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If you have sold or transferred all your shares in Xian Yuen Titanium Resources Holdings Limited (the “Company”), you should at once hand this circular accompanying with the form of proxy to the purchaser or transferee, or to the bank, licensed securities dealer or other agent through whom the sale or transfer was effected for transmission to the purchaser or transferee.

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XIAN YUEN TITANIUM RESOURCES HOLDINGS LIMITED

森源鈦礦控股有限公司*

(Incorporated in the Cayman Islands with limited liability)

(Stock code: 353)

VERY SUBSTANTIAL ACQUISITION

A notice convening the extraordinary general meeting of the Company to be held at Room 1102B, 11/F, Tower I, Admiralty Centre, 18 Harcourt Road, Hong Kong on 16 July 2010 at 4:00 p.m. is set out on pages 194 to 195 of this circular. Whether or not you are able to attend the meeting in person, please complete the accompanying form of proxy in accordance with the instructions printed thereon and return the same to the Company's share registrars, Tricor Tengis Limited at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong as soon as practicable but in any event not less than 48 hours before the time appointed for the holding of the meeting. Completion and return of the accompanying form of proxy will not preclude you from attending and voting at the meeting should you so wish.

* For identification purpose only

CONTENTS

	<i>Page</i>
Definitions	1
 Letter from the Board	
A. Introduction	6
B. The Agreement dated 5 November 2009	7
C. Consideration Shares	13
D. Convertible Notes	14
E. Shareholding structure of the Company before and after Completion	16
F. Information relating to the Target Group	18
G. Industry overview	21
H. Business model	27
I. Management discussion and analysis of the Target Group	37
J. Reasons for entering into the Agreement	47
K. Financial effect of the Acquisition	48
L. Financial and trading prospects of the Enlarged Group	48
M. Regulatory environment	56
N. Risk factors	64
O. EGM	66
P. Recommendations	67
Q. Additional information	67
 Appendix I – Accountants’ report of the Target Group	 68
Appendix II – Accountants’ report of the Project Company	86
Appendix III – Financial information of the Group	116
Appendix IV – Management discussion and analysis of the Group	119
Appendix V – Unaudited pro forma financial information of the Enlarged Group	135
Appendix VI – Property valuation of the Enlarged Group	154
Appendix VII – Valuation of the Project Company	169
Appendix VIII – General information	189
Notice of EGM	194

DEFINITIONS

In this circular, the following expressions have the following meanings, unless the context otherwise requires:–

“Acquisition”	the sale and purchase of the Sale Shares contemplated under the Agreement
“Agreement”	the sale and purchase agreement dated 5 November 2009 entered into between the Purchaser as purchaser, the Company as the Purchaser’s holding company, the Vendor as vendor and the Guarantor as guarantor for the acquisition of the Sale Shares by the Purchaser at the total consideration of HK\$350,860,000 which will be satisfied partly by cash and partly by the Company’s issue of the Consideration Shares and Convertible Notes to the Vendor or its nominee(s)
“Announcement”	the announcement of the Company dated 23 November 2009 in relation to the Acquisition
“Associates”	has the meaning given to that term in the Listing Rules
“Board”	the board of Directors
“Business Day(s)”	any day (excluding Saturday and Sunday) on which banks in Hong Kong are open for business
“Company”	Xian Yuen Titanium Resources Holdings Limited, a company incorporated under the laws of the Cayman Islands with limited liability and the shares of which are listed on the Stock Exchange (stock code: 353)
“Completion”	actual completion of the sale and purchase of the Sale Shares in accordance with the Agreement
“Connected Person(s)”	has the meaning given to that term in the Listing Rules
“Consideration Shares”	being 1,510,000,000 new Shares to be issued and allotted at the issue price of HK\$0.093 per Share, credited as full paid, by the Company to partly satisfy the consideration for the Acquisition under the Agreement
“Conversion Shares”	those Shares to be converted upon conversion of the conversion rights attached to the Convertible Notes at the conversion price of HK\$0.093 per Share (subject to adjustment)
“Convertible Notes”	the zero coupon convertible notes in registered form comprising a total principal amount of HK\$140,430,000, to be issued by the Company to the Vendor on the date of Completion to partly satisfy the consideration for the acquisition under the Agreement

DEFINITIONS

“Deeds of Charge”	collectively, the share charges to be executed by the Vendor, the Target Company and Pride Treasure respectively in favour of the Purchaser to secure the Vendor’s obligation to repay the Deposit and the Further Deposit
“Deposit”	the refundable initial deposit in the sum of HK\$35,000,000 payable by the Purchaser to the Target Company at the direction of the Vendor pursuant to the terms and conditions of the Agreement
“Director(s)”	director(s) of the Company
“EGM”	extraordinary general meeting of the Company to be held at Room 1102B, 11/F, Tower I, Admiralty Centre, 18 Harcourt Road, Hong Kong on 16 July 2010 at 4:00 p.m. to approve, inter alia, the Agreement and the transactions contemplated thereunder and the issue of the Consideration Shares and the Convertible Notes
“Enlarged Group”	the Group as enlarged by the Acquisition
“Further Deposit”	the refundable further deposit in the sum of HK\$35,000,000 payable by the Purchaser to the Vendor pursuant to the terms and conditions of the Agreement
“GDP”	gross domestic product
“Group”	the Company and its subsidiaries
“Guarantor”	Ms. Ho Mee Kuen Karen, the legal and beneficial owner of the Vendor and the guarantor under the Agreement
“GW”	unit of energy, gigawatt; 1 GW = 1,000 MW
“GWh”	unit of energy, gigawatt-hour; 1 GWh = 1 million kWh; GWh is typically used as a measure for the annual energy production of large power plants
“HK\$”	Hong Kong dollars, the lawful currency of Hong Kong
“Hong Kong”	Hong Kong Special Administrative Region of the PRC
“Independent Third Party(ies)”	party(ies) who is/are not Connected Person(s) of the Company and who together with its/their ultimate beneficial owner(s) are independent of the Company and of the Connected Persons of the Company

DEFINITIONS

“installed capacity”	the capacity of those wind turbines or power generators that have been completely assembled and erected and which have been commissioned and started producing electricity
“kW”	unit of energy, kilowatt; 1 kW = 1,000 watts
“kWh” or “unit (of electricity)”	unit of energy, kilowatt-hour; the standard unit of energy used in the electric power industry. One kilowatt-hour is the amount of energy that would be produced by a generator producing one thousand watts for one hour
“Last Trading Day”	5 November 2009, being the last trading day of the Shares on the Stock Exchange immediately prior to the date of the Announcement
“Latest Practicable Date”	25 June 2010, being the latest practicable date prior to the printing of this circular for ascertaining certain information in this circular
“Listing Rules”	the Rules Governing the Listing of Securities on the Stock Exchange
“Long Stop Date”	10 August 2010 or such later date to be agreed between the parties to the Agreement in writing
“MW”	unit of energy, megawatt; 1 MW = 1,000 kW; the installed capacity of power plants is generally expressed in MW
“MWh”	unit of energy, megawatt-hour; 1 MWh = 1,000 kWh
“NDRC”	National Development and Reform Commission of the PRC (國家發展和改革委員會)
“Ontop Finance”	Ontop Finance Limited, a company incorporated under the laws of Hong Kong and a direct wholly-owned subsidiary of Pride Treasure
“Petroleum Development Acquisition”	the proposed acquisition by the Company pursuant to the terms and conditions of a conditional share purchase agreement entered into by the Company on 25 September 2009 in relation to the acquisition of a group of companies which has entered into a cooperation contract with China National Petroleum Corporation, a state-owned petroleum enterprise in the PRC, in relation to the development and production of petroleum resources in Liangjing Block of Songliao Basin of the PRC

DEFINITIONS

“Pride Treasure”	Pride Treasure Limited, a company incorporated under the laws of Hong Kong and a direct wholly owned subsidiary of the Target Company
“Project Company”	山西中凱集團靈石熱電有限公司 (Shanxi Zhong Kai Group Lingshi Heat and Power Company Limited), a sino-foreign equity joint venture enterprise established under the laws of the PRC
“Purchaser”	Precious New Limited, a company incorporated under the laws of the British Virgin Islands and a wholly-owned subsidiary of the Company
“PRC”	People’s Republic of China
“RMB”	Renminbi, the lawful currency of the PRC
“Sale Shares”	such number of shares of US\$1.00 each in the capital of the Target Company representing the entire issued share capital of the Target Company immediately before Completion, which are legally and beneficially owned by the Vendor
“SFO”	the Securities and Futures Ordinance (Chapter 571 of the laws of Hong Kong)
“Share(s)”	ordinary share(s) of HK\$0.01 each in the existing issued share capital of the Company
“Shareholder(s)”	holder(s) of the Shares
“Shareholders Loan”	the loans owing from time to time by members of the Target Group to the Vendor and/or its Associates (for the avoidance of doubt and for the purpose of the Agreement, the Vendor’s Associates shall not include any member of the Group or any other shareholder of any member of the Group) and, for the purpose of the Agreement, will include such amount as equal to the Deposit which will be advanced by the Vendor to the Target Company to, ultimately, Ontop Finance which Ontop Finance will use solely for paying up the registered capital of the Project Company
“State Grid”	State Grid Corporation (國家電網公司) of the PRC
“Stock Exchange”	The Stock Exchange of Hong Kong Limited
“Target Company”	Sunlight Rise Limited, a company incorporated under the laws of the British Virgin Islands and the entire issued share capital of which is held by the Vendor as at the date of the Agreement

DEFINITIONS

“Target Group”	the Target Company and its subsidiaries
“TWh”	unit of energy, terawatt-hour; 1 TWh = 1 billion kWh
“US\$”	United States Dollars, the lawful currency of the United States of America
“Vendor”	Maycrown Capital Limited, a company incorporated under the laws of the British Virgin Islands and the entire issued share capital of which is held by the Guarantor as at the date of the Agreement
“W”	a derived unit of power in the International System of Units (SI). The unit measures the rate of energy conversion. By the definitions of the units for measuring electric potential (volt) and current (ampere), work is done at a rate of one watt when one ampere flows through a potential difference of one volt. One watt is equal to 1 joule (J) of energy per second
“Zhongkai Group”	Shanxi Zhong Kai Group Limited (山西中凱實業集團有限公司), a company incorporated under the laws of the PRC and a holder of 31.68% of the entire equity interest of the Project Company
“%”	per cent.

LETTER FROM THE BOARD



XIAN YUEN TITANIUM RESOURCES HOLDINGS LIMITED

森源鈦礦控股有限公司*

(Incorporated in the Cayman Islands with limited liability)

(Stock code: 353)

Executive Directors:

Mr. Law Fei Shing (*Chief Executive Officer*)

Mr. Chan Sung Wai

Mr. Chan Kwok Wing

Mr. Wang Donghai

Mr. Zhao Guoqiang

Registered Office:

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Hutchins Drive, P.O. Box 2681

Grand Cayman KY1-1111

Cayman Islands

Non-Executive Director:

Mr. Zhang Zhenming

Head Office and Principal Place of

Business in Hong Kong:

Room 1102B, 11th Floor

Tower I, Admiralty Centre

18 Harcourt Road

Hong Kong

Independent Non-Executive Directors:

Mr. Lum Pak Sum

Mr. Sun Tak Keung

Mr. Chow Pui Fung

28 June 2010

To the Shareholders

Dear Sir or Madam

VERY SUBSTANTIAL ACQUISITION

A. INTRODUCTION

On 23 November 2009, the Board announced that on 5 November 2009, the Purchaser (a wholly-owned subsidiary of the Company) and the Company entered into the Agreement with the Vendor and the Guarantor pursuant to which the Purchaser conditionally agreed to acquire from the Vendor the Sale Shares at the total consideration of HK\$350,860,000 to be paid to the Vendor partly by cash and partly by the Company's issue of the Consideration Shares and the Convertible Notes.

Given that the percentage ratios as defined in Rule 14.04(9) of the Listing Rules exceed 100%, the entering into of the Agreement constitutes a very substantial acquisition for the Company under the Listing Rules and will be subject to the approval of the Shareholders at the EGM under Chapter 14 of the Listing Rules.

The purpose of this circular is to give the Shareholders further details of the Acquisition and the issue of the Consideration Shares and the Convertible Notes and a notice of the EGM for the purpose of approving the Agreement and the transactions contemplated thereunder.

* For identification purpose only

LETTER FROM THE BOARD

B. THE AGREEMENT DATED 5 NOVEMBER 2009

Parties

1. The Purchaser
2. The Company
3. The Vendor
4. The Guarantor

The Vendor is a company incorporated under the laws of the British Virgin Islands and is legally and beneficially owned by the Guarantor. To the best of the Directors' knowledge, information and belief having made all reasonable enquiries, the Vendor and its ultimate beneficial owner are Independent Third Parties.

Assets to be acquired

The Sale Shares will comprise all those issued shares of the Target Company held by the Vendor and represent the entire issued share capital of the Target Company. The Target Company is an investment holding company which is wholly owned by the Vendor as at the Latest Practicable Date and it indirectly owns 60% equity interest in the Project Company.

Consideration

The total consideration for the Sale Shares under the Acquisition is HK\$350,860,000 which will be satisfied in the following manner:

- (a) as to HK\$35,000,000, will be paid by the Purchaser within two (2) Business Days after the date of the Agreement a refundable deposit by the Purchaser to (at the irrevocable direction of the Vendor) the Target Company. The Deposit will be treated as a loan from the Vendor to, ultimately, Ontop Finance which Ontop Finance will use solely for paying up the registered capital of the Project Company and which shall form part of the Shareholders Loan;
- (b) as to HK\$35,000,000, will be paid by the Purchaser to the Vendor a further refundable deposit in cash within three (3) Business Days after the completion of the due diligence investigation to be conducted by the Purchaser and its advisers on the Target Group and conditional upon, inter alia, the following conditions being fulfilled and/or waived by the Purchaser:
 - (i) a share charge over the entire issued share capital of the Target Company (in such form to be agreed and acceptable by the Purchaser in its absolute discretion) to be created by the Vendor in favour of the Purchaser for the purpose of securing the repayment of the Deposit and the Further Deposit duly executed and delivered to the Purchaser;

LETTER FROM THE BOARD

- (ii) a share charge over the entire issued share capital of Pride Treasure (in such form to be agreed and acceptable by the Purchaser in its absolute discretion) to be created by the Target Company in favour of the Purchaser for the purpose of securing the repayment of the Deposit and the Further Deposit duly executed and delivered to the Purchaser; and
- (iii) a share charge over the entire issued share capital of Ontop Finance (in such form to be agreed and acceptable by the Purchaser in its absolute discretion) to be created by Pride Treasure in favour of the Purchaser for the purpose of securing the repayment of the Deposit and the Further Deposit duly executed and delivered to the Purchaser; and
- (c) upon Completion,
 - (i) as to HK\$140,430,000 by the Company's issue to the Vendor or its nominee(s) of the Consideration Shares; and
 - (ii) as to HK\$140,430,000 by the Company's issue to the Vendor or its nominee(s) of the Convertible Notes.

The cash portion of the consideration will be funded by the internal resources of the Group. If any of the conditions precedents set out in the Agreement is not satisfied or waived by the Purchaser on or before 5:00 p.m. on the Long Stop Date or the Agreement is terminated for whatsoever reason, the Vendor shall within ten (10) Business Days after the Long Stop Date (or such later date to be agreed between the parties to the Agreement in writing) or the termination date (as the case may be) repay to the Purchaser an amount equivalent to the sum of the Deposit and the Further Deposit. If the Vendor fails to repay the entirety of the said entire amount of the Deposit and the Further Deposit to the Purchaser before the prescribed date, interest shall accrue from the due date of payment until the date of full repayment at the rate equivalent to the current Hong Kong dollar best lending rate (as quoted by The Hongkong and Shanghai Banking Corporation Limited for the same or substantially similar Hong Kong dollar amount) plus two (2)% per annum.

As at the date of the Announcement, the Purchaser has already paid the Deposit pursuant to the provisions of the Agreement. As at the Latest Practicable Date, all the conditions for the further refundable deposit of HK\$35,000,000 had yet to be fulfilled and the said further refundable deposit of HK\$35,000,000 had yet to be paid by the Purchaser to the Vendor.

The consideration for the Acquisition was arrived at based on normal commercial terms after arm's length negotiations between the parties to the Agreement and by reference to (a) the preliminary valuation of the value of the Target Group represented by the Vendor; (b) the book value of the land and power plant owned by the Project Company; (c) the commitment of the Group to contribute to and pay up the remaining balance of the unpaid registered capital of the Project Company in the sum of approximately RMB69,550,000 (equivalent to approximately HK\$79,942,529) (for further details, please refer to the subparagraph headed "Further commitment of the Group" below), (d) the expected costs and expenses for the Acquisition; and (e) other factors set out in the paragraph headed "J. Reasons for entering into the Agreement" below. Although the Company has initially

LETTER FROM THE BOARD

agreed to the basis on which the Vendor's preliminary valuation was prepared, the preliminary valuation is still subject to, among other things, a formal valuation report on the value of the 60% equity interest in the Project Company to be issued by an independent valuer engaged by the Company. As one of the conditions precedent to Completion, the Purchaser will obtain a valuation report issued by such professional valuer retained or to be retained by the Company that indicates the value of 60% equity interest in the Project Company is not less than HK\$440,000,000. Based on the factors mentioned above, the consideration for the Acquisition is considered by the Board as fair and reasonable and in the interests of the Group and of the Shareholders as a whole.

Based on the valuation report prepared by BMI Appraisals Limited, an Independent Third Party, the market value of the 60% equity interest in the Project Company as at 30 April 2010 was HK\$552,000,000. Details of the valuation of the Project Company are set out in Appendix VII to this circular.

The Consideration Shares will be issued to the Vendor at a price of HK\$0.093 per Share and the Convertible Notes will be converted at the initial conversion price of HK\$0.093 per Conversion Share. The issue price of the Consideration Shares and the conversion price of the Convertible Notes have been determined based on arm's length negotiation between the Company and the Vendor.

Particulars of the Consideration Shares and Convertible Notes are set out in the paragraphs headed "C. Consideration Shares" and "D. Convertible Notes" below.

Further commitment of the Group

Apart from the payment of the total consideration of HK\$350,860,000, after Completion, the Purchaser will, through Ontop Finance, assume the obligation to contribute to and pay up the remaining balance of the registered capital of the Project Company in the sum of approximately RMB69,550,000 (equivalent to approximately HK\$79,942,529). As at the Latest Practicable Date, the Project Company has a registered capital of RMB185,000,000, of which RMB85,000,000 has been fully paid up by the original shareholders of the Project Company. The unpaid registered capital of RMB100,000,000 will be paid as to HK\$35,000,000 (approximately RMB30,450,000) by the Vendor which will be funded by the Deposit and as to approximately RMB69,550,000 (equivalent to approximately HK\$79,942,529) will be paid by the Purchaser. Notwithstanding the above, based on the reasons set out in the paragraph headed "J. Reasons for entering into the Agreement" below and the valuation report to be obtained by the Company which indicates that the value of 60% equity interest in the Project Company is not less than HK\$440,000,000, the Directors consider that the Acquisition is fair and reasonable and in the interest of the Company and the Shareholders.

LETTER FROM THE BOARD

Pursuant to the articles of the Project Company dated 6 May 2009, Ontop Finance is required to inject into the Project Company the US\$ equivalent of RMB30,000,000 within 3 months from the date of the business licence (i.e, 11 August 2009), a further sum of RMB30,000,000, in US\$, shall be injected within the following 3 months; and the remaining balance shall be injected within one year. To the best of the Directors' knowledge, information and belief having made all reasonable enquiries, as at the Latest Practicable Date, the Vendor had already injected HK\$35,000,000 (equivalent to approximately US\$4,511,893) into the registered capital of the Project Company. After Completion, the Company will be responsible for injecting the remaining balance (i.e., approximately RMB69,550,000) and fully pay up the registered capital of the Project Company. In this respect, and as one of the conditions precedent to Completion, the Vendor has agreed to procure and obtain from the relevant PRC government authority to extend the time for paying up the registered capital to a date not earlier than 1 July 2011. As such, the Company is not required to contribute to the registered capital of the Project Company until 2011.

