)	142,553
	256,475

	Financial liabilities at amortised cost RMB'000
31 December 2015	
Trade and bills payables	124,703
Financial liabilities included in accruals, other payables and deferred income (note 20)	95,441
	220,144

28. FAIR VALUE AND FAIR VALUE HIERARCHY

The carrying amounts of the Group's financial instruments approximate to their fair values.

Management has assessed that the fair values of cash and bank balances, trade and bills receivables, trade and bills payables, financial assets included in prepayments, deposits and other receivables, financial liabilities included in accruals, other payables and deferred income, amounts due from/to subsidiaries approximate to their carrying amounts largely due to the short term maturities of these instruments.

The fair values of the financial assets and liabilities are included at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

The fair value of the unlisted available-for-sale equity investments cannot be measured reliably, because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, and therefore such investments are stated at cost less any impairment losses.

Fair value hierarchy

The Group did not have any financial assets or financial liabilities measured at fair value as at 31 December 2016 and 31 December 2015.

29. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments comprise cash and short term time deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as trade and bills receivables, deposits and other receivables, trade and bills payables and accruals and other payables, which arise directly from its operations.

It is, and has been, throughout the year under review, the Group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are foreign currency risk, credit risk and liquidity risk. The board of directors believes that the Group is not exposed to any material interest rate risk as the Group does not have any debt obligations that are subject to fluctuations in market interest rates. The board of directors reviews and agrees policies for managing each of these risks and they are summarised below.

Foreign currency risk

The Group has transactional currency exposures. Such exposures arise from sales or purchases by operating units in currencies other than the units' functional currencies. Approximately 6% (2015: 8%) of the Group's sales are denominated in currencies other than the functional currency of the operating units making the sale, whilst almost 61% (2015: 70%) of costs are denominated in the units' functional currencies. The Group keeps monetary items in foreign currencies at a certain level in order to meet the needs of purchases that are denominated in the foreign currencies. It is the Group's policy not to enter into forward contracts until a firm commitment is in place.

29. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Foreign currency risk *(continued)*

The following tables demonstrate the sensitivity at the end of the reporting period to a reasonably possible change in the foreign currency exchange rates, with all other variables held constant, of the Group's profit before tax (due to changes in the fair value of monetary assets and liabilities).

	Increase/(decrease) in foreign currency exchange rate %	Increase/ (decrease) in profit before tax RMB'000	Increase/ (decrease) in equity* RMB'000
2016			
If RMB weakens against			
United States dollar ("US\$")	+5	1,368	-
If RMB strengthens against US\$	-5	(1,368)	-
2015			
If RMB weakens against US\$	+5	(1,007)	-
If RMB strengthens against US\$	-5	1,007	-
If RMB weakens against			
Euro ("EUR€")	+5	23	-
If RMB strengthens against EUR€	-5	(23)	-

* Excluding retained profits.

Credit risk

The Group trades only with recognised and creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis and the Group's exposure to bad debts is not significant. For transactions that are not denominated in the functional currency of the relevant operating unit, the Group does not offer credit terms without the specific approval of management.

The credit risk of the Group's other financial assets, which comprise cash and bank balances, deposits and other receivables, and available-for-sale investments, arises from default of the counterparty, with a maximum exposure equal to the carrying amounts of these instruments.

Since the Group trades only with recognised and creditworthy third parties, there is no requirement for collateral. Concentrations of credit risk are managed by customer. At the end of the reporting period, the Group has certain concentrations of credit risk as the Group's sales are made to several major customers, 27% (2015: 27%) of the Group's trade and bills receivables were due from the Group's five largest customers within the design, development and sale of IC products segment. The Group seeks to maintain strict control over its outstanding receivables and closely monitors the collection to minimise credit risk.

Further quantitative data in respect of the Group's exposure to credit risk arising from trade and bills receivables are disclosed in note 17 to the financial statements.

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29. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Liquidity risk

The Group monitors its risk to a shortage of funds using a recurring liquidity planning tool. This tool considers the maturity of both its financial instruments and financial assets (e.g., trade and bills receivables) and projected cash flows from operations.

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of normal business credit terms obtained from various creditors.

The maturity profile of the Group's financial liabilities as at the end of the reporting period, based on the contractual undiscounted payments, is as follows:

	On demand RMB'000	Less than 3 months RMB'000	3 to less than 12 months RMB'000	1 year to 5 years RMB'000	Total RMB'000
31 December 2016					
Trade and bills payables	993	112,929	–	–	113,922
Financial liabilities included in accruals, other payables and deferred income	72,671	58,326	8,449	3,107	142,553
	73,664	171,255	8,449	3,107	256,475
31 December 2015					
Trade and bills payables	1,285	123,418	–	–	124,703
Financial liabilities included in accruals, other payables and deferred income	59,083	31,320	4,739	299	95,441
	60,368	154,738	4,739	299	220,144

29. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Capital management

The primary objectives of the Group's capital management are to safeguard the Group's ability to continue as a going concern and to maintain healthy capital ratios in order to support its business and maximise shareholders' value.