Conditions precedent

Completion of the Agreement is subject to the fulfillment of, inter alia, the following conditions precedent:

- (a) the Purchaser having completed and satisfied in its absolute discretion with the results of the legal, financial, business and other due diligence investigation in respect of the assets, liabilities, businesses, prospects and other affairs of the Target Group as the Purchaser may in its sole and absolute discretion consider necessary or desirable;
- (b) the Purchaser having received and satisfied in its absolute discretion (in substance and form) a legal opinion issued by a firm of lawyers qualified to practise in the PRC covering matters including, among other things, (I) the Project Company having been duly established and validly subsisting; (II) the Project Company having obtained all the licences and permits which are necessary for conducting the business of the Project Company and such licences and permits are in full force and effect (further information on the licences and permits will be disclosed in the circular); and (III) such other aspect of PRC laws as the Purchaser may consider appropriate or relevant to the transactions contemplated by the Agreement;
- (c) the Purchaser having received and satisfied in its absolute discretion (in substance and form) a legal opinion issued by a firm of lawyers qualified to practice in the British Virgin Islands (at the Vendor's cost and expense) covering matters including, among other things, (I) each of the Target Company and the Vendor having been duly established and validly subsisting, (II) updated lists of directors and shareholders of each of the Target Company and the Vendor, and (III) such other aspect of the laws of the British Virgin Islands as the Purchaser may consider appropriate or relevant to the transactions contemplated by the Agreement;

LETTER FROM THE BOARD

- (d) the approval by the Shareholders (or, as the case may be, the independent Shareholders) at the EGM of the Agreement and the transactions contemplated thereby (including without limitation the issue of the Convertible Notes and the allotment and issue of the Consideration Shares and the Conversion Shares) and all other consents and acts required under the Listing Rules having been obtained and completed;
- (e) the Listing Committee of the Stock Exchange having granted or having agreed to grant the listing of, and permission to deal in, the Consideration Shares and the Conversion Shares;
- (f) if required, all approvals, consents, authorisations and licences (so far as are necessary) in relation to the transactions contemplated under the Agreement having been obtained from the relevant governmental authorities;
- (g) the Purchaser being satisfied in its absolute discretion, from the date of the Agreement and at any time before Completion, that the warranties set out in the Agreement remain true and accurate in all material respects, not misleading or in breach in any material respect and that no events have suggested that there were any breach in any material respect of any warranties or other provisions of the Agreement by the Vendor;
- (h) the Purchaser being satisfied in its absolute discretion, from the date of the Agreement to Completion, there has not been any material adverse change in respect of any member of the Target Group;
- (i) the Purchaser having received and satisfied in its absolute discretion the documents provided by the Vendor which evidence that all outstanding Shareholders Loan due from the Target Group to the Vendor and/or its Associates (for the avoidance of doubt and for the purpose of the Agreement, the Vendor's Associates shall not include any member of the Group or any other shareholder of any member of the Group) have been capitalised and/or assigned to such party(ies) as nominated by the Purchase immediately before Completion, and all necessary approvals, consents, authorisations and licences in relation thereto having been obtained from the relevant governmental authorities or parties concerned;
- (j) the Purchaser having obtained a final valuation report issued by such professional valuer retained or to be retained by the Company, that indicates that the value of 60% equity interest in the Project Company is not less than HK\$440,000,000;
- (k) the Purchaser having received and satisfied in its absolute discretion the PRC approval documents provided by the Vendor which evidence that the time limit for Ontop Finance to fully pay up the registered capital of the Project Company of RMB185,000,000 has been extended by the relevant PRC government authority to a date not earlier than 1 July 2011; and
- (l) no indication being received from the Stock Exchange that the transactions contemplated under the Agreement will be treated or, as the case may be, ruled by the Stock Exchange as a "reverse takeover" under the Listing Rules.

LETTER FROM THE BOARD

The Purchaser may waive in writing any of the conditions specified above (save and except conditions (d) and (e)) at any time. If all the conditions specified above have not been satisfied or waived by the Long Stop Date then the Agreement shall lapse and have no further effect and the parties shall be released from all their respective obligations under the Agreement save and except for any antecedent breach. In such event, the Vendor shall refund the Deposit and the Further Deposit to the Purchaser. As mentioned in the announcement of the Company dated 31 March 2010, the Long Stop Date has been extended from 31 March 2010 to 10 August 2010.

As at the Latest Practicable Date, condition (l) had been fulfilled.

Due diligence

Due diligence work performed by the Company

One of the conditions of the Acquisition is the Company's satisfaction with the results of a due diligence investigation conducted by the Company and its advisers. The investigation will include the legal, financial and business investigation in respect of the assets, liabilities, businesses and prospects of the Target Group. As at the Latest Practicable Date, the Company was satisfied with the results of the due diligence investigation conducted so far. The Company has instructed its PRC legal advisers to perform a due diligence investigation over the PRC matters including to review the relevant PRC rules and regulations and to ascertain, among other things, whether the Project Company has obtained all the licences and permits necessary for conducting the generating and supplying of electricity and heat business in the PRC. The Company has also instructed its auditors to review the financial information of the Target Group and its property valuer to value the property held or leased by the Enlarged Group. For the material findings from the due diligence investigation, please refer to Appendix I to Appendix II to this circular for the financial information of the Target Group and Appendix VI to this circular for the property valuation of the Enlarged Group.

Feasibility study

Prior to the entering of the Agreement, one of the Directors conducted a site visit to the power plant of the Project Company and had a chance to meet and discuss with the senior management of the Project Company and to peruse and consider various documents of the Project Company, including but not limited to the unaudited management accounts, the business licences, the land use right certificate, and a feasibility report prepared by the founder of Project Company in 2004 for the application of the incorporation and operation of the Project Company. The unaudited management accounts of the Project Company for the year ended 31 December 2008 showed that the Project Company made a net profit of approximately RMB28,680,000 in the year 2008. To the best of knowledge, information and belief of the Director who conducted the due diligence, the Project Company was the only heat and electricity generating company in the area of Lingshi County and the operation of the Project Company was highly supported by the local government of Lingshi County.

LETTER FROM THE BOARD

Material findings from the due diligence investigation and feasibility study

Based on the due diligence investigation conducted, the Board noted the following material findings: (i) the business of the Project Company is viable with the ability to generate net profit during the two years ended 31 December 2009 with a potential to increase further in the coming years due to the further urbanisation of Lingshi County; (ii) the value of the 60% equity interest in the Project Company as at 30 April 2010, i.e. HK\$552,000,000.00 (as shown in Appendix VII to this circular), is higher than the total consideration of the Acquisition; and (iii) the Project Company is technically viable.

Guarantee

The Guarantor is the sole legal and beneficial owner of the Vendor. The Guarantor has agreed to guarantee the performance by the Vendor of all its obligations under the Agreement.

Completion

Completion shall take place on a date which is the fifth (5th) Business Day after the date on which the conditions precedent are satisfied or waived or such other date as the Vendor and the Purchaser may agree in writing.

Neither the Vendor nor the original shareholders of the Project Company will appoint or nominate any director to the Company upon Completion.

C. CONSIDERATION SHARES

HK\$140,430,000 of the consideration under the Agreement will be satisfied by the issue of the Consideration Shares by the Company to the Vendor on Completion. The issue price of the Consideration Shares of HK\$0.093 per Consideration Share was determined after arm's length negotiations between the parties with reference to the recent market price of the Shares and the net asset value per Share as at 30 June 2009 of HK\$0.183 and represents:

- (i) a discount of approximately 49.18% to the net asset value per Share as at 30 June 2009;
- (ii) a discount of approximately 31.62% to the closing price of HK\$0.136 per Share as quoted on the Stock Exchange on the Last Trading Day;
- (iii) a discount of approximately 31.11% to the average closing price of HK\$0.135 per Share as quoted on the Stock Exchange on the last five trading days immediately prior to the Last Trading Day;
- (iv) a discount of approximately 32.12% to the average closing price of HK\$0.137 per Share as quoted on the Stock Exchange on the last ten trading days immediately prior to the Last Trading Day; and
- (v) a discount of approximately 30.60% to the closing price of HK\$0.134 per Share as quoted on the Stock Exchange on the Latest Practicable Date.

The Board considers the issue price of HK\$0.093 of the Consideration Shares is fair and reasonable and in the interests of the Company and the Shareholders as a whole.

LETTER FROM THE BOARD

The Consideration Shares represent approximately 20.50% of the issued share capital of the Company as at the Latest Practicable Date and approximately 17.01% of the issued share capital of the Company as enlarged by the issue of the Consideration Shares. The Consideration Shares will be issued under a specific mandate proposed to be obtained at the EGM. An application will be made to the Stock Exchange for the listing of, and permission to deal in, the Consideration Shares.

D. CONVERTIBLE NOTES

Up to HK\$140,430,000 of the consideration under the Agreement will be satisfied by the issue of the Convertible Notes by the Company to the Vendor on Completion. The principal terms of the Convertible Notes are as follows:

Issuer:	The Company
Principal amount:	HK\$140,430,000
Interest:	The Convertible Notes shall not bear interest.
Maturity:	The date falling on the 10th anniversary of the date of issue of the Convertible Notes.
Conversion price:	The conversion price, subject to the usual adjustment, is HK\$0.093 per Conversion Share. The initial conversion price of HK\$0.093 per Conversion Share represents: (i) a discount of approximately 31.62% to the closing price of HK\$0.136 per Share as quoted on the Stock Exchange on the Last Trading Day; and (ii) a discount of approximately 31.11% to the average closing price of approximately HK\$0.135 per Share for the last five trading days immediately prior to the Last Trading Day.

The conversion price of the Convertible Notes is subject to adjustment provisions which are standard terms for convertible securities of similar type. The adjustment events will arise as a result of certain change in the Shares including, inter alia, consolidation or sub-division of Shares, capitalisation of profits or reserves, capital distributions in cash or specie or rights issues and grant of options and warrants.

LETTER FROM THE BOARD

Conversion rights:

The conversion rights under the Convertible Notes shall be exercisable during the conversion period commencing from the date of issue of the Convertible Notes and the Business Day immediately preceding the maturity date. Upon the exercise of any conversion rights under the Convertible Notes, the Company will allot the number of Conversion Shares in respect of which conversion rights are exercised provided that no conversion right may be exercised, to the extent that following such exercise (i) a holder of the Convertible Notes and parties acting in concert with it, taken together, will directly or indirectly, control or be interested in 25% or more of the entire issued Shares or such percentage as may from time to time be specified in the Hong Kong Code on Takeovers and Mergers as being the level for triggering a mandatory general offer, whichever is lower, or (ii) the Company will be in breach of the minimum public float requirement under the Listing Rules.

Any Convertible Note which remains outstanding by 4:00 p.m. (Hong Kong time) on the maturity date shall be converted automatically into the Conversion Shares. However, there will not be any automatic conversion of the Convertible Notes at maturity if such conversion will result in (i) a holder of the Convertible Notes and parties acting in concert with it, taken together, will directly or indirectly, control or be interested in 25% or more of the entire issued shares of the Company or such percentage as may from time to time be specified in the Hong Kong Code on Takeovers and Mergers as being the level for triggering a mandatory general offer, whichever is lower, or (ii) the Company will be in breach of the minimum public float requirement under the Listing Rules. In such event, the Company may consider liaising with the holders of the outstanding Convertible Notes to extend the maturity date of the Convertible Notes. Should the maturity date of the Convertible Notes be extended, it will constitute a change in material terms of the Convertible Notes and the Company will seek the approval of the Shareholders (or as the case may be, independent Shareholders) of such alteration at general meeting in accordance with the requirements under the Listing Rules and comply with the applicable requirements of the Listing Rules (including but not limited to Chapters 14 and 14A of the Listing Rules).

LETTER FROM THE BOARD

Conversion Shares: The Conversion Shares will rank pari passu in all respects with all existing Shares in issue at the date of the notice of conversion. Assuming that the Convertible Notes are fully converted into Conversion Shares at the initial conversion price of HK\$0.093, a total of 1,510,000,000 Conversion Shares will be issued which represent approximately 20.50% of the issued share capital of the Company as at the Latest Practicable Date and approximately 17.01% of the issued share capital of the Company as enlarged by the allotment and issue of the Conversion Shares (but not the Consideration Shares).

The Conversion Shares will be issued under a special mandate proposed to be obtained at the EGM. An application will be made to the Stock Exchange for the listing of, and permission to deal in, the Conversion Shares.

Early Redemption: There are no early redemption rights.

Status of the Convertible Notes: The Convertible Notes constitute a direct, general, unconditional and unsecured obligation of the Company and rank pari passu and rateably without preference (with the exception of obligations in respect of taxes and certain other mandatory provisions of applicable law exceptions) equally with all other present and/or future unsecured and unsubordinated obligations of the Company.

Transferability: The Convertible Notes will be freely transferable provided that if the transfer is made to a Connected Person, such transfer shall comply with the requirements under the Listing Rules.

Voting rights: The Convertible Notes do not confer any voting rights at any meetings of the Company.

Application for Listing: No application will be made for the listing of the Convertible Notes.

E. SHAREHOLDING STRUCTURE OF THE COMPANY BEFORE AND AFTER COMPLETION

Upon Completion and assuming there is an immediate exercise in full of the conversion rights attaching to the Convertible Notes in aggregate of HK\$140,430,000 at the conversion price of HK\$0.093 by the holders thereof, the Company will issue an aggregate of 1,510,000,000 Conversion Shares, representing approximately 20.50% of the issued share capital of the Company as at the Latest Practicable Date, approximately 17.01% of the issued share capital of the Company as enlarged by the allotment and issue of the Conversion Shares (but not the Consideration Shares), and approximately 14.54% of the issued share capital of the Company as enlarged by the allotment and issue of the Conversion Shares and the Consideration Shares. The Conversion Shares will be issued pursuant to the passing of the relevant resolution at the EGM.

LETTER FROM THE BOARD

As at the Latest Practicable Date, there were two outstanding tranches of convertible bonds in the aggregate principal amount of HK\$28.9 million and 58,264,003 Shares may be issued and allotted upon exercise in full of the conversion rights attached to the aforesaid two tranches convertible bonds.

Details of the shareholding structure of the Company (i) as at the Latest Practicable Date, (ii) after Completion and the issue of the Consideration Shares but before the conversion of the Convertible Notes, (iii) after Completion, the issue of the Consideration Shares and the full conversion of the Convertible Notes, (iv) after Completion, the issue of the Consideration Shares and the conversion of the Convertible Notes (assuming that the conversion restriction of the Convertible Notes applies), and (v) after Completion, the issue of the Consideration Shares and the full conversion of the Convertible Notes, full conversion of the existing two tranches of convertible bonds of HK\$28.9 million and the issue of the consideration shares and full conversion of the convertible bonds upon completion of the very substantial acquisition announced by the Company on 22 October 2009; assuming that there is no other change in the share capital of the Company are set out below:

Name	Number of Shares held directly or indirectly as at the Latest Practicable Date (Note 1)		Number of Shares held after Completion and the issue of the Consideration Shares but before the conversion of the Convertible Notes		Number of Shares held after Completion, the issue of the Consideration Shares and full conversion of the Convertible Notes (Note 2)		Number of Shares held after Completion, the issue of the Consideration Shares and conversion of the Convertible Notes, assuming that the conversion restriction applies (Note 3)		Number of Shares held (1) after Completion, the issue of the Consideration Shares and full conversion of the Convertible Notes, (2) full conversion of the existing two tranches of convertible bonds of HK\$28.9 million, and (3) the issue of the consideration shares and full conversion of the convertible bonds upon completion of the very substantial acquisition announced by the Company on 22 October 2009 (Note 4)	
		%		%		%		%		%
Greater Finance Limited	-	-	-	-	-	-	-	-	16,250,000,000	60.88
Vendor	-	-	1,510,000,000	17.01	3,020,000,000	29.08	2,454,862,204	25.00	3,020,000,000	11.31
Public	7,364,586,614	100.00	7,364,586,614	82.99	7,364,586,614	70.92	7,364,586,614	75.00	7,422,850,617	27.81
Total	7,364,586,614	100.00	8,874,586,614	100.00	10,384,586,614	100.00	9,819,448,818	100.00	26,692,850,617	100.00

LETTER FROM THE BOARD

Notes:

1. To the best knowledge, information and belief of the Directors after making all reasonable enquiries, as at the Latest Practicable Date, the Company did not have any Shareholder holding 5% or more of the issued share capital of the Company.
2. The approximate percentage shown is for illustrative purpose only. Under the terms of the Convertible Notes, the Vendor shall not exercise the conversion rights attaching to the Convertible Notes such that (i) it and parties acting in concert with her, taken together, will directly or indirectly, control or be interested in 25% or more of the entire issued Shares or such percentage as may from time to time be specified in the Hong Kong Code on Takeovers and Mergers as being the level for triggering a mandatory general offer, whichever is lower, or (ii) the Company will be in breach of the minimum public float requirement under the Listing Rules.
3. As the Vendor cannot control or be interested in 25% or more of the entire issued Shares, less Conversion Shares will be issued by the Company to the Vendor (assuming that the remaining Conversion Shares are not issued).
4. The approximate percentage shown is for illustrative purpose only.

The Acquisition will not result in a change of control of the Company.

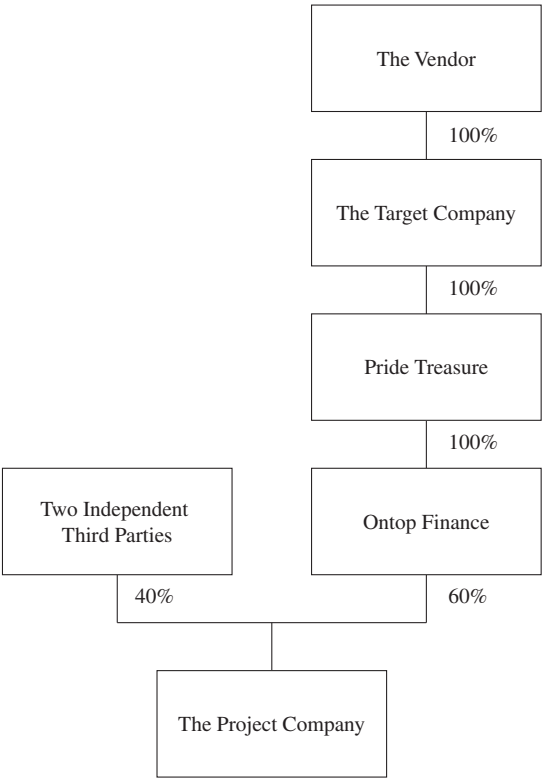
F. INFORMATION RELATING TO THE TARGET GROUP

The principal activities of the Vendor is investment holding. The Vendor and its ultimate beneficial owner are not related to Mr. Li Weijin and Greater Finance Limited, the counterparty to the very substantial acquisition announced by the Company on 22 October 2009 or to Ms. Leung Lai Ching Margaret, the counterparty to the very substantial acquisitions announced by the Company on 20 July 2007 and 18 April 2008 respectively.

The Target Company is an investment holding company incorporated under the laws of the British Virgin Islands on 20 October 2009 and is wholly owned by the Vendor. Based on the information provided by the Vendor, the Target Company does not have any asset other than its investment in Pride Treasure. Pride Treasure is an investment holding company incorporated under the laws of Hong Kong on 27 March 2009 and is wholly owned by the Target Company. Based on the information provided by the Vendor, Pride Treasure does not have any asset other than its investment in Ontop Finance. Ontop Finance is an investment holding company incorporated under the laws of Hong Kong on 29 April 2009 and is wholly owned by Pride Treasure. Based on the information provided by the Vendor, Ontop Finance does not have any asset other than its investment of 60% equity interest in the Project Company.

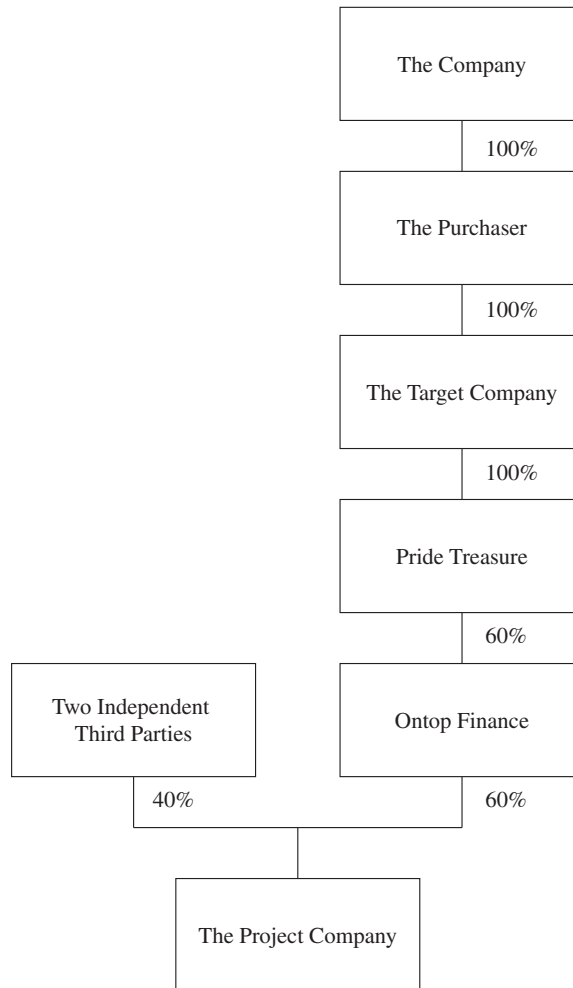
LETTER FROM THE BOARD

The corporate structure as at the Latest Practicable Date and immediately before Completion is as follows:



LETTER FROM THE BOARD

The corporate structure of the Enlarged Group immediately after the Completion is as follows:



The Project Company was incorporated under the laws of the PRC on 31 December 2005 as a domestic company with a registered capital of RMB85,000,000. In August 2009, with the approval from the relevant PRC government authorities, the Project Company was converted into a sino-foreign joint venture company with a registered capital of RMB185,000,000, of which RMB85,000,000 had been fully paid up as at the date of Agreement with Ontop Finance becoming the foreign shareholder of the Project Company. Under the agreement to increase registered capital made between Ontop Finance and the two original shareholders of the Project Company on 6 May 2009, Ontop Finance had agreed to inject RMB100,000,000 into the Project Company, of which approximately RMB30,450,000 had been paid by the Vendor pursuant to the Agreement. The remaining unpaid registered capital of approximately RMB69,550,000 (equivalent to approximately HK\$79,942,529) will be paid by the Purchaser. As at the Latest Practicable Date, the Project Company was held as to 60% by Ontop Finance, as to 31.68% by Zhongkai Group and the remaining 8.32% by Mr. Li Jinduo. To the best of the Directors' knowledge, information and belief having made all reasonable enquiries, both Zhongkai Group and Mr. Li Jinduo are Independent Third Parties and do not have any relationship with the Vendor and the Guarantor.

LETTER FROM THE BOARD

As at the Latest Practicable Date, the outstanding registered capital of approximately RMB69,550,000 (equivalent to approximately HK\$79,942,529) remained unpaid. As one of the conditions precedent to Completion, the Vendor has agreed to use its best endeavour to procure and obtain from the relevant PRC government authority to extend the time for paying up the registered capital to a date not earlier than 1 July 2011.

The injected capital of HK\$35,000,000 (equivalent to approximately RMB30,450,000) was deposited to one of the bank accounts in PRC owned by the Project Company and has been retained as working capital of the Project Company. It is the intention of the Project Company to utilise the said amount of injected capital only after Completion.

Although the registered capital of the Project Company has not been fully paid up, according to the PRC legal opinion issued by Shanxi Jiajing Law Firm (山西佳鏡律師事務所), since the relevant government authority of Shanxi Government has approved that Ontop Finance can hold 60% of the shareholding in the Project Company, and that the updated business licence of the Project Company has been issued by Shanxi Administration for Industry and Commerce (山西省工商行政管理局) on 11 August 2009, which states Ontop Finance as a shareholder holding 60% equity interest in the Project Company, therefore, it is the opinion of Shanxi Jiajing Law Firm that Ontop Finance has held 60% equity interest in the Project Company since the date of the business licence (i.e. 11 August 2009).

In addition, Shanxi Jiajing Law Firm further confirmed that Ontop Finance has obtained the control of the Project Company since 11 August 2009 through controlling the majority of the Project Company's board of directors and the legal representative. Pursuant to the articles of the Project Company dated 6 May 2009, Ontop Finance is entitled to nominate up to three directors out of the five directors in the board of directors of the Project Company, which has the power to further appoint the general manager, financial controller and the other senior management personnel of the Project Company. In this respect, Ontop Finance has nominated three directors to the board and appointed the legal representative of the Project Company. Therefore, despite the additional registered capital is yet to be fully injected or paid, Ontop Finance has already obtained the control of the Project Company, and thereby the Project Company shall be accounted for a subsidiary of Ontop Finance.

G. INDUSTRY OVERVIEW

Supply and demand for electricity in the PRC

The PRC is one of the fastest growing economies in the world. According to the figures published by the International Monetary Fund in World Economic Outlook Database as in April 2009 and BP Statistical Review of World Energy as in June 2009, since 2001, electricity generation in the PRC has grown at a rate higher than the PRC's GDP in most years. It is believed that the faster growth of electricity generation since 2001 has largely been driven by rapid industrialisation and also by rising residential electricity demand as per capita income increased.

According to the China Electric Power Yearbook of 2008, the PRC had an aggregate installed capacity of approximately 793 GW at the end of 2008, compared to 338.6 GW at the end of 2001 (i.e. increased by 134.2%), and the PRC's total electricity generation mostly grew faster than its installed capacity since 2001 (especially during the period of 2001 to 2004), from 1,480.8 TWh to 3,433.4 TWh in 2008 (i.e. increased by 131.86%), resulting in increasing utilisation hours from 2001 to 2004. However, starting in 2005, installed capacity began to outpace demand for power throughout the PRC. This trend has caused utilisation hours to decrease between 2004 and 2008.

LETTER FROM THE BOARD

Despite the above-mentioned high rate in increase in both the economy growth and electricity generation, according to the BP Statistical Review of World Energy of June 2009, the PRC has the lowest per capita electricity generation among other countries like the United States of America and Japan.

Future plan for the PRC power industry

Energy scarcity and environmental deterioration are major global concerns. Due to the rapid economic development, rising living standards and continuous increase in per capita energy consumption in the PRC, energy shortage has been a limiting factor for the PRC's economic development. As such, in the outline of the Eleventh Five Year Plan for National Economy and Social Development (the “**Eleventh Five Year Plan**”) published in 2005, the PRC government suggested a number of energy conservation and environmental protection policies and national targets for 2006 to 2010. Some of the PRC government's targets mentioned in the Eleventh Five Year Plan include reduction of energy consumption per unit of GDP by 20% and significant expansion of highly efficient energy sources, including wind, hydroelectric, natural gas, nuclear, other renewable sources and cogeneration. The Directors believed that the demand for electricity in the coming years will continue.

History on restructuring of the PRC power industry

Change in supervisory regime

In January 1997, the State Power Corporation was established to take ownership of the state-owned power generation assets and virtually all of the high voltage power transmission grids and local electricity distribution networks in the PRC. The State Power Corporation was responsible for the investment, development, construction, management, operation and ownership of power plants, the inter-connections of interprovincial and interregional electricity grids, and the transmission of electricity across regions. As a result of further restructuring of the PRC power industry, in December 2002, the State Power Corporation was reorganised into two power grid companies and five large independent power generation groups. The two power grid companies are State Grid and the China Southern Power Grid Company (中國南方電網有限公司) (“**Southern Grid**”). In 2002, the State Electricity Regulatory Commission of the PRC (國家電力監管委員會), a new regulator of the electric power industry was established under the State Council. The main responsibilities of the State Electricity Regulatory Commission include ensuring fair competition in the electric power industry, monitoring the quality and standard of power plant production, administering electric power business permits and handling electric power market disputes.

Transmission and dispatch

All electricity generated in the PRC is dispatched by power grid companies, except for the electricity generated by power plants which are not connected to a grid. The electricity dispatched to each grid is administered by dispatch centers owned and operated by the power grid companies. The main system for the transmission and distribution of power in the PRC consists of the five interprovincial power grids owned by State Grid and six power grids owned by Southern Grid.

LETTER FROM THE BOARD

In order to achieve a more efficient and rational dispatch of electric power, the State Council issued, with effect from 1 November 1993, the Regulations on the Administration of Electric Power Dispatch to Networks and Grids (《電網調度管理條例》) (the “**Dispatch Regulations**”). Under the Dispatch Regulations, dispatch centers were established at each of the five levels: the national dispatch center, the dispatch centers of the interprovincial power grid, the dispatch centers of the provincial power grid, the dispatch centers of the power grid of municipalities under provinces and the dispatch centers of the county power grid. Dispatch centers are responsible for the administration and dispatch of planned output of power plants connected to the grid. Each power plant will receive on a daily basis from its local dispatch center an expected hour-by-hour output schedule for the following day, based on expected demand, the weather and other factors.

On-grid tariffs

An on-grid tariff is the tariff that the grid companies are required to pay to the companies generating the electricity. Different on-grid tariffs are applicable to planned output, excess output and output subject to competitive bidding. For further information on on-grid tariffs, please see the paragraph headed “M. Regulatory Environment – Applicable regulatory scheme on the operation of the Project Company – On-grid tariffs and electricity prices” below.

Electricity generation industry at provincial and county level – Shanxi Province and Lingshi County

Overview of electricity industry in Shanxi Province

According to the figures issued by the China Electricity Council in its annual report of 2009, as of 30 June 2009, the total power installed capacity (with unit capacity over 6,000 kW) in Shanxi Province was 37,040 MW, and the net power generation by all power sources was 44,030 GWh, which respectively ranks the 8th and 10th among all the provinces and municipality in the PRC. Shandong is the province with the most total power installed capacity (with unit capacity over 6,000 kW) at 58,070 MW, whilst Guangdong had the largest figure of net power generation by all power sources at 141,532 GWh. These figures reveal that in relation to the electricity generation, Shanxi Province has reached a high-middle level compared to other provinces and municipalities.

Shanxi Province’s policy on electricity industry

Shanxi Province is grouped under the North China Grid Company Limited (華北電網有限公司) under State Grid. In addition to the usual State Grid practices, pursuant to the Eleventh Five Year Plan, the provincial government published the Proposal for Reconstruction and Advancement of Electricity Industry of Shanxi Province (山西省電力產業調整和振興規劃) (the “**Shanxi Electricity Proposal**”) and the Proposal for Promoting Combined Heat and Power Generation (關於推進城市熱電聯產的實施方案) (the “**Combined Generation Proposal**”) in 2009 to outline the proposal for electricity development in Shanxi Province in the following years.

LETTER FROM THE BOARD

The Shanxi Electricity Proposal outlined the following targets in relation to the electricity industry in Shanxi:

- (i) to increase the total installed capacity;
- (ii) to eliminate outdated plant for better environmental protection;
- (iii) to improve the technical effectiveness of the installed facilities;
- (iv) to reorganise the electricity network;
- (v) to promote the combined heat and electricity generation; and
- (iv) to promote energy saving and less pollutants emission.

In order to meet the above targets, the Shanxi Electricity Proposal proposed various tasks and actions to be taken, including (1) to intensify the elimination of outdated and below-standard facilities; (2) to promote the re-organisation of electricity generation companies; (3) to restructure the components of sources of electricity, especially to increase the contribution by recyclable and environmental friendly means of electricity generation like hydro, solar and wind electricity; (4) to improve the electricity infrastructure in Jinbei, Jinzhong and Jindong; (5) to develop the 'export' market in neighbour provinces for electricity generation; and (6) to improve the infrastructure and facilities for intra- and inter-provincial electricity transmission.

In order to provide further practical information on the implementation of the Shanxi Electricity Proposal, the Combined Generation Proposal was issued in October 2009 as it is Shanxi Province's priority to increase the number of power plants which can generate and supply electricity and heat simultaneously.

LETTER FROM THE BOARD

Information on Lingshi County

Social-demographical information of Lingshi County



Figure 1. Shanxi Province in the PRC (shown in light grey) and Jinzhong City (shown in dark grey)



Figure 2. Location of Lingshi County in Jinzhong City of Shanxi Province (around the circled area)

Lingshi County (靈石縣) is a county under the administration of Jinzhong City (晉中市) in Shanxi Province (山西省) of the PRC with an area of approximately 1,206 square kilometers.

LETTER FROM THE BOARD

Coal is one of the most abundant mineral resources found in Lingshi County, and coal industry is one of the major economic industries in Lingshi County. There are four major coal mines in Lingshi County, and there are around 200 companies operating in coal-related businesses. The coal-related industry is growing rapidly and it is expected that more coal manufacturing and advancing factories will be built in Lingshi County. The rapid development of coal-related and various industrial businesses will increase the demand for electricity in Lingshi County. The Directors believed that as there will be more working opportunities in Lingshi County due to the steady growth of industrial businesses, urbanisation will be rapid, which can also contribute to the increase in demand for electricity (and also heat).

Lingshi County's policies towards electricity industry

As disclosed previously, one of the proposals under the Combined Generation Proposal is the establishment of power plants which can supply electricity and heat simultaneously in different prefecture-level cities and counties in Shanxi Province. The target is to ensure that there is at least one large heat and electricity combined generation plant in each prefecture-level city. For Jinzhong City, plans on establishing or improving plant for various counties are provided, but there is no plan for Lingshi County specified. Although there is no specified target for Lingshi County in relation to the establishment of heat-electricity combined generation plant, other guiding principles for improving electricity generation including energy-saving, efficiency enhancement, better project management and supervision and environmental protection and wastage emission elimination should be observed by the local government of Lingshi County.

The local government of Lingshi County issued an Outline for Lingshi County's Economic and Social Development Plan (Draft) (靈石縣國民經濟與社會發展第十一個五年規劃綱要(草案)) (the "**Lingshi Development Outline**") on 13 November 2009, setting out its policy towards different industries in Lingshi County including the electricity industry. The Lingshi Development Outline provided various targets for Lingshi County, including, (1) to ensure that 80% of the area in Lingshi County are covered by centralised heat and electricity supply network; and (2) to increase the recycling rate of coal stone created by the coal mines to 80%. The business of the Project Company is named as one of the twenty major development projects in Lingshi Development Outline.

Overview of heat supply industry

National policy: centralised heat supply in each county and incentives

Since 1998, in order to better supervise the quality of heat supplying, to improve the cost-efficiency in heat generating and to eliminate the environmental impacts of heat supplying, it is a national policy to centralise the heat supplying at prefecture-level city or county level. To this end, the Central Heat Transmit Station of Lingshi County (靈石縣城市集中供熱總站) (the "**Central Heat Station**") was established in June 2005.

In addition to the above, it is also a national policy to subsidise the heat generation business. According to the Notice of Continuance of Favourable Tax Policies to Heat Generating Business (關於繼續執行供熱企業增值稅、房產稅、城鎮土地使用稅優惠政策的通知) issued by the Ministry of Finance and the State Administration of Taxation on 10 February 2009, (i) in relation to the revenue generated by heat supplying companies to residents during November 2009 to March 2010, it shall be value-added tax free; (ii) from 1 January 2009 to 30 June 2011, the plants for heat generation to residents shall be exempted from property tax and use of city's land tax.

LETTER FROM THE BOARD

Further, it is also a national and provincial policy to encourage combined generation of heat and electricity due to the growing concern in environmental protection and recycling.

Under the national regulation of price levels, the local government of Lingshi County has discretion in determining the price for heat. In determining the price, the local government will take into account the costs of heat generation by the Project Company and the affordability of the local residence, and will from time to time pay a lump sum subsidy to the Project Company. The Project Company received RMB1,500,000, RMB3,000,000 and RMB3,000,000 in the years ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively as local government subsidy for its heat generation business, which represented approximately 14.1% and 6.5% of the profit (after tax) of the Project Company for the years ended 31 December 2008 and 31 December 2009 respectively. As for the year ended 31 December 2007, as the Project Company had just begun its operation for a few months after the construction period, a loss was recorded. Based on the above figures, the Directors are of the view that the Project Company does not highly rely on the local government subsidy.

Heat supply network in Lingshi County and future plan

Due to the urbanisation in Lingshi County, the area of heat supplying network in Lingshi County has been increasing, expanded from approximately 600,000 square meters in 2001 to approximately 1,500,000 square meters in 2006, and then to approximately 2,000,000 square meters in 2009. Due to the rapid expansion of the heat supply network, the local government of Lingshi County approved the Project Company's application in operation of heat and electricity supply in 2006, and the Project Company is the only heat supply which has obtained the permit for heat supply and joint operation with the Central Heat Station.

Due to the continuing urbanisation of Lingshi County, it is expected that the population will also increase rapidly. To cope with the increase in demand for heat supply subsequent to the increase in population in Lingshi County, it is estimated that by 2011 the area of heat supply network in Lingshi County will further increase by approximately 700,000 square meters. Therefore, the local government of Lingshi County has first arranged and financed the construction of new boiler in the site of the power plant of the Project Company in order to cope with the expected increase in demand for heat supply.

H. BUSINESS MODEL

The Project Company is engaged in the business of generating and supplying electricity and heat by using coke oven gas and alternatively, burning coal gravel or gangue, in the PRC.

Approval and required minimum capacity of generation

Under the current regulatory regime, the local State Grid manages the dispatch center of the county's power grid and is responsible for administrating and despatching the planned output of the power plants connected to the grid.

LETTER FROM THE BOARD

Pursuant to the approval document issued by the Economy Committee of Shanxi Province (山西省經濟委員會) on 3 April 2006, the Project Company's application for operating a combined heat and electricity generation plant was approved, and the Project Company was approved to generate not less than 168 million units (kWh) of electricity annually and not less than 723,700 GJ of heat annually (i.e. the minimum production capacity of the Project Company). Upon receipt of such approval, the Project Company obtained further approval from the local branch of State Grid for the dispatch of electricity and entered into an agreement for operating and supplying high-pressure electricity (高壓供用電合同) with the Jinzhong branch of State Grid (山西省電力公司晉中大用戶營業所) ("**Jinzhong Branch**") on 25 April 2007 (the "**2007 Dispatch Agreement**").

Jinzhong Branch is the local branch of the Central China Power Grid of State Grid which is responsible for supervising the supply and dispatch of electricity in the area of prefecture-level city of Jinzhong in the Shanxi Province. It has authority to enter into dispatch agreements with local electricity generator including the Project Company. Pursuant to the 2007 Dispatch Agreement, 40% of the electricity generated by the Project Company will be provided to State Grid whereas the Project Company is at liberty to sell the remaining 60% to its cooperation parties (協作單位) which are non-State Grid private entities. The tariffs of providing electricity to State Grid's network will be determined in accordance to the electricity price announced by the provincial price control bureau. There is no special condition imposed on the Project Company under the 2007 Dispatch Agreement for its sales and dispatch of electricity to non-State Grid private entities. The 2007 Dispatch Agreement will be renewed annually, and if there is no amendment to the agreement at the time of the renewal, the terms of the 2007 Dispatch Agreement will be automatically extended for one year. There is no other condition, performance or safety target which the Project Company will need to satisfy or follow before the renewal of the terms of the 2007 Dispatch Agreement. Since the execution of the 2007 Dispatch Agreement on 25 April 2007, the terms of the agreement have remained the same.

According to the Company's legal adviser as to PRC laws, (i) Jinzhong Branch has the authority to enter into the 2007 Dispatch Agreement on behalf of State Grid for regulating the dispatch of electricity including approving the Project Company to supply and dispatch electricity to its cooperation parties (i.e. non-State Grid entities); and (ii) the sale of electricity to customers other than State Grid is legal.

Pursuant to the 2007 Dispatch Agreement, the Project Company had supplied electricity to Jinzhong Branch for the three years ended 31 December 2009 and Jinzhong Branch had paid the Project Company approximately RMB472,000, RMB2,396,000 and RMB5,732,000 as the tariff for the Project Company's electricity in the years ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

Pursuant to the 2007 Dispatch Agreement, the tariff payable by Jinzhong Branch to the Project Company for the electricity dispatch to State Grid is determined according to the tariffs set by the relevant provincial price control bureau as no competitive bidding tariff-setting mechanism has been implemented under the Power Tariff Reform Plan (《電價改革方案》) issued in July 2003. The tariffs applicable to the Project Company has been RMB0.2344 per kWh since September 2007.

The Project Company commenced its business in or about September 2007. In the two years ended 31 December 2009, the Project Company generated more than 210 million kWh of electricity and 1 million GJ of heat, and met the minimum production capacity requirements in the PRC.

LETTER FROM THE BOARD

The combined heat and electricity generation power plant

The Project Company owns a piece of land situated in Nanwangzhong Village, Cuifeng Town, Lingshi County, Shanxi Province, the PRC with a total site area of approximately 76,666.67 square meters. The land is free from any charge or mortgage. A power plant and factory with an area of approximately 56,506.15 square meters was erected on the land, and in which about 380 employees were employed as at the Latest Practicable Date.

According to the PRC legal opinion issued by Shanxi Jiajing Law Firm (山西佳鏡律師事務所), the Project Company has obtained the long-term land use right certificate on 6 February 2007 on the use of the said piece of land for the purpose of running a plant for generating heat and electricity, and there is no expiry date for the said land use.

Operation processes

The Project Company operates a combined heat and electricity generation plant using coal waste or gangue from the many coal mines and processing plants in the area and coke oven gas from coking plants near the plant. During the initial stage in applying for permit to construct and operate the combined heat and power generation plant, the Project Company had intended to utilize coal wastes from neighboring coal related industries to good use.

The combined heat and electricity generation plant is located in Lingshi County, part of Jinzhong City of Shanxi Province, at the southern tip of the city, adjacent to Changzhi City and Linfen City about 150 kilometers away from Jinzhong City (Yuci District) and Taiyuan City. It lies in the Chengdong Industrial Zone, Lingshi County and approximately 3 kilometers away from the central area of the county, with good transportation conditions.