The Group manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. The Group is not subject to any externally imposed capital requirements. No changes were made in the objectives, policies or processes for managing capital during the years ended 31 December 2016 and 31 December 2015.

The Group monitors capital using a gearing ratio, which is the total liabilities divided by the net assets. The gearing ratios as at the end of the reporting periods were as follows:

	2016 RMB'000	2015 RMB'000
Total liabilities	428,436	404,877
Net assets	1,374,432	1,113,586
Gearing ratio	31.2%	36.4%

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30. STATEMENT OF FINANCIAL POSITION OF THE COMPANY

Information about the statement of financial position of the Company at the end of the reporting period is as follows:

	2016 RMB'000	2015 RMB'000
NON-CURRENT ASSETS		
Property, plant and equipment	220,552	221,198
Intangible assets	135,397	157,686
Investments in subsidiaries	56,581	56,581
Deferred tax assets	34,764	28,114
Total non-current assets	447,294	463,579
CURRENT ASSETS		
Inventories	281,215	214,370
Due from subsidiaries	4,168	6,183
Trade and bills receivables	442,283	340,372
Prepayments, deposits and other receivables	12,629	11,725
Cash and bank balances	252,651	202,740
Total current assets	992,946	775,390
CURRENT LIABILITIES		
Due to subsidiaries	8,433	9,289
Trade and bills payables	113,367	122,896
Accruals, other payables and deferred income	203,986	174,873
Tax payable	604	1,553
Total current liabilities	326,390	308,611
NET CURRENT ASSETS	666,556	466,779
TOTAL ASSETS LESS CURRENT LIABILITIES	1,113,850	930,358
NON-CURRENT LIABILITIES		
Deferred income	1,802	3,229
Net assets	1,112,048	927,129

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30. STATEMENT OF FINANCIAL POSITION OF THE COMPANY (continued)

	2016 RMB'000	2015 RMB'000
EQUITY		
Share capital	61,733	61,733
Reserves	1,050,315	865,396
Total equity	1,112,048	927,129

Shi Lei
Director

Cheng Junxia
Director

Note:

A summary of the Company's reserves is as follows:

	Share premium account RMB'000	Statutory surplus reserve RMB'000	Retained profits RMB'000	Total RMB'000
At January 2015	168,486	35,478	514,098	718,062
Total comprehensive income for the year	–	–	147,334	147,334
At 31 December 2015	168,486	35,478	661,432	865,396
Total comprehensive income for the year	–	–	184,919	184,919
At 31 December 2016	168,486	35,478	846,351	1,050,315

31. EVENT AFTER THE REPORTING PERIOD

On 15 March 2017, the shareholders of Doublepoint passed a resolution for the dissolution of Doublepoint.

32. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 28 March 2017.

Five Year Financial Summary

A summary of the results and of the assets, liabilities and non-controlling interests of the Group for the last five financial years, as extracted from the published audited financial statements and reclassified as appropriate, is set out below.

	Year ended 31 December				
	2016 RMB'000	2015 RMB'000	2014 RMB'000	2013 RMB'000	2012 RMB'000
RESULTS					
REVENUE	1,187,490	1,039,725	843,913	816,931	704,064
Cost of sales	(556,198)	(489,416)	(443,131)	(419,472)	(367,919)
Gross profit	631,292	550,309	400,782	397,459	336,145
Other income and gains	162,985	83,080	102,722	104,234	105,277
Selling and distribution expenses	(68,428)	(61,887)	(55,566)	(58,637)	(36,861)
Administrative expenses	(87,300)	(80,579)	(71,894)	(60,573)	(58,168)
Other expenses	(378,692)	(297,598)	(192,402)	(213,343)	(183,380)
Share of profit and loss of an associate	–	–	–	(110)	(376)
PROFIT BEFORE TAX	259,857	193,325	183,642	169,030	162,637
Tax	(19,767)	(15,335)	(6,653)	(4,753)	(19,049)
PROFIT FOR THE YEAR	240,090	177,990	176,989	164,277	143,588
Attributable to:					
Owners of the parent	212,258	158,898	167,963	159,398	140,068
Non-controlling interests	27,832	19,092	9,026	4,879	3,520
	240,090	177,990	176,989	164,277	143,588

	As at 31 December				
	2016 RMB'000	2015 RMB'000	2014 RMB'000	2013 RMB'000	2012 RMB'000
ASSETS, LIABILITIES AND NON-CONTROLLING INTERESTS					
TOTAL ASSETS	1,802,868	1,518,463	1,276,461	1,046,443	846,868
TOTAL LIABILITIES	(428,436)	(404,877)	(341,533)	(289,102)	(204,452)
NON-CONTROLLING INTERESTS	(152,666)	(111,756)	(92,664)	(41,486)	(36,304)
	1,221,766	1,001,830	842,264	715,855	606,112