The combined heat and electricity generation plant consists of Thermal Plant I which began operation in 2004 with 2 x 6 MW generators and two sets of 35 t/h circulating fluidised bed boilers fired by coal waste from local coal mining operations and Thermal Plant II which began operation in 2007 with 2 x 12 MW generators and three sets of 85 t/h circulating fluidised bed boilers fired by coal waste and coke oven gas. In 2008, a flue gas desulfurisation system was added to Thermal Plant I to reduce SO₂ emissions. Limestone is used in Thermal Plant II for the fluidised bed and it is not necessary to install any desulfurisation equipment in Thermal Plant II. With such arrangement, the Project Company is entitled to the tariff surcharge for desulphurised coal power generators. During the winter months from November to March, steam produced at Thermal Plant II is exported to a two million square meters district heating system in the town of Lingshi County.

LETTER FROM THE BOARD

Thermal Plant I began its operation in 2004 and was previously operated by Shanxi Zhong Kai Group Zhongya Electricity Limited (山西中凱集團靈石中亞發電有限公司), which merged with the Project Company on 25 August 2007. The Project Company finished the construction of Thermal Plant II in mid-2007 and acquired Thermal Plant I at the same time. In September 2007, the Project Company started operating both Thermal Plant I and Thermal Plant II. The number of boilers and electrical generators and the installed capacity had remained the same during the three years ended 31 December 2009. The Project Company did not start to operate the new boiler constructed under the expansion plan in 2009. But as advised by the Vendor, the Project Company has intended to start operating the said new boiler in late 2010. The following table summarize the key information on the stores and electrical generations installed in Thermal Plants I and II:

	Capacity	In Service Date	Fuel
Thermal Plant I			
Boiler 1	35 Tph steam	May 2004	Coal Gangue
Boiler 2	35 Tph steam	December 2004	Coal Gangue
Electrical Generator 1	6 MW	May 2004	N/A
Electrical Generator 2	6 MW	December 2004	N/A
Thermal Plant II			
Boiler 1	75 Tph steam	August 2007	Gangue, Coke oven gas
Boiler 2	75 Tph steam	August 2007	Gangue, Coke oven gas
Boiler 3	75 Tph steam	August 2007	Gangue, Coke oven gas
Electrical Generator 1	12 MW	July 2007	N/A
Electrical Generator 2	12 MW	November 2007	N/A

LETTER FROM THE BOARD

The following tables show the highlights of key technical information of the boilers and power generators installed in the plant of the Project Company:

Year		2007	2008	2009
Power generated (kWh)		56,378,451	216,312,636	217,453,830
Thermal Plant I	Generator 1	11,296,000	28,012,889	38,491,968
	Generator 2	20,464,000	34,104,643	34,202,312
Thermal Plant II	Generator 1	14,651,071	80,157,454	70,944,180
	Generator 2	9,967,380	74,037,650	73,815,370
Volume of heat sales (GJ)		388,045	1,082,792	1,361,782
Fuel (Coal ubsk/gangue) Usage (in tons)				
Aggregate consumption		127,040	356,316	482,997
Thermal Plant I consumption		82,104	70,135	129,895
Boiler 1		43,515	37,172	68,844
Boiler 2		38,589	32,963	61,051
Thermal Plant II consumption		44,936	286,181	353,102
Boiler 1		16,177	92,526	113,589
Boiler 2		15,278	109,536	134,019
Boiler 3		13,481	84,119	105,494
Fuel (coke over gas) Usage (Nm³/h)				
Thermal Plant II	Boiler 1	11,492,595	29,737,816	23,365,136
	Boiler 2	11,924,280	25,971,216	24,440,144
	Boiler 3	10,629,225	22,489,656	21,182,544

LETTER FROM THE BOARD

Operating hours (hours)		2007	2008	2009
Thermal Plant I	Boiler 1	2,448.00	5,495.00	7,874.00
	Boiler 2	4,132.00	7,244.00	6,716.00
	Generator 1	2,433.00	5,800.00	7,725.00
	Generator 2	4,092.80	6,919.00	6,840.00
Thermal Plant II	Boiler 1	1,411.00	7,303.00	5,738.00
	Boiler 2	1,464.00	6,378.00	6,002.00
	Boiler 3	1,305.00	5,523.00	5,202.00
	Generator 1	1,629.00	7,314.00	6,449.00
	Generator 2	1,021.00	6,929.00	6,724.00
Utilisation %		2007	2008	2009
Thermal Plant I	Boiler 1	77.14	97.09	98.65
	Boiler 2	92.80	90.91	90.65
	Generator 1	76.85	95.89	96.40
	Generator 2	92.00	87.20	91.78
Thermal Plant II	Boiler 1	55.99	94.33	95.64
	Boiler 2	58.10	91.99	95.91
	Boiler 3	51.79	90.45	92.26
	Generator 1	76.55	94.55	84.58
	Generator 2	52.42	90.05	87.72

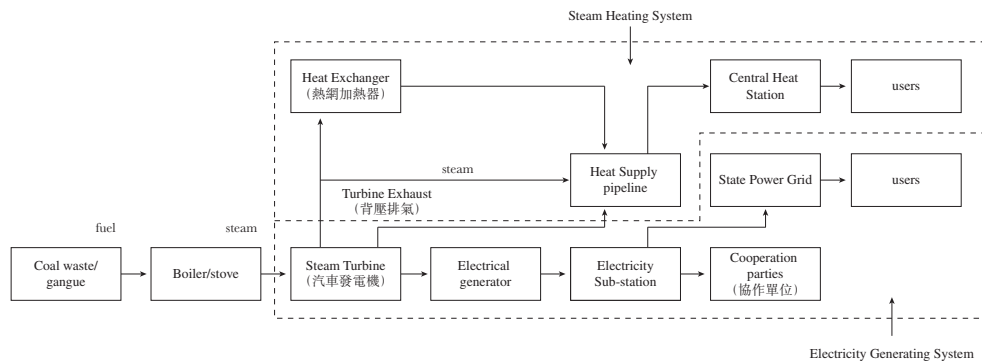
Internal control system

The Project Company has issued various guidelines to its employees in relation to the operation of the thermal plants and ancillary supporting units located in the combined heat and electricity power plant in compliance with the requirements under the Measures on Supervision and Administration of the Work Safety of Electricity Industry (《電力安全生產監督管理辦法》) and the work safety law (《中華人民共和國安全生產法》). As informed by the Vendor and to the best of the Directors' knowledge, information and belief having made all reasonable enquiries, up to the Latest Practicable Date, there had been no major breach of the safety regulations and laws in the PRC. The Project Company has also implemented an incident report system pursuant to which supervisors of the power plant are required to report any accident (whether major or minor) to the vice general manager immediate after an occurrence of an accident.

LETTER FROM THE BOARD

Heat and electricity generation and supply

The following diagram shows the operation of the Project Company in heat and electricity generation and supply:



The boilers/stoves produce steam through the combustion of gangue or coke oven gas. The steam then flows to the steam turbine generators where it drives the turbines to produce electricity. In Thermal Plant I, both boilers/stoves supply steam to a header which can then direct the steam from either boiler/stove to either turbine. In Thermal Plant II, all three boilers/stoves direct steam to a header system which can then supply steam to either steam turbine or to the steam heating system if a turbine is not operating. A steam heating system refers to those equipment responsible for the transmission of heat. A more efficient way to supply heating steam is to extract some of the steam from the steam turbines at a lower pressure after it has been used to drive a turbine, and then direct it to the steam heating system.

The Project Company has also installed a computerised system to supervise the operation of the respective electrical generators and boilers/stoves, which is further monitored by its staff.

Since the Thermal Plant I and II have been in operation for less than 6 and 3 years respectively, there was no plans for major overhaul as at the Latest Practicable Date.

Major customers

The majority of the Project Company's customers are private enterprises. Each of the six major customers of the Project Company has signed an electricity and heat supply agreement with the Project Company, some of these agreements last for a term of one year which will be automatically renewed for a further year at the end of each term.

LETTER FROM THE BOARD

i. Major customer for heat: Central Heat Supply Station of Lingshi County (靈石縣城市集中供熱總站) (the “Central Heat Station”)

The Central Heat Station is a subsidiary of the local government of Lingshi responsible for the supply of heat to all the residents in the Lingshi County during winter (from November to the end of March). In late October each year, the Central Heat Station will enter into a heat supply and purchase agreement with the Project Company to regulate the supply and purchase of heat during the coming winter. The latest heat supply and purchase agreement was entered into between the Central Heat Station and the Project Company on 29 October 2009 (the “**2009 Heat Agreement**”), pursuant to which the Project Company has agreed to provide heat to an area of approximately 2 million square meters from 18:00 on 31 October 2009 to 24:00 on 31 March 2010 at an agreed cost to be settled by the Central Heat Station monthly.

Pursuant to the 2009 Heat Agreement, the Project Company is required to prepare and complete a record of the heat supplied by it in the prescribed format which will be used by the Lingshi County Bureau of Quality and Technical Supervision (靈石縣品質技術監督局) as the basis of confirming the units of heat supplied by the Project Company each month. In addition, the costs for the installation of the meters for heat supplied and the ancillary equipment in the power plant and the corresponding maintenance fee for such meters and equipment will be borne by both parties in equal share. The Central Heat Station, the Lingshi County Bureau of Quality and Technical Supervision and the Project Company will each send one representative to collect information from the meters installed on the 15th and 30th day of each month. Based on such information, the volume of heat supplied by the Project Company during the relevant month will be confirmed. The unit price of heat was set at RMB20 per GJ under the 2009 Heat Agreement, which was determined by the local government of Lingshi County pursuant to the notice issued by Shanxi Provincial Price Control Bureau (山西省物價局) on 1 July 2010 (i.e. 晉價商字[2009]150號). Under the said notice, the Shanxi Provincial Price Control Bureau announced that each local government in Shanxi Province will have the discretion to determine the tariffs and unit prices of heat for its county/prefecture-level with reference to the circumstances of its local area. The unit price of heat stipulated under the 2009 Heat Agreement is subject to adjustment announced and directed by the Shanxi Provincial Price Control Bureau under the price control policy of the Shanxi Provincial Government from time to time.

The Project Company also entered into heat supply and purchase agreement with the Central Heat Station in 2007 and 2008 with terms materially the same as those of the 2009 Heat Agreement.

The Project Company supplied approximately 388,045GJ, 1,082,792GJ and 1,361,782GJ of heat to the Central Heat Station in the years ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, and the Central Heat Station spent approximately RMB4,829,288, RMB11,230,890 and RMB25,934,498 for its purchase of heat from the Project Company in the years ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, which accounted for approximately 17.7%, 12.7% and 25.9% of the total turnover of the Project Company during the respective periods.

As the Project Company is only allowed to supply heat through the Central Heat Station under the national policy of centralisation of heat supply, the Central Heat Station took up 100% of the heat supplied by the Project Company.

LETTER FROM THE BOARD

ii. Major customers for electricity

For the year ended 31 December 2007, 4 major customers of the Project Company, collectively spent approximately RMB19,700,676 for their purchase of electricity from the Project Company, which accounted for approximately 87.6% of the Project Company's turnover attributable to the sale of electricity. 2 out of the said 4 major customers are related parties to the Project Company, namely Zhongkai Group and 山西中凱集團靈石巨源石墨化有限公司 (in English, for identification purpose only, Shanxi Zhongkai Lingshi Juyuan Shimuhua Limited) ("**Juyuan Limited**"), which accounted for approximately 52.7% of the totally amount spent by the 4 major customers.

For the year ended 31 December 2008, 4 major customers (2 of which were also the major customers referred to in 2007), collectively spent approximately RMB61,932,777 for their purchase of electricity from the Project Company, which accounted for approximately 80.1% of the Project Company's turnover attributable to the sale of electricity. 2 out of the said 4 major customers are related parties to the Project Company, namely 山西中凱集團靈石能源開發有限公司 (in English, for identification purpose only, Shanxi Zhongkai Group Lingshi Power Company Limited) ("**Nungyuan Limited**") and Juyuan Limited, which accounted for approximately 66.2% of the totally amount spent by the 4 major customers.

For the year ended 31 December 2009, 3 major customers (2 of which were also the major customers referred to in 2008), collectively spent approximately RMB57,238,937 for their purchase of electricity from the Project Company, which accounted for approximately 77.0% of turnover the Project Company's attributable from to the sale of electricity. 1 out of the said 3 major customers are related parties to the Project Company, namely Nungyuan Limited, which accounted for approximately 56.6% of the totally amount spent by the 3 major customers.

The major customers mentioned above are companies situate at Lingshi County operating industrial businesses including manufacturing of steel, cement and processing of coal and fuel coke. For these customers, the Project Company has installed electricity substations, pressure transformers and separate meters for the supply of electricity (i.e. not dispatch through network under State Grid).

The particulars of the 4 major customers for electricity and their respective contribution to the Project Company's turnover are as follows:

(1) Juyuan Limited

Juyuan Limited is a local and private-owned company situate at Lingshi County engaged in the business of manufacturing of steel and production of steel related ancillary products. As at the Latest Practicable Date, Zhongkai Group held 53% of the equity interest in Juyuan Limited. On 2 February 2010, Juyuan Limited entered into an electricity supply and purchase agreement with the Project Company for an unspecified term, pursuant to which the Project Company shall supply not less than 3.8 million kWh of electricity to Juyuan Limited per month. Juyuan Limited spent approximately RMB4,329,480, RMB11,257,046 and RMB3,862,509 for the purchase of electricity from the Project Company in the year ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, which accounted for approximately 19.25%, 14.56% and 5.20% of the total turnover of the Project Company attributable from the sale of electricity in the respective periods.

LETTER FROM THE BOARD

- (2) 山西晉投夏工水泥有限公司 (*in English, for identification purpose only Shanxi Jintou Xiangong Cement Limited*) (“**Jintou Limited**”)

Jintou Limited is a state-owned enterprise situate at Lingshi County engaged in the business of production of cement and ancillary products. Jintou is an Independent Third Party. Jintou Limited entered into an electricity supply and purchase agreement with the Project Company for a term of one year commencing on 1 January 2009 (and the contractual term shall automatically renew annually unless the parties agree otherwise), under which the Project Company shall supply not less than 50 million kWh but not more than 90 million kWh electricity to Jintou Limited annually. Jintou Limited spent approximately RMB4,579,908, RMB6,526,812 and RMB10,572,947 respectively for its purchase of electricity from the Project Company in the years ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, which accounted for approximately 20.37%, 8.44% and 14.23% of the total turnover of the Project Company attributable from the sale of electricity in the respective periods.

- (3) 天星煤氣化有限公司 (*in English, for identification purpose only, Tianxing Meiqihua Limited*) (“**Tianxing Limited**”)

Tianxing Limited is a local and private-owned company situate at Lingshi County engaged in the business of production of fuel coke and ancillary products. Tianxing is an Independent Third Party. In around November 2007, Tianxing Limited entered into an electricity supply and purchase agreement with the Project Company for an unspecified term. In addition, no minimum volume of electricity required to be supplied by the Project Company was set out in the agreement. Tianxing Limited spent approximately RMB4,736,053, RMB11,383,092 and RMB14,285,474 for its purchase of electricity from the Project Company in the years ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, which accounted for approximately 21.06%, 14.72% and 19.22% of the total turnover of the Project Company attributable from the sale of electricity in the respective periods.

- (4) *Nungyuan Limited*

Nungyuan Limited is a local and private-owned company situate at Lingshi County engaged in the business of raw materials for steel production. As at the Latest Practicable Date, Zhongkai Group held 51% of the equity interest in Nungyuan. In around November 2007, Nungyuan Limited entered into an electricity supply and purchase agreement with the Project Company for an unspecified term. In addition, no minimum volume of electricity required to be supplied by the Project Company was set out in the agreement. Nungyuan Limited spent RMB24,597, RMB29,729,196 and RMB32,380,516 for its purchase of electricity from the Project Company in the years ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively, which accounts for approximately 0.11%, 38.46% and 43.57% of the total turnover of the Project Company attributable from the sale of electricity in the respective period.

LETTER FROM THE BOARD

Supply

The Project Company purchased approximately 127,000 tons, 356,300 tons and 483,000 tons of coal gravel/gangue for the generation of heat and electricity in the years ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively. For the periods mentioned, the average spot price of coal stone/gangue was approximately RMB60 per ton. To the best of the Directors' knowledge, information and belief having made all reasonable enquiries, the spot price of coal stone/gangue has remained rather stable in the previous years with fluctuations within the range of approximately RMB55 to 65 per ton.

The Project Company has not entered into any gravel of coal stone/gangue supply agreement with any supplier. The intensity of coal-processing factories and industries creates much gravel of coal and gangue, and therefore there has always been a steady spot market in Lingshi County from which the Project Company could purchase coal stone/gangue at a favourable and steady price (since the supply is abundant). The Project Company believed that it is not necessary to enter into long term coal stone supply agreements with any one particular supplier.

In addition to burning coal gravel/gangue for steams, coke oven gas is also used in Thermal Plant II for running the electrical generators. The coke oven gas utilised by Thermal Plant II was transmitted from the neighbouring coal-processing factories through the pipes connected to Thermal Plant II, which will be otherwise emitted to the air through vertical pipes. Since emission of coke oven gas to air will increase the environment duties payable by neighbouring factories, the neighbouring factories are willing to cooperate with the Project Company and to supply coke oven gas to the Project Company free of charge. Coke oven gas is used as major fuel for Thermal Plant II whereas coal waste/gangue is used as major fuel for Thermal Plant I and supplemental fuel for Thermal Plant II.

I. MANAGEMENT DISCUSSION AND ANALYSIS OF THE TARGET GROUP

The Target Company

The Target Company was incorporated on 20 October 2009 and is an investment holding company. As at 31 December 2009, the Target Company had three subsidiaries, namely, Pride Treasure which was incorporated on 27 March 2009, Ontop Finance which was incorporated on 29 April 2009 and the Project Company which was incorporated on 31 December 2005. Given that the Target Company, Pride Treasure and Ontop Finance are investment holding companies and have not involved in any other business transactions other than their investments in the Project Company and the Project Company has only become a 60% owned subsidiary of the Target Company since 4 November 2009 (the acquisition date of Pride Treasure by the Target Company); the details of the accountants' report of the Project Company for the three years ended 31 December 2009 are set out in Appendix II to this circular; and the impact of consolidating the Project Company to the Group's financial position upon Completion are set out in the unaudited pro forma financial statement of the Enlarged Group and disclosed in note (a) of pro forma adjustments as set out in Appendix V to this circular, the financial statements of the Project Company were not consolidated in the accountants' report of the Target Group as set out in Appendix I to this circular.

LETTER FROM THE BOARD

Since the Project Company will become a non-wholly owned subsidiary of the Company upon Completion and the Company will adopt Hong Kong Financial Reporting Standards (“HKFRS”) 3 (Revised) – Business Combinations and Hong Kong Accounting Standard 27 – Consolidated and Separate Financial Statements (“HKAS 27”) to consolidate its results into the Group, the financial statements of the Project Company will not depart from HKAS 27 upon Completion.

Given that each of the Target Company, Pride Treasure and Ontop Finance has not conducted any other business since its incorporation, no turnover was recorded for the period from 20 October 2009 (date of incorporation) to 31 December 2009. Based on the consolidated balance sheet of the Target Group (excluding the Project Company) as at 31 December 2009 as set out in Appendix I to this circular, the sole asset of the Target Group (excluding the Project Company) comprised of the investment in subsidiaries of HK\$35,000,000 and the cash balance of HK\$6,231 and the total liabilities of HK\$35,060,631 which were mainly the amount due to ultimate parent and a director and accruals.

The Project Company

Set out below is certain financial information extracted from the accountants’ report of the Project Company for the three years ended 31 December 2009 prepared under Hong Kong Financial Reporting Standards, details of which are included in Appendix II in this circular.

	For the year ended 31 December 2007 <i>RMB’000</i>	For the year ended 31 December 2008 <i>RMB’000</i>	For the year ended 31 December 2009 <i>RMB’000</i>
Net Profit/(loss) before taxation	(7,147)	29,818	56,882
Net Profit/(loss) after taxation	(5,649)	21,262	46,109
	As at 31 December 2007 <i>RMB’000</i>	As at 31 December 2008 <i>RMB’000</i>	As at 31 December 2009 <i>RMB’000</i>
Total assets	262,928	305,338	349,983
Total liabilities	185,896	207,044	175,579
Net assets	77,032	98,294	174,404

Upon Completion (if so completed), the Project Company will become a 60% owned subsidiary of the Company.

LETTER FROM THE BOARD

Business overview

The Project Company is principally engaged in the generation and supply of heat and electricity to customers in the PRC and commenced the business from September 2007. Revenue from sale of power is recognised upon the transmission of electricity and heat to the customers as determined based on the volume of electricity and heat transmitted and the applicable fixed tariff rates agreed with the respective customers annually. The Project Company reported turnover of approximately RMB27,317,000, RMB88,528,000 and RMB100,248,000 for the years ended 31 December 2007, 2008 and 2009 respectively. Turnover increased 13% in 2009 as there was an increase in revenue from sale of heat as a result of rising demand from the growing population in Lingshi County and the cold winter weather.

The supply of heat contributed approximately RMB4,829,000, RMB11,231,000 and RMB25,934,000 to the Project Company's revenue for each of the three years ended 31 December 2009. The supply of electricity contributed approximately RMB22,488,000, RMB77,297,000 and RMB74,313,000 to the Project Company's revenue for each of the three years ended 31 December 2009.

The net loss of RMB5,649,000 was recorded for the year ended 31 December 2007 was mainly due to the administrative expenses and finance costs incurred since the commencement of business. After its first anniversary of operation, the Project Company recorded a net profit of approximately RMB21,262,000 for the year ended 31 December 2008. The profit for the year ended 31 December 2009 amounted to RMB46,109,000, which registered a growth of approximately 1.2 times over 2008. The growth was mainly attributable to (a) the increase in revenue of approximately RMB11,720,000, (b) the increase in rental income of approximately RMB7,945,000 and (c) imputed interest income on interest-free loan from a related company and a shareholder of approximately RMB8,194,000 recorded for the year ended 31 December 2009. It contributes a stable profit and steady cash flow and return to the owners of the Project Company.

Gross profit margins

The gross profit margins for each of the three years ended 31 December 2009 were 7%, 40% and 41%, respectively. The low gross profit margin in 2007 was mainly due to the start-up costs incurred for the power plant in its first year operation. With secured sales contracts from its major customers, gross profit margin of the Project Company was at a steady level of about 40% for the years ended 31 December 2008 and 2009.

Cost of sales mainly represents raw materials, direct staff costs, depreciation of plant and machinery and other production costs. The raw materials consumed by the Project Company are mainly coal stone or gangue which can be purchased at a spot market in Lingshi County at a stable price.

Other income

Other income mainly consists of government grants, rental income from the lease of power generators and electricity supply line, imputed interest from interest-free loan from a shareholder and a related company.

LETTER FROM THE BOARD

The Project Company initially entered into an agreement with a customer for granting a right to the customer for the use of certain power generating facilities for a term of 3 years from August 2008 to August 2011 at an annual rental of RMB12 million. However, as the economy is picking up in late 2009, the management has liaised with the customer for the early termination of the lease. The lease agreement has then been terminated with effect from November 2009 by mutual agreement. Rental income from the lease of power generators amounted to RMB4,955,000 and RMB10,000,000 for the years ended 31 December 2008 and 2009 respectively.

For the year ended 31 December 2009, the Project Company also recorded a rental income from the lease of electricity supply line of RMB2,900,000, which is expected to be a non-recurrent income.

Administrative expenses

Administrative expenses primarily consist of staff costs and general office expenses. The administrative expenses represented 14%, 4% and 5% of the Project Company's turnover for each of the three years ended 31 December 2009, respectively.

Other operating expenses

Other operating expenses mainly represent amortization of prepaid land lease payments and depreciation of office equipments, furniture and fixtures.

Finance costs

Finance costs mainly represent bank loan interest, which increased from RMB5,555,000 in 2007 to RMB9,200,000 in 2008. The bank loan was arranged for the purchase of property, plant and equipment for the establishment of the power plant in 2007. Finance cost decreased by 47% from 2008 to 2009 was mainly due to the repayment of bank loan subsequent to 2007.

Accruals and other payables

Accruals and other payables are primarily comprised of payables for the purchase of property, plant and equipment, payables for other taxes, customer deposits, receipts in advance, accruals and other payables.

Payables for the purchase of property, plant and equipment was RMB36,668,000, RMB19,852,000 and RMB16,280,000 as at 31 December 2007, 2008 and 2009, respectively. The decreasing trend reflected the decrease in construction payables as the substantial construction work of the power plant was completed in 2007.

Payables for other taxes was RMB1,856,000, RMB8,665,000 and RMB14,637,000 as at 31 December 2007, 2008 and 2009, respectively. The increase was mainly due to the increase in value added tax payables as a result of sales growth during the years from 2007 to 2009.

Customer deposits, and receipts in advance was RMB2,797,000, RMB9,659,000 and RMB5,469,000 as at 31 December 2007, 2008 and 2009, respectively. The increase as at 31 December 2008 was due to the increase of advance payments received from customers for the supply of electricity and heat in the period.

LETTER FROM THE BOARD

Statements of financial position

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Non-current assets			
Property, plant and equipment	221,608,921	236,695,378	239,238,009
Prepaid land lease payments	26,714,593	26,158,039	25,601,485
Deferred tax assets	2,095,447	3,099,452	1,936,285
	<u>250,418,961</u>	<u>265,952,869</u>	<u>266,775,779</u>
Current assets			
Inventories	228,896	1,146,573	2,453,225
Trade and bills receivable	3,006,518	1,135,451	9,472,925
Prepayments, deposits and other receivables	5,600,000	7,522,671	11,027,128
Due from fellow subsidiaries	49,992	2,903,696	–
Due from a shareholder	–	–	5,500,000
Due from a related company	1,537,125	24,983,753	22,636,487
Bank and cash balances	2,086,172	1,692,810	32,117,277
	<u>12,508,703</u>	<u>39,384,954</u>	<u>83,207,042</u>
Total assets	262,927,664	305,337,823	349,982,821
Current liabilities			
Trade payables	5,212,838	4,036,004	12,943,048
Accruals and other payables	44,244,402	44,799,307	47,287,294
Due to fellow subsidiaries	–	1,067,824	–
Due to a shareholder	2,000,000	–	–
Due to a related company	–	–	1,065,519
Due to the former ultimate parent	51,638,516	85,280,457	–
Tax payables	–	9,560,000	19,169,643
Bank loans	42,800,000	32,300,000	20,900,000
	<u>145,895,756</u>	<u>177,043,592</u>	<u>101,365,504</u>
Net current liabilities	<u>(133,387,053)</u>	<u>(137,658,638)</u>	<u>(18,158,462)</u>
Non-current liabilities			
Loan from a related company	–	–	6,317,004
Loan from a shareholder (the former ultimate parent)	–	–	47,896,714
Bank loans	40,000,000	30,000,000	20,000,000
	<u>185,895,756</u>	<u>207,043,592</u>	<u>175,579,222</u>
NET ASSETS	<u>77,031,908</u>	<u>98,294,231</u>	<u>174,403,599</u>
Current ratio	0.09	0.22	0.82
Gearing ratio (calculated on the basis of total liabilities over total assets)	0.71	0.68	0.50

LETTER FROM THE BOARD

Amount due from/to fellow subsidiaries, related companies and former ultimate parent represent balances arising from trading transactions and current accounts with the fellow subsidiaries, related companies and former ultimate parent. The Project Company carries out the trading transactions with its fellow subsidiaries, related companies and former ultimate parent in the normal course of business. The trading transactions represent the supply of electricity by the Project Company during the three years ended 31 December 2009. The credit terms given to customers vary and are generally based on the financial strength of individual customers. The Project Company normally grants 60-90 days credit period to third party customers and 180 days to related companies. Related companies are subsidiaries of Zhongkai Group.

Amount due from/to a shareholder represent balances arising from current accounts with the shareholder. The current account comprises advances from/to a shareholder. The balance is unsecured, interest free and with no fixed terms of repayment.

Loan from a related company represents balance arising from current account with the related company. The balance is unsecured, interest free and matures in September 2012.

Loan from a shareholder (the former ultimate parent) represents balance arising from current account with the shareholder which was also a former ultimate parent prior to 11 August 2009. The balance is unsecured, interest free and matures in August 2012.

Financial resources, capital structure, gearing ratio and liquidity

The source of fund was mainly from the cash generated from operations, loan advanced by the original shareholder and bank loans. The loan from original shareholder are unsecured and interest free. The bank loan of RMB50,000,000, RMB40,000,000 and RMB33,000,000 as at 31 December 2007, 2008 and 2009 respectively were secured by a charge over the property of a former fellow subsidiary/related company of the Project Company. Please refer to the above table for the information of the nature of major assets and liabilities, gearing ratio and liquidity of the Project Company for each of the three years ended 31 December 2009.

Significant investments, material acquisition and disposal

The Project Company did not have any significant investments, material acquisition and disposals for each of the three years ended 31 December 2009.

Capital commitment

The Project Company had capital commitment as at 31 December 2007, 31 December 2008 and 31 December 2009. Please refer to the details on page 115 in Appendix II to this circular. Save as aforesaid, the Project Company did not have any significant capital commitment as at 31 December 2009.

Treasury policies

The Project Company had no formal treasury policy and did not enter into any form of financial arrangement for hedging for each of the three years ended 31 December 2009.

LETTER FROM THE BOARD

Exchange rate exposure

The Project Company did not have significant foreign currency operations, which exposed the Project Company to foreign currency. The Project Company did not have a foreign currency hedging policy during the years.

Contingent liabilities

The Project Company did not have any contingent liabilities as at 31 December 2007, 31 December 2008 and 31 December 2009.

Employment and remuneration policy

As at 31 December 2007, 31 December 2008 and 31 December 2009, the Project Company had employed about 250, 300 and 380 full time managerial, administrative employees respectively, the Project Company affords competitive remuneration package to its employee based on prevailing and industry practice. The staff costs were approximately RMB6,034,000, RMB7,852,000 and RMB8,701,000 for the years ended 31 December 2007, 31 December 2008 and 31 December 2009 respectively.

Pledge of assets

As at 31 December 2007, 31 December 2008 and 31 December 2009, the Project Company secured a charge over the property of a former fellow subsidiary of the Project Company. The said former fellow subsidiary has become a related company of the Project Company since 11 August 2009.

Future plan

Pursuant to the expected increase in demand for both electricity and heat as discussed, it is the common understanding between the local government of Lingshi County and the Project Company upon several negotiations and discussions that the power plant of the Project Company shall be expanded to cope with such increase in demand by substantially increasing the capacity of heat and electricity generating of the Project Company. To secure the increase in capacity, the local government of Lingshi County verbally agreed to first finance the construction of new boilers and ancillary building in the power plant of the Project Company, and will afterwards further discuss and negotiate with the Project Company as to the assignment of the newly-constructed boilers and the consideration of the transfer.

The construction works for the expansion plan began in 2009, and three new boilers of capacity of 58 MW each together with a new plant building are expected to be built at the power plant of the Project Company, which may increase the annual capacity of generation of heat by approximately 600,000 GJ. It is also expected that the new system will be able to transmit heat to an area of approximately 3 million square meters. The first stage of construction works (i.e. construction of one boiler and ancillary building) was completed in late 2009 and was fully financed by the local government of Lingshi County. Two further boilers will be constructed and such construction will be financed by the Project Company according to the verbal agreement made between the local government of Lingshi County and the Project Company. It is understood that the construction works for the boilers will be completed in late 2011. The estimated costs of construction for the first stage is approximately RMB59.79 million and RMB39.86 million for the remaining boilers. The

LETTER FROM THE BOARD

Project Company and the local government of Lingshi County has yet come to a formal and written agreement as to the acquisition price of the newly-constructed boiler or whether the local government will lease the boiler to the Project Company instead, or whether the costs borne by the local government will be treated as loan to the Project Company. As informed by the Vendor, it is the Project Company's current intention to enter into a formal written agreement with the local government of Lingshi County in relation to the operation of the newly constructed boiler as soon as practicable after its registered capital has been fully paid up. Based on the verbal agreement between the Project Company and the local government of Lingshi County, as all the construction works of the said expansion project were conducted on the piece of land owned by the Project Company, the Project Company will have the exclusive right to acquire and participate in the expansion project. The Company will comply with the applicable Listing Rules when Project Company and the local government of Lingshi County has come to an agreement in relation to the newly-constructed boiler.

The Company has obtained a feasibility report from Shanxi Changhe Heat and Electricity Plant Engineering and Surveying Design Limited (山西正和熱電工程勘測設計有限公司) in relation to the estimated costs and financial effects of the aforesaid expansion plan. According to the said feasibility report, in addition to the increase of heat generating capacity by approximately 600,000 GJ, after the new boilers start operation, Thermal Plant II will concentrate in electricity generation and its annual capacity of electricity generation will be increase by approximately 45 GWh, which is expected to increase the revenue from sale of electricity by approximately RMB20 million. Together with the expected increase of revenue from sale of heat by approximately RMB12 million (i.e. 600,000 GJ times RMB20, which is the current unit price of heat under the 2009 Heat Agreement), it is expected that the expansion plan will increase the annual turnover (before tax) of the Project Company by approximately RMB32 million, which is approximately 32.1% of the total expected costs of the expansion plan.

The capital required for the above-stated expansion plan and acquisitions will be obtained mainly through the additional share capital of RMB100 million to be injected by Ontop Finance and the Company. Other financing methods, including the debts financing and financing from the Company after the Completion will also be considered if required.

Related parties transactions

The following is a summary of the Project Company's transactions with related parties. Related parties transactions include a relevant transaction pursuant to section 161B of the Companies Ordinance. As such, the definition of related parties is different from the definition of connected persons under Chapter 14A of the Listing Rules.

	Transaction	Related Party	Nature of relationship
1.	Sale of electricity	Zhongkai Group	holding company ^(a)
2.	Purchase of fixed assets	Shanxi Zhong Kai Group Zhongya Electricity Limited (山西中凱集團靈石中亞發電有限公司) ("Zhongya")	holding company ^(b)
3.	Purchase of steams	Zhongya	holding company ^(b)
4.	Purchase of electricity	Zhongya	holding company ^(b)

LETTER FROM THE BOARD

	Transaction	Related Party	Nature of relationship
5.	Sale of electricity	Juyuan Limited (山西中凱集團靈石巨源石墨化有限公司)	fellow subsidiary of holding company ^(c)
6.	Sale of electricity (during the three years ended 31 December 2009)	Shanxi Zhong Kai Group Lingshi Properties Management Limited (山西中凱集團靈石物業管理有限公司) (“Zhong Kai Properties”)	fellow subsidiary of holding company ^(d)
7.	Sale of electricity	Nungyuan Limited (山西中凱集團靈石能源開發有限公司)	fellow subsidiary of holding company ^(e)
8.	Sale of electricity (during the two years ended 31 December 2009)	Shanxi Zhong Kai Group Lingshi Electrical Construction Limited (山西中凱集團靈石電建工程有限公司) (“Electrical Construction”)	fellow subsidiary of holding company ^(f)
9.	Sale of electricity (during the two years ended 31 December 2009)	Shanxi Zhong Kai Group Qilin Hotel Limited (山西中凱集團麒麟大酒店有限公司) (“Qilin Hotel”)	fellow subsidiary of holding company ^(g)

Notes:

- (a) Zhongkai Group held 51%, 73.32%, 79.2% and 31.68% of the equity interest in the Project Company during the period from 31 December 2005 to 24 August 2007, from 25 August 2007 to March 2008, from March 2008 to 10 August 2009 and since 11 August 2009 respectively.
- (b) Zhongya held 49% of the equity interest in the Project Company from 31 December 2005 to 24 August 2007. Zhongya was dissolved on 25 August 2007.
- (c) Zhongkai Group held 53% of the equity interest in Juyuan Limited at all material times.
- (d) Zhongkai Group held 80% of the equity interest in Zhong Kai Properties at all material times.
- (e) Zhongkai Group held 51% of the equity interest in Nungyuan Limited at all material times.
- (f) Zhongkai Group held 62.17% of the equity interest in Electrical Construction at all material times.
- (g) Zhongkai Group held 100% of the equity interest in Qilin Hotel from at all material times.

The Project Company was a subsidiary of Zhongkai Group before 11 August 2009. Since 11 August 2009, Zhongkai Group ceased to be the majority shareholder of the Project Company, and these companies are no longer the fellow companies of the Project Company since then.

Zhongkai Group, as a shareholder of the Project Company holding 31.68% of the equity interest of the Project Company, will become a connected person under Rule 14A.11(1) of the Listing Rules when the Project Company becomes one of the subsidiaries of the Company.

As at the Latest Practicable Date, Juyuan Limited, Zhong Kai Properties, Nungyuan Limited, Electrical Construction and Qilin Hotel, Zhongkai Group were subsidiaries of the shareholder of the Project Company, they will all become Connected Persons when the Project Company becomes a subsidiary of the Company.

LETTER FROM THE BOARD

Management expertise

The following are the biographical details of the senior managing personnel of the Project Company:–

Mr. Li Jinxu (李金胥), aged 51. Mr. Li previously worked in the Lingshi County's local branch of State Grid since 1980 and was prompted as a general manager and later promoted to be the vice-general manager of Jinzhong branch of State Grid in 2000. After working in local branch of State Grid for more than 25 years, Mr. Li later left State Grid and found Zhongkai Group, the former majority shareholder of the Project Company, which later established the Project Company in late 2005. Mr. Li is currently the chief executive officer of both Zhongkai Group and the Project Company and is the chairman of the board of directors of the Project Company. In relation to Project Company, Mr. Li is responsible for liaison with local authorities in relation to the operation of the Project Company and the expansion plan and cooperation, liaison with major customers and to make major decisions in relation to the operation of the Project Company.

Mr. Pei Chiqiang (裴志強), aged 51. Mr. Pei previously worked for Coal Stone Logistics Company of Lingshi County, Shanxi (山西靈石煤炭運輸公司) since 1978 and was later prompted as a vice-general manager and general manager for years. In 2005, Mr. Pei joined the Project Company as the general manager. Mr. Pei is responsible to implement the resolutions and decisions passed by the board of directors of the Project Company and to attend the meetings of board of directors, draft and implement internal control and financial control codes for the Project Company and to overlook and supervise the daily operation of the Project Company.

Mr. Zhang Jianzhong (張建中), aged 50. Mr. Zhang has been working in different industrial entities in Lingshi County for different positions, including working as a electrical technician in Hemp Factory of Lingshi County of Shanxi Province (山西靈石麻紡廠) from 1982 to 1990, as a manager of technical department of Resin Factory of Lingshi County of Shanxi Province (山西靈石樹脂廠) from 1990 to 1999 and as a chief engineer of Shanxi Lingshi County Calcium Carbide Company Limited (山西靈石電石有限公司) from 1999 to 2005. Mr. Zhang joined the Project Company in late 2005 and is currently the vice-general manager and the chief supervisor of Thermal Plant II of the Project Company, and he is responsible for supervising the operating of Thermal Plant II including but not limited to the implementation of safety regulations and the due operation of the machineries installed in the plant.

LETTER FROM THE BOARD

J. REASONS FOR ENTERING INTO THE AGREEMENT

The Company is an investment holding company and its subsidiaries are principally engaged in trading of a wide range of carpets and the exploration and mining of natural resources.

The Company intends to expand its existing business to generating and supplying electricity and heat by using coke oven gas (or alternatively, by burning coal gravel) in the PRC, which, the Directors believed has ample growth opportunities due to the increased demand for electricity caused by the continued growth of the PRC and Lingshi County's economy. The use of coke oven gas to create electricity and heat can not only help to reduce this hazardous gas, but it also benefits the environment by avoiding disposal of wasted coal gravel created by neighbouring coal-related business. In addition, coke oven gas is of lower cost when compared with other fuel such as natural gas or heavy oil. The Directors considered that the Acquisition represents an opportunity for the Group to enter into the power generation industry, and believed that the Group could broaden its source of income by vertically diversifying into such industry.

The Board has considered the unaudited total tangible assets value per Share as at 30 June 2009 of HK\$0.012 in determining the issue price of the Consideration Shares and conversion price of Convertible Notes. The issue price of the Consideration Shares and conversion price of HK\$0.093 per Share represented a premium of about 675% over the unaudited total tangible assets value per Shares as at 30 June 2009. Taking into account the fact that the Group made losses for the previous years, the parties to the Agreement consider that it is more appropriate to use the unaudited total tangible assets value per Share of the Company as at 30 June 2009 as the pricing benchmark for the issue price of the Consideration Shares and Conversion Shares.

Based on the above, the Board considers the issue price of the Consideration Shares and Conversion Shares is fair and reasonable and in the interests of the Shareholders. Given the aforesaid massive premium of the issue price of the Consideration Shares and Conversion Shares over the unaudited total tangible assets value per Share as at 30 June 2009 and from the arm's length commercial negotiations between the parties to the Agreement, the Board considers a discount of around 32% represented by the issue price of the Consideration Shares and Conversion Shares to the closing price of the Shares immediately before the date of the Agreement are fair and reasonable and in the interest of the Shareholders.

The Directors (including the independent non-executive Directors) are of the view that the terms of the Agreement are fair and reasonable and in the interests of the Company and its Shareholders as a whole. The Company has no intention currently to dispose of its existing business resulting from the Acquisition.

None of the Directors has previous managerial experience in operating a power plants. Nevertheless, as Zhongkai Group, the founding shareholder of the Project Company, will remain as a minority shareholder of the Project Company, it will provide assistance in the operation of the Project Company. In addition, the existing directors of the Project Company and members of the senior management with experiences in the operation of the power plant business will remain in their respective positions in the Project Company. Therefore, the Directors are of the view that there will be no problem in the continuing operation of the Project Company upon Completion.

LETTER FROM THE BOARD

K. FINANCIAL EFFECT OF THE ACQUISITION

Based on the unaudited pro forma financial information of the Enlarged Group as set out in Appendix V to this circular, the audited total assets of the Group as at 31 December 2009 were approximately HK\$669,574,000 and the unaudited pro forma total assets of the Enlarged Group would amount to approximately HK\$1,303,120,000. The audited total liabilities of the Group as at 31 December 2009 were approximately HK\$41,838,000 and the unaudited pro forma total liabilities of the Enlarged Group would amount to approximately HK\$254,447,000. The audited net assets of the Group as at 31 December 2009 was approximately HK\$627,736,000 and the unaudited pro forma net assets of the Enlarged Group would increase to approximately HK\$1,048,673,000. Assuming the Acquisition took place on 1 January 2009, the Group's loss attributable to owners of the Company for the year ended 31 December 2009 of approximately HK\$432,187,000 would become to a loss of approximately HK\$408,849,000, deriving mainly from the profit of the Project Company of approximately HK\$31,438,000.

L. FINANCIAL AND TRADING PROSPECTS OF THE ENLARGED GROUP

Carpet trading business

As disclosed in the Company's 2009 annual report, turnover of the carpet trading operation decreased by 19.6%, or HK\$2.5 million, to HK\$10.3 million in 2009, which was attributable to the global economic downturn and intense market competition and incurred a loss of HK\$1.6 million in carpets trading business. Despite the decrease in the turnover, the Group will continue its carpet trading business. The Group will take more effort to source more orders from both new and existing customers to improve the results.

Exploration and mining business

Current operation

The titanium mine is located at Xiao Hong Shan in Inner Mongolia, the PRC. A technical report in respect of the titanium mine is set out in the circular of the Company dated 15 October 2007. The indicated mineral resources containing iron, vanadium and titanium in the titanium mine (the "**Mineral Resources**") of the titanium mine – first portion (an area of approximately 0.7 square kilometers and within the titanium mine) amounted to 16.2 million tones at 19.5% total iron (TFe), 3.86% titanium (TiO₂) and 0.03% vanadium (V₂O₅) respectively, which represented an estimate of proven exploitable reserves at the titanium mine. The technical report also concludes that with continued on-going exploration by diamond drilling, the potential for increasing resources and reserves in the proposed pit area and in the remaining portion of the titanium mine (i.e. the portion other than the titanium mine – First Portion) is considered to be good. At present, the exploration licence which confers the right to conduct exploration work for the Mineral Resources in the titanium mine has already been obtained and is held by Qinghai Forest Source Mining Industry Developing Company Limited (the "**Qinghai Subsidiary**").

The current and on-going operation of the Qinghai Subsidiary principally includes the exploration of the titanium mine including surveying and diamond drilling; chemical assaying of the samples obtained from the titanium mine; metallurgical testing of the samples obtained from the titanium mine; feasibility study for the development of the titanium mine; and preparatory work for the application of the mining licence. At present and as set out above, the Qinghai Subsidiary is the holder of the exploration licence which covers the titanium mine. The exploration licence confers the Qinghai Subsidiary the rights to, among other things, (1) carry out exploration (such as diamond drilling) of the Mineral Resources of the titanium mine; (2) facilitate the construction of wiring at the titanium mine and neighboring areas for communication purpose and facilitate the supply of water and

LETTER FROM THE BOARD

electricity to the titanium mine; (3) access to the titanium mine and neighboring areas; (4) use the land on a temporary basis in accordance with the exploration work being carried out at the titanium mine; (5) be entitled to priority in exploring new type(s) of mineral resources (if any) discovered at the titanium mine; and (6) be entitled to priority in obtaining the mining right at the titanium mine. Whilst the exploration licence confers such rights to the Qinghai Subsidiary, under the relevant PRC laws, the ownership as to the titanium mine still vests with the PRC government but not the Qinghai Subsidiary, but this would not affect the rights of exploration as conferred to the Qinghai Subsidiary under the exploration licence.

Since the completion of the very substantial acquisition in relation to the titanium mine in November 2007, the Group has conducted various amount of work for the development of its exploration and mining business. Such work included: renewing the exploration licence in March 2009; conducting further chemical tests on the Mineral Resources of the titanium mine; conducting feasibility study on mine processing; preparing for the environmental study; applying for and obtaining the approval for the supply of water and building a communication tower. In addition, the Company has also been preparing for the application of the mining licence. For such preparation, the Company has liaised with various universities and companies in the PRC to prepare, revise and finalise testing reports in respect of the quantity and grade of the Mineral Resources of the titanium mine. Upon completion of the testing reports, the Group submitted an application for the registration of the Mineral Resources to the Ministry of Land and Resources of the PRC in mid 2009. The application was approved and the official approval document regarding the actual quantity of Mineral Resources was issued on 4 August 2009. This marks the completion of stage 1 of the mining licence application process. Stage 2 of the application process involves the preparation and completion of a feasibility report and an integrated utilisation plan for the Mineral Resources and the application for the approval of a delineation of the mining zone. Upon receipt of the approval of the delineation of the mining plan from the Mineral Resources to the Ministry of Land and Resources of the PRC, stage 3 (the final stage) will begin which will involve application to the Mineral Resources to the Ministry of Land and Resources of the PRC for the mining licence.

Application for mining license

As disclosed in the Company's 2009 annual report, the Group is still in the process of preparing for the application for the mining license of the Mineral Resources of the titanium mine. The Group is currently preparing the feasibility report and the integrated utilisation plan, and the application for the approval of the delineation of the mining zone. Upon receipt of the approval of the delineation of the mining plan, and subject to review of the status reports and other relevant information on the titanium mine to be provided by the Qinghai Subsidiary with reference to the expected amount of return on investment and economic benefit of the project, the Company will consider whether the application of the mining licence of the Mineral Resources will be made. It is expected that certain amount of work will still need to be completed before the mining licence will be issued.

Due to the global financial turmoil which has limited the possibility for the Company to raise additional funding to meet the future capital requirements for the mining project and the possible deregistration of Inner Mongolia Forest Source Mining Industry Developing Company Limited (the "**Inner Mongolia Subsidiary**"), the Group has intended to slow down the mining licence application until (1) further funding can be secured; (2) the change of the local management of both the Qinghai Subsidiary and the Inner Mongolia Subsidiary is completed; (3) the establishment of a new subsidiary in the PRC for applying for the mining licence is completed in the event that the Inner Mongolia Subsidiary is deregistered; and (4) the preparation for the application of the mining licence is completed.

LETTER FROM THE BOARD

Regarding the possible deregistration of the Inner Mongolia Subsidiary, as far as the Company is given to understand, this subsidiary of the Company will be deregistered when it fails to pay up the registered capital within the prescribed time. The Inner Mongolia Subsidiary was incorporated on 14 November 2007 for the purpose of applying for the mining licence of the titanium mine on behalf of the Qinghai Subsidiary. The Inner Mongolia Subsidiary has not commenced business since its incorporation and does not hold or own any asset. The exploration licence of the titanium mine is held by the Qinghai Subsidiary. To the best of the Directors' knowledge, information and belief having made all reasonable enquiries, the deregistration of the Inner Mongolia Subsidiary will not have any impact on the exploration licence. The Inner Mongolia Subsidiary was established by the Company to apply for the mining licence of the titanium mine, the process of which is still on-going and yet to be completed. The Company, however, can establish another wholly-foreign owned enterprise to apply for the mining licence if it deems necessary.

Future development

As described above, the Group is currently preparing the feasibility report and the integrated utilisation plan, and the application for the approval of the delineation of the mining zone. The Board, however, for the main reasons below, have decided to slow down the development of the Group's exploration and mining business:

- (i) The respective members of the board of directors and legal representatives of the Qinghai Subsidiary and the Inner Mongolia Subsidiary have yet to be officially changed, although the directors and legal representatives were removed on 10 September 2009. To the best of the Directors' knowledge, information and belief having made all reasonable enquiries, the procedure for changing and updating the official record of directors and legal representatives of the two PRC subsidiaries at the relevant PRC authorities (工商局) is taking longer than expected because the previous legal representatives of the Qinghai Subsidiary and the Inner Mongolia Subsidiary was not cooperative and failed to provide the requested documents and corporate seals. In this respect, the Company has already engaged a firm of PRC lawyers to attend to this matter on behalf of the Group to speed up the changing and updating of the official records. As advised by the Company's PRC legal advisers, pursuant to the relevant PRC laws and regulations, the previous legal representatives of the Qinghai Subsidiary and the Inner Mongolia Subsidiary is required to return the corporate seals of the two subsidiaries to the Company. The Directors believed that the Company would be able to obtain possession of the corporate seals in due course. The PRC legal advisers have also advised that under the relevant PRC rules and regulations, shareholders of a limited liability company in the PRC as a whole has the highest level of authority over the company and has the right to decide on the major issues of the company; while the board of directors is only responsible for executing the decisions made by the shareholders. In the circumstances, although the official records of directors and legal representatives have not been changed and updated, Hong Kong Forest Source Mining Industry Holding Company Limited (an indirect wholly owned subsidiary of the Company), being the only shareholder of the Qinghai Subsidiary, has maintained the control of the Qinghai Subsidiary and has also the right and power to remove and appoint directors to its board of directors. Based on the above advice, the Directors are of the view that the Company has maintained control on the Qinghai Subsidiary and the Inner Mongolia Subsidiary.

LETTER FROM THE BOARD

- (ii) The prices for metals such as iron, vanadium and titanium have been decreasing over the past two years. The purpose of the acquisition in relation to the titanium mine in 2007 was to explore the Group's opportunities to derive income from the sales of the Mineral Resources to be extracted from the titanium mine and thereby broadening the Group's source of income. However, due to the downturn of the global economy caused by the financial crisis, on one hand the prices for metals have decreased, on the other hand the costs for the exploration and mining of Mineral Resources have increased. The Board believed that such changes in the global environment could adversely affect the economic benefit which the exploration and mining business could bring to the Group.

To the best of the Directors' knowledge, information and belief having made all reasonable enquiries, the estimated funding required for the mining licence application is approximately HK\$458 million, of which approximately HK\$282 million will be for the mineral resources tax/fee in PRC, approximately HK\$51 million will be for the foundation cost, approximately HK\$57 million will be for the completion of the feasibility study and design fee, and HK\$45 million will be used as secured money proof for the application of mining licence. As at the Latest Practicable Date, the Company had no funding-raising plan for the titanium mine.

Petroleum resources development and production business

In addition to the Acquisition, on 25 September 2009, the Company entered in a conditional share purchase agreement in relation to the Petroleum Development Acquisition. The consideration for the Petroleum Development Acquisition is HK\$1,500 million which will be settled as to HK\$150 million by cash, as to HK\$50 million by the purchaser's (a wholly-owned subsidiary of the Company) issue and delivery of promissory notes, as to HK\$246,240,000 by the Company's allotment and issue of consideration shares and as to HK\$1,053,760,000 by the Company's creation and issue of convertible notes. Completion of the Petroleum Development Acquisition is conditional, among other things, the approval of the Shareholders at an extraordinary general meeting.

The Company has taken initiative in identifying investment opportunities that will broaden its revenue sources. The Petroleum Development Acquisition represents a good opportunity for the Company to diversify its business into the petroleum businesses in cooperation with China National Petroleum Corporation, a state-owned petroleum enterprise in the PRC. With the anticipated continued growth of the PRC economy which will fuel the demand for oil as basis of the acquisition cost, the Board believes that the oil business under the proposed acquisition is beneficial to the Group's profile.

Generating and supplying electricity and heat business

On 5 November 2009, the Company and the Purchaser entered into the Agreement to acquire 60% of the Project Company which is engaged in the business of generating and supplying electricity and heat by using coke oven gas in the PRC for a total consideration of HK\$350,860,000, of which HK\$70,000,000 will be settled by cash, HK\$140,430,000 will be settled by the Company's allotment and issue of the Consideration Shares and HK\$140,430,000 will be settled by the Company's creation and issue of the Convertible Notes. Apart from the payment of the total consideration of HK\$350,860,000, after completion, the Company will, through its subsidiary, assume the obligation to contribute to and pay up the remaining balance of the registered capital of the project company in the sum of approximately RMB69,550,000 (equivalent to approximately HK\$79,942,529).

LETTER FROM THE BOARD

The Company intends to expand its existing business to generating and supplying electricity and heat by using coke oven gas in the PRC, which, the Directors believed has ample growth opportunities due to the increased demand for electricity caused by the continued growth of the PRC economy. The use of coke oven gas to create electricity and heat can not only help to reduce this hazardous gas, but it also benefits the environment. In addition, coke oven gas is of lower cost when compared with other fuel such as natural gas or heavy oil. The Board considered that the acquisition represents an opportunity for the Group to enter into the power generation industry, and believed that the Group could broaden its source of income by vertically diversifying into such industry.

Previous fund raising activities

The Company raised approximately HK\$192 million through the placing of 809,280,000 new Shares (the “**Placement**”) pursuant to the placing agreement dated 6 August 2009 (as amended by the supplemental agreement dated 10 August 2009) entered into by the Company, details of which are disclosed in the announcements of the Company dated 7 August 2009 and 10 August 2009 and approximately HK\$108 million from the open offer of 2,452,500,000 offer shares of HK\$0.01 each at the subscription price of HK\$0.08 per offer share (the “**Open Offer**”), details of which are disclosed in the announcement of the Company dated 26 August 2009 and prospectus of the Company dated 16 September 2009.

As disclosed in the Company’s 2009 annual report, the year of 2010 will still be a year with great challenges. However, the Board believes that whenever there is a crisis, there is an opportunity. In the future, the Group will strive to combat the adverse impact arising from the financial crisis, and will adjust its business strategies to meet the changes of economic environment. It will also seek to capture any favorable opportunities for prudent investment in order to ensure a continuous, stable and healthy growth, and generate greater value for the Shareholders.

LETTER FROM THE BOARD

Company's plan pursuant to various recent acquisitions

The details of the various recent acquisitions of the Company are as follows:

	The exploration and mining business acquisition (the "Xiao Hong Shan Project")	The Petroleum Development Acquisition	The Acquisition
Management and expertise	The titanium mine was first acquired in 2007. Since then, the existing management of the Group has acquired the relevant experience in the Xiao Hong Shan Project. It is the Company's intention that as soon as the mining licence is obtained, additional staff with mining experience and expertise will be recruited to join the management team of this project. Although the existing members of the Board do not have experience in the exploration and mining business, the Board will gather a professional management team with relevant experience. On the other hand, the existing Board has much experience in operating PRC companies and managing business in the PRC. The Board is of the view that the Directors can assist to oversee and manage the businesses of the recent acquisitions.	Four Directors, namely Mr. Chan Kwok Wing, Mr. Zhao Guoqiang, Mr. Wang Donghai and Mr. Zhang Zhenming, have relevant experiences in oil and gas related projects in the PRC. In addition, to the best of the Directors' knowledge, information and belief having made all reasonable enquiries, the management team of the project company of the Petroleum Development Acquisition comprised of very experienced managers and technical advisers with local and first-hand experience in oil industry and in project area; and they will remain in their posts after the completion of the Petroleum Development Acquisition.	It is the Company's current intention to retain the senior management of the Project Company. None of the Directors has previous managerial experience in operating power plants. Nevertheless, as Zhongkai Group, the founding shareholder of the Project Company, will remain as a minority shareholder of the Project Company, it will provide assistance in the operation of the Project Company. In addition, to the best of the Directors' knowledge, the existing directors of the Project Company and members of the senior management with experiences in the operation of the power plant business will remain in their respective positions in the Project Company.
Allocation of time and resources	The mining licence of the titanium mine is yet to be obtained by the Group. It is, however, the intention of the management to allocate more of its time and resources to the Xian Hong Shan Project as soon as the mining licence is obtained.	It is the Company's current intention to designate four Directors (who have the relevant experiences in oil and gas related projects in the PRC) to be responsible for the overall development and management of the petroleum resources development and production business.	It is the Company's current intention to designate one to two Directors (or senior management) to be mainly responsible for the overall development, strategic planning and management of the Project Company.

LETTER FROM THE BOARD

	The exploration and mining business acquisition (the “Xiao Hong Shan Project”)	The Petroleum Development Acquisition	The Acquisition
Existing commitments	Consideration in an aggregate amount of HK\$780.78 million will be satisfied by the Company’s issue of convertible notes after the receipt of a mining licence of the titanium mine.	Consideration of HK\$1,500 million will be satisfied in the following manner: – as to HK\$150 million in cash (paid); – as to HK\$50 million by the Company’s issue of promissory note(s); – as to HK\$246,240,000 by the Company’s issue of consideration shares; – as to HK\$1,053,760,000 by the Company’s issue of convertible bonds	Consideration of HK\$350.86 million will be satisfied in the following manner – as to HK\$70 million in cash (HK\$35 million of which has already paid); – as to HK\$140.43 million by the Company’s issue of Consideration Shares; – as to HK\$140.43 million by the Company’s issue of Convertible Notes
Expected capital expenditure	As disclosed by the Company previously, subject to the review of the status reports and other relevant information on the titanium mine to be provided by Qinghai Forest Source Mining Industry Developing Company Limited with reference to the expected amount of return on investment and economic benefit of the project, the Company will consider whether an application for the mining license of the mineral resources in the titanium mine should be made. Upon receipt of the said information on the titanium mine, the Company will reassess the expected amount of capital commitment, the expected time for such commitment, their relevant uses and the plan of the relevant source of funding.	The term of the cooperation contract (the “ Cooperation Contract ”) dated 13 August 2007 between China National Petroleum Corporation and the project company consists of three phases, namely the evaluation period, the development period and the production period. According to the vendor and to the best knowledge and information of the Directors, as at the Latest Practicable Date, the said cooperation contract was at the development period. In addition, according to the vendor, the major source of capital expenditure and/or commitment is the cost of drilling wells. Since it is planned to further drill a numbers of traditional wells in the contract area during the development period, to the best of the Directors’ knowledge, information and belief having made all reasonable enquiries, the estimated capital expenditure for each of the first, the second, the third and the fourth year of the development period is approximately HK\$70 million, HK\$115 million, HK\$115 million and HK\$130 million respectively.	Please refer to the paragraph headed “B. The Agreement Dated 5 November 2009 - Further commitment of the Group” above.

LETTER FROM THE BOARD

	The exploration and mining business acquisition (the “Xiao Hong Shan Project”)	The Petroleum Development Acquisition	The Acquisition
Source of funding	Please see above. In addition, the Company intends to finance the Xian Hong Shan Project by the Company’s internal resources, bank borrowings, and if considered appropriate, proceeds from any future fund raising activity of the Company if the business requires additional funding.	Part of the amount of capital commitment will be paid from the proceeds of a placement which was completed in August 2009 and raised approximately HK\$108 million, and from the proceeds of an open offer which was completed on 5 October 2009 and raised approximately HK\$192 million. The remaining consideration will be satisfied by the Company’s issue of promissory note(s), consideration shares and convertible bonds. In addition, the Company intends to finance the petroleum resources development and production business by the Company’s internal resources, bank borrowings, and if considered appropriate, proceeds from any future fund raising activity of the Company if the business requires additional funding.	The registered capital of approximately HK\$79,942,529 will be paid from the proceeds of a placement which was completed in August 2009 and raised approximately HK\$108 million, and from the proceeds of an open offer which was completed on 5 October 2009 and raised approximately HK\$192 million. In addition, the Company intends to finance the generating and supplying electricity and heat business by the Company’s internal resources, bank borrowings, and if considered appropriate, proceeds from any future fund raising activity of the Company if the business requires additional funding.
Company’s strategic plan on each project	Upon review of the status reports and other relevant information on the titanium mine to be received by the Company with reference to the expected amount of return on investment and economic benefit of the Xiao Hong Shan Project, the Company will consider whether the application for the mining licence should be made. In the meantime, it is the Company’s current intention to put more focus and resources on the Acquisition and the Petroleum Development Acquisition, both of which are in their respective operation stages and are expected to generate cash inflow to the Group in a near future.	The objective of the Cooperation Contract is to develop the petroleum discovery with proved commercial value within the relevant contract area and to produce the petroleum to arrive at the cooperative targets expected by China National Petroleum Corporation and the project company. To the best of the Directors’ knowledge, it is the intention of the project company to adopt flexible production schedule in order to maximize the revenue and provide the highest return possible; and the project company will increase its production when the oil price is on its upward swing and slow down production when oil price is not favourable. Accordingly to the vendor, the production period under the Cooperation Contract will commence immediately after 40,000 metric tones of crude oil is produced from the target oilfield, and the production period will continue for 20 years.	After Completion (if applicable), the Company will own 60% of the Project Company. It is the Company’s intention to expand the business of the Project Company and to continue the expansion of the power plant and to increase its capacity to generate electricity and heat. For further information, please also refer to the paragraph headed “H. Business Model” above.
Short term and long term challenges and risks to the Company for each project	The Group is unable to obtain the mining licence	Insufficient working capital to finance the continue development of the petroleum resources development and production business.	Insufficient working capital to finance the continue development of the generating and supplying electricity and heat business.

LETTER FROM THE BOARD

M. REGULATORY ENVIRONMENT

The business of the Project Company is subject to extensive regulations by the PRC government. These regulations govern a wide range of areas including, among others, project approvals, power generation, transmission and dispatch, on-grid tariffs and environmental protection and safety.

Relevant supervising authorities

NDRC and its provincial branch are responsible for the following:

- setting and implementing major policies concerning the PRC’s economic and social development;
- promulgating regulations and rules in connection with the operation of power plants;
- setting power tariffs; and
- accepting and approving the Clean Development Mechanism, an arrangement under the Kyoto Protocol allowing industrialized countries to invest in projects that reduce greenhouse gas emissions in developing countries in order to earn emission credits

As a combined heat and electricity generation plant, the Project Company obtained the approval for running its business from Provincial Economy Committee of Shanxi Province (山西省經濟委員會) (“**Shanxi EC**”).

The State Electricity Regulatory Commission of the PRC (國家電力監管委員會) and its local branches are mainly responsible for (i) promulgating rules for the power industry; (ii) supervising the operations and legal compliance of the power industry; (iii) issuing and administering electric power business permits; and (iv) supervising the power market.

Whereas the national and provincial level of Ministry of Housing and Urban-Rural Development of the PRC (“MOHURD”) under the State Council is responsible for reviewing the policy on heat supply system in the PRC, the MOHURD of each prefecture-level city are responsible for establishing and maintaining the centralized heat supply station in each prefecture-level city and county and to liaison with heat supplier or generator. City’s Construction and Development Bureau of Lingshi County (靈石縣城市建設局), which is supervised by the local people’s government of Lingshi County, is responsible for making strategic plan for heat supplying network in Lingshi County and to supervise the operation of Central Heat Station, whereas Lingshi Central Heat Station is a separate legal entity responsible for daily operation of the heat transmit system and liaison with heat generator and heat customer including entering into heat supply/transmission contract with them.

LETTER FROM THE BOARD

The Ministry of Environmental Protection of the PRC (中國環境保護部) (“**MEP**”), which was formed pursuant to a resolution passed by the eleventh National People’s Congress in March 2008, is responsible for the supervision and control of environmental protection and monitoring of the PRC’s environmental system at the national level.

The State Administration of Work Safety (國家安全生產監督管理總局) (“**SAWS**”) is responsible for supervising work safety of power generation operations and project construction, and implementing various safety regulations.

Finally, the State Administration of Taxation of the PRC (國家稅務總局) (“**SAT**”) is responsible for promulgating and implementing tax policies and regulations.

Applicable regulatory scheme on the operation of the Project Company

Permit

As a combined heat and electricity generation plant, rules for obtaining an electric power permit under the State Electricity Regulatory Commission’s Provision on the Administration of the Electric Power Business Permit is not applicable to the Project Company. The permit for the operation of a combined heat and electricity generation plant by the Project Company was issued by the Shanxi EC upon the application made by the Project Company. The Shanxi EC, upon the said approval, informed other relevant supervising authorities, including (but not limited to) provincial and local MEP, SAWS, SAT and State Grid as to the issuance of the permit for running a heat-electricity joint generation plant and to instruct these authorities to enter into appropriate agreements with the Project Company in relation to the operation of combined heat and electricity generation businesses, which include electricity dispatch agreement.

Electric Power Law

The regulatory framework of the PRC power industry is set out in the Electric Power Law of the PRC (“**Electric Power Law**” 《中華人民共和國電力法》) and the Electric Power Regulatory Ordinance (《電力監管條例》), which became effective on 1 April 1996 and 1 May 2005 respectively. One of the stated purposes of the Electric Power Law is to protect the legitimate interests of investors, operators and users and to ensure the safety of power operations. The Electric Power Law also states that the PRC government encourages and regulates PRC and foreign investment in the power industry. The Electric Power Regulatory Ordinance sets forth regulatory requirements for many aspects of the power industry, including, among others, the regulatory inspections of power generators and grid companies and the legal liabilities from violations of the regulatory requirements.

LETTER FROM THE BOARD

Dispatch

All electric power generated in the PRC is dispatched through power grids, except for electric power generated by facilities not connected to a grid. Dispatch of power to each grid is administered by dispatch centers. Dispatch centers are responsible for the administration and dispatch of planned output of power plants connected to the grid. The Regulations on the Administration of Electric Power Dispatch to Networks and Grids (《電網調度管理條例》) issued by the State Council, effective on 1 November 1993, regulates the operation of dispatch centers.

On-grid tariffs and electricity prices

An on-grid tariff is the tariff that grid companies pay to the Project Company as the generating company. The PRC Electric Power Law, which came into effect in 1996, sets out the general principles for determining on-grid tariffs in the PRC. Under the PRC Electric Power Law, the on-grid tariffs granted to a power producer are formulated to provide reasonable compensation for costs as well as a reasonable return on investment. Different on-grid tariffs are applicable to planned output, excess output and output subject to competitive bidding. In general, the on-grid tariffs for planned output and excess output are subject to a review and approval processes involving the relevant provincial price bureaus and the NDRC. Each year, the relevant provincial government agency forecasts the electricity demand in the region based on the projected economic growth to determine total electricity output. Pursuant to such estimates, each power plant and the power purchaser reach an agreement on the amount of planned output and excess output. Additional output is subject to the competitive bidding of on-grid tariffs.

LETTER FROM THE BOARD

On 28 March 2005, the NDRC issued the Provisional Measures for the Administration of On-grid Tariff (《上網電價管理暫行辦法》), which provides regulatory guidance for the Power Tariff Reform Plan (《電價改革方案》) issued in July 2003. For power plants within the regional grids that have not implemented competitive bidding tariff-setting mechanisms, on-grid tariffs will be set and announced by relevant pricing bureaus based on production costs plus a reasonable investment return. For power plants within the regional grids that have implemented competitive bidding tariff-setting mechanisms, on-grid tariffs are two folds: (i) a capacity tariff determined by the NDRC based on the average investment cost of the power generators competing within the same regional grid and (ii) a competitive tariff determined through the competitive bidding process. This NDRC regulation became effective from 1 May 2005.

In order to reduce environmental pollution, the NDRC has also provided incentives for IPPs to install desulphurization equipment. In June 2006, the NDRC announced an on-grid tariff premium of RMB15 per MWh for all plants which had installed and operated flue gas desulfurization equipment and had acquired the final acceptance from relevant authorities before the end of 2006. To accelerate the development of desulphurizing facilities and reduce the emission of carbon dioxide in the PRC, the Provisional Measures on the Administration of Price of the Desulphurized Coal Power and Operation of the Desulphurizing Facilities (《燃煤發電機組脫硫電價及脫硫設施運行管理辦法(試行)》) was jointly issued by the NDRC and the Ministry of Environmental Protection of the PRC (previously known as State Environmental Protection Administration (中華人民共和國環境保護部)). and became effective on 1 July 2007. Regarding the on-grid tariffs, these measures include, among others, the following:

- a tariff surcharge of RMB0.015 per kWh was added to the selling price of electricity generated from desulphurized coal power generators; and
- power plants using coal with average sulphureous content above 2% or below 0.5%, the tariff surcharge for the installation of desulphurizing facilities of which may be set by the local government and subject to a review and approval process involving the provincial pricing bureaus and the NDRC.

On 2 July 2008, the NDRC announced the details of an on-grid tariff increase by the provincial authorities. The national average on-grid tariff hike was RMB17 to 18 per MWh. On 19 August 2008, the NDRC announced a further overall increase in on-grid tariff of RMB10 to 25 per MWh, averaging RMB20 per MWh (including 17% VAT), without adjusting the retail tariffs.

LETTER FROM THE BOARD

In November 2009, the NDRC announced plans to adjust tariff for coal power. Effective from 20 November 2009, the average national retail tariff payable by non-residential users will increase by RMB28 per MWh, but the adjustments for each individual region and industry will vary. According to the announcement made available on the NDRC's website, the retail tariff increase is intended to alleviate profitability margin pressure on grid companies which resulted when the national average on-grid tariff was increased in 2008 by an average of RMB20 per MWh, while the retail tariff was not correspondingly adjusted.

In addition to the tariffs, NDRC also set the price levels of electricity, which is subsequently announced and implemented by provincial bureau of price level (物價局). Pursuant to the change of set prices of electricity as announced by NDRC in 2006, 2008 and 2009 respectively, the provincial bureau of price level of Shanxi Province also modified the prices for electricity in 2006, 2008 and 2009. The following table shows the set prices for electricity as announced:

Unit: RMB dollar per unit of electricity (kWh)

	Price in 2006	Price in 2008	Price in 2009
Residential user (less than 1 kW)	0.467	0.477	0.467
Residential user (1 kW to 10 kW)	0.457	0.467	0.457
Residential user (20 kW)	N/A	N/A	0.457
Commercial user (less than 1 kW)	0.760	0.675	0.7117
Commercial user (1kW to 10 kW)	0.750	0.660	0.6917
Commercial user (20kW)	N/A	N/A	0.6857
Commercial user (35 kW to 110 kW)	0.750	0.650	0.6767
Industrial user (1 kW to 10kW)	0.379	0.431	0.4521
Industrial user (20kW)	N/A	N/A	0.4441
Industrial user (35 kW to 110kW)	0.364	0.416	0.4321
Industrial user (110 kW to 220kW)	0.354	0.406	0.4221
Industrial user (over 220kW)	0.349	0.401	0.4171
Agricultural user (less than 1 kW)	0.357	0.382	0.4231
Agricultural user (1kW to 10 kW)	0.347	0.372	0.4081
Agricultural user (20kW)	N/A	N/A	0.4021
Agricultural user (35kW to 100kW)	0.337	0.362	0.3931

Note: for industrial users, they are required to pay for surcharge fee in accordance to the usage of pressure transformer. The surcharge fee was 22.00 per kilovolt-ampere per month in 2006 and 25.00 per kilovolt-ampere per month for both 2008 and 2009.

LETTER FROM THE BOARD

Incentives

According to the Administrative Measures on the Recognition of Comprehensive Resource Utilisation Encouraged by the State (《國家鼓勵的資源綜合利用認定管理辦法》), if a coal power plant uses no less than 60% coal sludge as fuel and blends this coal fuel with coke, it may be recognized by the PRC government as a Resource Comprehensive Utilisation Plant, which would entitle it to a reduction of 50% of the value-added Tax levied on electricity generation according to applicable PRC tax laws.

According to the Interim Provisions on the Administration of the Construction of Power Generation Projects of Steam-Electricity Cogeneration and Comprehensive Utilisation of Coal Sludge (《熱電聯產和煤矸石綜合利用發電項目建設管理暫行規定》), if a coal power plant provides steam simultaneously during the power generation process, the power generation units may be recognised as cogeneration units by the PRC government, which entitles it to sell steam to the customers within the heat zone of the coal plant (generally within an eight-kilometer radius) on an exclusive basis and enjoy higher dispatch priority under some conditions.

Regulations on heat supply

Rules on Centralised heat supply for Jinzhong

According to the Notice of drafting plan for centralisation of heat supply in prefecture-level city of Shanxi Province (山西省城市集中供熱專項規劃編制綱要試行通知) issued by the Shanxi Provincial government in May 2009, local Construction and Development Bureau of each prefecture-level city are required to draft a plan for centralising heat supply by the end of 2009 with prescribed contents, which shall be later reviewed and reported to the People's Government of Shanxi Province in 2010.

In July 2009, the City's Construction and Development Bureau of Jinzhong City issued the proposal for managing centralised heat supply in Jinzhong City (晉中市城區集中供熱管理辦法(試行)) (**"Heat Supply Proposal"**), stipulating the fundamental principles and regulations for operating heat supply in all counties in Jinzhong City, including Lingshi County.

Under the Heat Supply Proposal, the guiding principles for centralising heat supply include enhancing the safety and reliability of heat supply network and to accommodate the needs of the prefecture-level city and county. The heat supplying period usually begins on the 1st day of November each year and ends on the 31st day of March in the next year, which is subject to the extension as the City's Construction and Development Bureau or local government thinks fit. Further, the City's Construction and Development Bureau shall enter into heat supply agreement with the heat user and stipulates the term, price and area of heat supply whereas the corresponding heat supply station shall enter into heat supply agreement with heat generator (if applicable). For those intended heat customers who still have no infrastructure for heat transmission, the City's Construction and Development Bureau shall arrange the construction of heat transmission network infrastructure in order to centralise heat supply. It is prohibited for the heat user to re-arrange the heat supply network without the approval of City's Construction and Development Bureau or local government.

LETTER FROM THE BOARD

Environmental Protection Law

The main PRC environmental laws and regulations applicable to construction and operation of the Project Company include the Environmental Protection Law of the PRC (《中華人民共和國環境保護法》), the PRC Law on the Prevention and Treatment of Water Pollution (《中華人民共和國水污染防治法》), the PRC Law on the Prevention and Treatment of Air Pollution (《中華人民共和國大氣污染防治法》), the PRC Law on Prevention and Treatment of Solid Waste Pollution (《中華人民共和國固體廢物污染環境防治法》) and the PRC Law on Appraising Environment Impacts (《中華人民共和國環境影響評價法》).

According to the Measures on the Administration of Environmental Protection of Electric Power Industry (《電力工業環境保護管理辦法》), which became effective on 2 December 1996, coal power construction projects are subject to the PRC's environmental impact assessment system. The power generators may choose its environmental assessor, subject to the confirmation of local administrative authorities in charge of environmental protection at the provincial level, and file an environmental impact assessment report with the local administrative authorities. In addition, power plants must assign a specific department and its personnel to discharge its obligations with regard to environmental protection. Power enterprises should also set aside funds for the prevention and treatment of environmental pollution caused by their own construction operation.

Safety Law and Labour Law

The Work Safety Law of the PRC (《中華人民共和國安全生產法》), which became effective on November 1, 2002, is the principal law governing the supervision and administration of work safety and labor protection. In accordance with the Measures on Supervision and Administration of the Work Safety of Electricity Industry (《電力安全生產監督管理辦法》), issued by the SERC in March 2004, the Project Company is responsible for maintaining their safety operations in accordance with requirements set by the regional grid in which they are located. The Project Company is required to report to the SERC, the SAWS and relevant local government authorities, within 24 hours, any safety accident that causes worker fatalities or is classified as a serious or extraordinary accident.

The main PRC employment laws and regulations applicable to the Project Company include the Labour Law of the PRC (《中華人民共和國勞動法》), the Employment Contract Law of the PRC (《中華人民共和國勞動合同法》) and the Implementing Regulations of the Employment Contract Law of the PRC (《中華人民共和國勞動合同法實施條例》). The Employment Contract Law of the PRC (《中華人民共和國勞動合同法》) was promulgated on 29 June, 2007 and became effective on 1 January, 2008. This law governs the establishment of employment relationships between employers and employees, and the execution, performance, termination of, and the amendment to, employment contracts. Compared to the PRC Labour Law, the new PRC Employment Contract Law provides additional protection to employees by requiring written labor employment contracts and long-term contractual employment relationships, limiting the scope of the circumstances under which employees could be required to pay penalties for breach of employment contracts and imposing stricter sanctions on employers who fail to pay remuneration or social security premiums for their employees.

LETTER FROM THE BOARD

Taxation Law

Heat and power generators in the PRC are subject to a variety of taxes and fees levied by the PRC central and local governments.

Enterprise Income Tax Law

On 16 March 2007, the PRC National People's Congress enacted the PRC Enterprise Income Tax Law (the "**EIT Law**"), which, together with its related implementation rules issued by the PRC State Council on 6 December 2007, became effective on 1 January 2008. The EIT Law imposes a single uniform income tax rate of 25% on all Chinese enterprises, including foreign invested enterprises, and eliminates or modifies most of the tax exemptions, reductions and preferential treatment available under the previous tax laws and regulations. On 26 December 2007, the PRC State Council issued a Notice on the Implementation of the Transitional Preferential Tax Policies (國務院關於實施企業所得稅過渡優惠政策的通知), or Circular 39. Pursuant to Circular 39, with the effectiveness of the EIT Law, the Project Company is entitled to apply the transitional rates of 18%, 20%, 22%, 24% and 25% for 2008, 2009, 2010, 2011 and 2012 onwards, respectively. Further, Circular 39 grandfathers the tax holidays already granted to those foreign invested production type enterprises scheduled to operate for a period not less than ten years and requires such holidays to commence on 1 January 2008 should they have not started earlier.

Under the EIT law, foreign invested enterprises engaged in energy transportation are also taxed at a preferential income tax rate of 15%. In addition, pursuant to the Notice on the Execution of the Catalogue of Public Infrastructure Projects Entitled for Preferential Tax Treatment (財政部、國家稅務總局關於執行公共基礎設施項目企業所得稅優惠目錄有關問題的通知), an enterprise set up after 1 January 2008 and engaged in public infrastructure projects is entitled to a tax holiday of a three-year full exemption followed by a three-year 50% exemption commencing from the first year it generates operating income.

In addition, pursuant to the EIT Law, starting from 1 January 2008, dividends and interest payable to foreign investors are subject to a 10% withholding tax (unless the foreign investor's jurisdiction of incorporation has a tax treaty with the PRC that provides for a different withholding arrangement, and the preferential tax rate is approved by the competent authorities).

Waiver on taxation in relation to heat generation business

As mentioned, under the Notice of continuance of favourable tax policies to heat generating business (財政部、國家稅務總局關於繼續執行供熱企業增值稅、房產稅、城鎮土地使用稅優惠政策的通知) issued by the Ministry of Finance and the State Administration of Taxation on 10 February 2009, it is provided that (i) in relation to the revenue generated by heat supplying companies to residents during November 2009 to March 2010, it shall be value-added tax free; (ii) from 1 January 2009 to 30 June 2011, the plants for heat generation to residents shall be exempted from property tax and use of city's land tax.

LETTER FROM THE BOARD

N. RISK FACTORS

Possible risk factors which may be faced by the Group in connection with the Acquisition are as follows:

New business segment of the Group

The Acquisition constitutes an investment in a new business sector for the Group. The new business, coupled with the regulatory environment, may pose significant challenges to the Company's administrative, financial and operational resources. Since the Company does not have significant experience in the new energy generation and supply business, it is not in a position to ascertain the timing and amount of any return or benefits that may be received from the new business. If the new energy generation and supply business does not develop and progress as planned, the Company may not recover the funds and resources it has spent, and this may affect the Company.

Although the existing members of the Board do not have experience in the energy generation and supply business, the Board will gather a professional management team with the relevant experience. On the other hand, the existing Board has much experience in operating PRC companies and managing business in the PRC. The Board is of the view that the Directors can assist to oversee and manage the new energy generation and supply business. Further, as the Project Company's founding shareholder (namely, Zhongkai Group) will remain as a shareholder of the Project Company, the directors with experiences in running the Project Company will be retained in the board of directors of the Project Company.

Regulatory control

The generating and supplying electricity and heat business intended to be undertaken by the Group are regulated by legislation and various regulatory authorities in the PRC. The Group will be required to obtain the relevant licences for the operation of such business in the PRC. In this respect, the Group has to ensure continuous compliance with all applicable laws, regulations and codes in the PRC to avoid any fines or any form of sanctions. Failure to comply with the relevant laws and regulations may adversely affect the Group's operation of the energy generation and supply business.

There are ongoing changes to the regulations governing the PRC power industry. If the PRC government applies more stringent and additional laws and regulations in the future, the Group may require additional investments, or may incur additional costs in order to comply with such laws and regulations, which may adversely affect the Group's operations and profitability.

The Company will seek and continuously consult its PRC legal advisers in these respects to ensure the minimization of the above risks.

Price control

As the prices of electricity and heat are strictly regulated by NDRC and the local authorities, the Project Company is vulnerable to unfavourable prices which may limit the Group's earning potential.

LETTER FROM THE BOARD

Change of policy

The Project Company was established pursuant to the national and provincial policy of encouraging the establishment of heat-electricity joint generation plant, and is currently receiving subsidy and tax benefits pursuant to this policy. Therefore, any change in such policy may affect the subsidy and tax benefits available to the Project Company.

Future increase in overall energy in the PRC may have material adverse impact on the Group's energy sales

Recently, there has been significant investment in new energy generation capacities and facilities alongside the increase in demand in the past few years. There is no assurance that in future the supply will not exceed the demand of energy in the PRC. In such event, demand for electricity from the Group's power plant may reduce, materially affecting the Group's energy sales. One of the purposes of the recent acquisitions of the Company is to allow the Company not to be dependent on only one line of business and to broaden its source of income. In the event that the supply of energy exceeds the demand of energy in the PRC, the Company may divert more of its resources to the other business and operations of the Group.

Recent global economic turmoil

The recent global credit crisis has led to deteriorating worldwide economic conditions, in particular, liquidity problems and the tightening of credit policies by financial institutions. With weakening global consumer demand, overall demand for electricity may also decline, which in turn will affect the operations of the Group's energy generation and supply business.

Operations of foreign owned enterprises in the PRC

The Group's operation of generating and supplying electricity and heat in the PRC may incur increasing regulatory risks which are inherent in the operations of foreign owned enterprises in the PRC, including:

- loss of business and revenue, property interest and equipment as a result of hazards such as expropriation, nationalization, civil disturbance and other political risks;
- the adverse effects of currency fluctuations and exchange controls, such as appreciation of RMB or devaluation of foreign currencies or other economic problems; and
- changes in law, regulations and policies on the operation of foreign owned enterprises of the PRC government irrespective of whether at the central, provincial or municipal levels.

Over reliance on local economy and small group of customers

As the only heat-electricity joint generation plant in Lingshi County, the Project Company's business relies on the economic growth and development in Lingshi County. Furthermore, the Project Company's electricity business is mostly relied on a very small group of industrial customers.

LETTER FROM THE BOARD

Sustainability of the business model

The term under the respective agreements for heat/electricity supply signed between the Project Company and its major customers are relatively short (i.e. term of 1 year) or with no specified term provided; and there is no guarantee that all of these customers will continue to engage the Project Company as its heat/electricity supplier for a longer period of time. If any one of these major customers declines to renew or otherwise terminate its contract of purchase with the Project Company, which is possible within a short period of time (i.e. less than one year from the Latest Practicable Date), the turnover of the Project Company may be adversely affected, which poses the problem of substitutability of the business model of the Project Company. Nevertheless, as the Project Company is the only private heat and electricity generator in the area of Lingshi County, and as the Project Company can offer a lower price for supplying electricity compared to State Grid, in the absence of competition and alternative choice of heat/electricity supplier, the risk for the Project Company's major customers to terminate its contract with the Project Company is low.

Insufficient working capital to finance the continue development of the Group's businesses

Apart from the Acquisition, recently, the Group has also made the Petroleum Development Acquisition. Completion of the Petroleum Development Acquisition is conditional, among other things, the approval of the Shareholders at an extraordinary general meeting to be held by the Company for approving such acquisition. Upon completion of these recent acquisitions, the Group's working capital requirement will increase. The Group will require additional working capital to finance the continue development of the new businesses. If the Group has insufficient working capital reserves to fund the incremental working capital requirements, the Group's growth and expansion may be restricted.

O. EGM

A notice convening the extraordinary general meeting of the Company to be held at Room 1102B, 11/F, Tower I, Admiralty Centre, 18 Harcourt Road, Hong Kong on 16 July 2010 at 4:00 p.m. is set out on pages 194 to 195 of this circular. Whether or not you are able to attend the meeting in person, please complete the accompanying form of proxy in accordance with the instructions printed thereon and return the same to the Company's share registrars, Tricor Tengis Limited at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong as soon as practicable but in any event not less than 48 hours before the time appointed for the holding of the meeting. Completion and return of the accompanying form of proxy will not preclude you from attending and voting at the meeting should you so wish.

To the best knowledge, information and belief of the Directors, having made all reasonable enquiry, each of the Vendor, their respective ultimate beneficial owners and associates did not hold any Shares as at the Latest Practicable Date and no other Shareholder has a material interest in the Acquisition. Therefore, no Shareholder is required to abstain from voting on the relevant resolution to be proposed at the EGM to approve the Agreement and the transactions contemplated thereunder.

LETTER FROM THE BOARD

P. RECOMMENDATIONS

Based on the reasons set out in the paragraph headed “J. Reasons for entering into the Agreement” above, the Board considers that the terms of the Acquisition are fair and reasonable so far as the Shareholders are concerned and the Acquisition is in the interests of the Company and the Shareholders as a whole. Accordingly, the Board recommends the Shareholders to vote in favour of the ordinary resolution to be put forward to the Shareholders at the EGM to consider and, if thought fit, approve the Agreement and the transactions contemplated thereunder.

Q. ADDITIONAL INFORMATION

Your attention is also drawn to the additional information contained in the appendices to this circular.

By order of the Board
Xian Yuen Titanium Resources Holdings Limited
Law Fei Shing
Chief Executive Officer and Executive Director

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

The following is the text of a report, prepared for the sole purpose of inclusion in this circular, from the independent reporting accountants, RSM Nelson Wheeler, Certified Public Accountants, Hong Kong.

RSM Nelson Wheeler
中瑞岳華 (香港) 會計師事務所
Certified Public Accountants

29th Floor,
Caroline Centre,
Lee Gardens Two,
28 Yun Ping Road,
Hong Kong

28 June 2010

The Board of Directors
Xian Yuen Titanium Resources Holdings Limited

Dear Sirs,

We set out below our report on the financial information (the “Financial Information”) of Sunlight Rise Limited and its subsidiaries (hereinafter collectively referred to as the “Target Group”) for the period from 20 October 2009 (date of incorporation) to 31 December 2009 (the “Relevant Period”) for inclusion in the circular dated 28 June 2010 issued by Xian Yuen Titanium Resources Holdings Limited (the “Company”) in connection with the proposed acquisition of the 100% equity interest in the Target Group (the “Circular”).

Sunlight Rise Limited was incorporated on 20 October 2009 in the British Virgin Islands with limited liability and engaged in investment holding in the Relevant Period. As at the date of this report, Sunlight Rise Limited has the following subsidiaries:

Name of subsidiary	Place and date of incorporation/ establishment	Issued and fully paid share/ registered capital	Attributable equity interest of the Target Group		Principal activity
			Direct	Indirect	
Pride Treasure Limited	Hong Kong 27 March 2009	HK\$10,000	100%	–	Investment holding
Ontop Finance Limited	Hong Kong 29 April 2009	HK\$1	–	100%	Investment holding
Shanxi Zhong Kai Lingshi Heat & Power Company Limited	People's Republic of China (the “PRC”) 31 December 2005	Registered capital of RMB115,000,000	–	60%	Generation and supplying of electricity and heat

No audited financial statements of Sunlight Rise Limited have been prepared for the Relevant Period as there is no statutory audit requirement in the country of their incorporation.

No audited financial statements of Pride Treasure Limited and Ontop Finance Limited have been prepared since its date of incorporation.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

The financial year end of Shanxi Zhong Kai Lingshi Heat & Power Company Limited is 31 December and the statutory audited financial statements of Shanxi Zhong Kai for the years ended 31 December 2007 and 2008 were prepared in accordance with accounting principles and regulations applicable in the PRC and audited by Shanxi Jinhe Certified Public Accountants (山西晉和會計師事務所). No audited financial statements have been prepared for the year ended 31 December 2009.

For the purpose of this report, the directors of Sunlight Rise Limited have prepared the consolidated financial statements of the Target Group for the Relevant Period in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA") (the "HKFRS Financial Statements").

Except for the limitation in the scope of our work as described in the basis for qualified opinion paragraph, we have performed our independent audit on the HKFRS Financial Statements in accordance with Hong Kong Standards on Auditing issued by the HKICPA and have examined the HKFRS Financial Statements in accordance with Auditing Guideline 3.340 "Prospectuses and the Reporting Accountant" issued by the HKICPA. The Financial Information has been prepared from the HKFRS Financial Statements in accordance with HKFRSs. No adjustments were considered necessary for the purpose of preparing our report for inclusion in the Circular.

The directors of Sunlight Rise Limited are responsible for the preparation of the HKFRS Financial Statements. The directors of the Company are responsible for the contents of the Circular in which this report is included. It is our responsibility to compile the Financial Information set out in this report from the HKFRS Financial Statements, to form an independent opinion on the Financial Information and to report our opinion to you.

BASIS FOR QUALIFIED OPINION

The financial statements of one of Sunlight Rise Limited's subsidiaries, Shanxi Zhong Kai Lingshi Heat & Power Company Limited, were not consolidated in the Financial Information of the Target Group. This is not in accordance with Hong Kong Accounting Standard 27 "Consolidated and Separate Financial Statements" ("HKAS 27") which requires all subsidiaries to be included in the consolidated financial statements of the parent. In addition, the information required under paragraph 18(4) of the tenth schedule to the Hong Kong Companies Ordinance in respect of this subsidiary has not been disclosed in the Financial Information. In our opinion, these constitute a departure from the HKAS 27 and the disclosure requirements of the Hong Kong Companies Ordinance. Because we have not been provided with sufficient financial information of this subsidiary for the consolidation, we are unable to quantify the effect of not consolidating this subsidiary on the Financial Information.

QUALIFIED OPINION ARISING FROM NON-COMPLIANCE WITH HKAS 27 AND THE DISCLOSURE REQUIREMENTS OF THE HONG KONG COMPANIES ORDINANCE

In our opinion, for the purpose of this report, except for the non-compliance with HKAS 27 and disclosure requirements of the Hong Kong Companies Ordinance as described above, the Financial Information gives a true and fair view of the state of affairs of Sunlight Rise Limited and of the Target Group as at 31 December 2009 and the result and cash flows of the Target Group for the Relevant Period.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

I. FINANCIAL INFORMATION

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	<i>Note</i>	Period from 20 October 2009 to 31 December 2009 <i>HK\$</i>
Turnover	<i>6</i>	–
Administrative expenses		(54,408)
Loss before tax		(54,408)
Income tax expense	<i>7</i>	–
Loss for the period	<i>8</i>	(54,408)
Other comprehensive income for the period		–
Total comprehensive income for the period		(54,408)

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	<i>Note</i>	As at 31 December 2009 HK\$
Non-current assets		
Investment in subsidiaries	<i>10</i>	35,000,000
Current assets		
Cash balance		6,231
Current liabilities		
Accruals and other payables		48,638
Due to a director	<i>11</i>	11,993
Due to ultimate parent	<i>11</i>	35,000,000
		35,060,631
Net current liabilities		(35,054,400)
NET LIABILITIES		(54,400)
Capital and reserves		
Share capital	<i>12</i>	8
Accumulated losses		(54,408)
TOTAL EQUITY		(54,400)

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

STATEMENT OF FINANCIAL POSITION

	<i>Note</i>	As at 31 December 2009 HK\$
Non current assets		
Investments in subsidiaries	<i>10</i>	10,000
Current assets		
Due from a subsidiary	<i>11</i>	35,000,000
Cash balance		1,000
		35,001,000
Current liabilities		
Accruals and other payables		16,618
Due to a director	<i>11</i>	10,992
Due to ultimate parent	<i>11</i>	35,000,000
		35,027,610
Net current liabilities		(26,610)
NET LIABILITIES		(16,610)
Capital and reserves		
Share capital	<i>12</i>	8
Accumulated losses	<i>13</i>	(16,618)
TOTAL EQUITY		(16,610)

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Share capital <i>HK\$</i>	Accumulated losses <i>HK\$</i>	Total <i>HK\$</i>
Issue of share	8	–	8
Total comprehensive income for the period	<u>–</u>	<u>(54,408)</u>	<u>(54,408)</u>
At 31 December 2009	<u><u>8</u></u>	<u><u>(54,408)</u></u>	<u><u>(54,400)</u></u>

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

CONSOLIDATED STATEMENT OF CASH FLOWS

	Period from 20 October 2009 to 31 December 2009 HK\$
CASH FLOWS FROM OPERATING ACTIVITIES	
Operating loss before working capital changes	(54,408)
Increase in accruals and other payables	<u>48,638</u>
Net cash used in operating activities	<u>(5,770)</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from issue of share	8
Capital injected to a subsidiary	<u>(35,000,000)</u>
Net cash used in investing activities	<u>(34,999,992)</u>
CASH FLOWS FROM FINANCING ACTIVITIES	
Advanced from a director	11,993
Advanced from ultimate parent	<u>35,000,000</u>
Net cash generated form financing activities	<u>35,011,993</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS AND AT THE END OF PERIOD	<u>6,231</u>
ANALYSIS OF CASH AND CASH EQUIVALENTS	
Cash balance	<u><u>6,231</u></u>

II. NOTES TO THE FINANCIAL INFORMATION**1. General Information**

Sunlight Rise Limited was incorporated in the British Virgin Islands with limited liability. The address of its registered office is P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands.

Sunlight Rise Limited is engaged in investment holding during the Relevant Period. The principal activities of its subsidiaries are set out in note 10 to the Financial Information.

In the opinion of the directors of Sunlight Rise Limited, as at 31 December 2009, Maycrown Capital Limited, a company incorporated in the British Virgin Islands, is the ultimate parent and Miss Ho Mee Kuen Karen is the ultimate controlling party of Sunlight Rise Limited.

2. Adoption of new and revised Hong Kong Financial Reporting Standards

During the Relevant Period, the Target Group has adopted all the new and revised HKFRSs that are relevant to its operations and effective for its accounting period beginning on 20 October 2009. HKFRSs comprise Hong Kong Financial Reporting Standards; Hong Kong Accounting Standards; and Interpretations.

The Target Group has not applied the new HKFRSs that have been issued but are not yet effective. The Target Group has already commenced an assessment of the impact of these new HKFRSs but is not yet in a position to state whether these new HKFRSs would have a material impact on its results of operation and financial position.

3. Significant accounting policies

The Financial Information has been prepared in accordance with HKFRSs, accounting principles generally accepted in Hong Kong and the applicable disclosures required by the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and the Hong Kong Companies Ordinance.

The Financial Information has been prepared under the historical cost convention.

The preparation of Financial Information in conformity with HKFRSs requires the use of certain key assumptions and estimates. It also requires the directors to exercise its judgements in the process of applying the accounting policies. The areas involving critical judgements and areas where assumptions and estimates are significant to the Financial Information, are disclosed in note 4 to the Financial Information.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

The significant accounting policies applied in the preparation of the Financial Information are set out below.

(a) Consolidation

The consolidated financial statements include the financial information of Sunlight Rise Limited and its subsidiaries made up to 31 December. Subsidiaries are entities over which the Target Group has control. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Target Group has control.

Subsidiaries are fully consolidated from the date on which control is transferred to the Target Group. They are de-consolidated from the date the control ceases.

Inter-company transactions, balances and unrealised profits on transactions between the Target Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Target Group.

In Sunlight Rise Limited's statement of financial position, the investments in subsidiaries are stated at cost less allowance for impairment losses. The results of subsidiaries are accounted for by Sunlight Rise Limited on the basis of dividends received and receivable.

(b) Foreign currency translation

(i) Functional and presentation currency

Items included in the Financial Information of each of the Target Group's entities are measured using the currency of the primary economic environment in which Sunlight Rise Limited operates (the "functional currency"). The consolidated financial information are presented in Hong Kong dollars, which is Sunlight Rise Limited's functional and presentation currency.

(ii) Transactions and balances in each entity's financial statements

Transactions in foreign currencies are translated into the functional currency on initial recognition using the exchange rates prevailing on the transaction dates. Monetary assets and liabilities in foreign currencies are translated at the exchange rates at the end of each reporting period. Gains and losses resulting from this translation policy are recognised in profit or loss.

Non-monetary items that are measured at fair values in foreign currencies are translated using the exchange rates at the dates when the fair values are determined.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

When a gain or loss on a non-monetary item is recognised in other comprehensive income, any exchange component of that gain or loss is recognised in other comprehensive income. When a gain or loss on a non-monetary item is recognised in profit or loss, any exchange component of that gain or loss is recognised in profit or loss.

(iii) Translation on consolidation

The results and financial position of all the Target Group entities that have a functional currency different from Sunlight Rise Limited's presentation currency are translated into Sunlight Rise Limited's presentation currency as follows:

- Assets and liabilities for each statement of financial position presented are translated at the closing rate at the date of that statement of financial position;
- Income and expenses for each statement of comprehensive income are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the exchange rates on the transaction dates); and
- All resulting exchange differences are recognised in the foreign currency translation reserve.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities and of borrowings are recognised in the foreign currency translation reserve. When a foreign operation is sold, such exchange differences are recognised in consolidated profit or loss as part of the gain or loss on disposal.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

(c) Recognition and derecognition of financial instruments

Financial assets and financial liabilities are recognised in the statement of financial position when the Target Group becomes a party to the contractual provisions of the instruments.

Financial assets are derecognised when the contractual rights to receive cash flows from the assets expire; the Target Group transfers substantially all the risks and rewards of ownership of the assets; or the Target Group neither transfers nor retains substantially all the risks and rewards of ownership of the assets but has not retained control on the assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income is recognised in profit or loss.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid is recognised in profit or loss.

(d) *Cash and cash equivalents*

For the purpose of the statement of cash flows, cash and cash equivalents represent cash on hand.

(e) *Other payables*

Other payables are stated initially at their fair value and subsequently measured at amortised cost using the effective interest method unless the effect of discounting would be immaterial, in which case they are stated at cost.

(f) *Taxation*

Income tax represents the sum of the current tax and deferred tax.

The tax currently payable is based on taxable profit for the period. Taxable profit differs from profit recognised in profit or loss because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Target Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of each reporting period.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the Financial Information and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences, unused tax losses or unused tax credits can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries, except where the Target Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

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 profits will be available to allow all or part of the asset to be recovered.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised, based on tax rates that have been enacted or substantively enacted by the end of each reporting period. Deferred tax is recognised in profit or loss, except when it relates to items recognised in other comprehensive income or directly in equity, in which case the deferred tax is also recognised in other comprehensive income or directly in equity.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Target Group intends to settle its current tax assets and liabilities on a net basis.

(g) *Related parties*

A party is related to the Target Group if:

- (i) directly or indirectly through one or more intermediaries, the party controls, is controlled by, or is under common control with, the Target Group; has an interest in the Target Group that gives it significant influence over the Target Group; or has joint control over the Target Group;
- (ii) the party is an associate;
- (iii) the party is a joint venture;
- (iv) the party is a member of the key management personnel of Sunlight Rise Limited or its parent;
- (v) the party is a close member of the family of any individual referred to in (i) or (iv);
- (vi) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (iv) or (v); or
- (vii) the party is a post-employment benefit plan for the benefit of employees of the Target Group, or of any entity that is a related party of the Target Group.

(h) *Provisions and contingent liabilities*

Provisions are recognised for liabilities of uncertain timing or amount when the Target Group has a present legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow is remote.

(i) Events after the reporting period

Events after the reporting period that provide additional information about the Target Group's position at the end of each reporting period or those that indicate the going concern assumption is not appropriate are adjusting events and are reflected in the Financial Information. Events after the reporting period that are not adjusting events are disclosed in the notes to the Financial Information when material.

4. Critical judgements and key estimates

These are no critical accounting judgements and key estimates in the preparation of the Financial Information.

5. Financial risk management

The Target Group's activities expose it to a variety of financial risks: foreign currency risk, credit risk and liquidity risk. The Target Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Target Group's financial performances.

(a) Foreign currency risk

The Target Group has minimal exposure to foreign currency risk as most of its business transactions, assets and liabilities are principally denominated in Hong Kong dollars, which is the functional currency of the Target Group. The Target Group currently does not have a foreign currency hedging policy in respect of foreign currency transactions, assets and liabilities. The Target Group will monitor its foreign currency exposure closely and will consider hedging significant foreign currency exposure should the need arise.

(b) Credit risk

The Target Group has no significant concentration of credit risk.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

(c) *Liquidity risk*

At 31 December 2009, the Target Group had net current liabilities and net liabilities of HK\$35,054,400 and HK\$54,400 respectively. The liquidity of the Target Group is primarily dependent on its ability to obtain ongoing support from its ultimate parent.

The maturity analysis of the Target Group's financial liabilities is as follows:

	Less than 1 year HK\$	Between 1 and 2 years HK\$	Between 2 and 5 years HK\$	Over 5 years HK\$
Accruals and other payables	35,011,993	–	–	–

(d) *Categories of financial instruments*

	As at 31 December 2009 HK\$
Financial assets	
– Loan and receivables (including cash and cash equivalents)	6,231
Financial liabilities	
– Amortised cost	35,011,993

(e) *Fair values*

The carrying amounts of the Target Group's financial assets and financial liabilities as reflected in the statement of financial position approximate their respective fair values.

6. *Turnover*

The Target Group had no turnover during the Relevant Period.

7. *Income tax expense*

- (a) No provision for Hong Kong Profits Tax is required since the Target Group has no assessable profit for the Relevant Period.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

- (b) The reconciliation between the income tax expense and the product of loss before tax multiplied by the Hong Kong Profits Tax rate is as follows:

	Period from 20 October 2009 to 31 December 2009 HK\$
Loss before tax	54,408
Tax at the income tax rate of 16.5%	(8,977)
Tax effect of expenses that are not deductible	8,977
Income tax expense	—

- (c) No provision for deferred taxation has been made in the Financial Information as the tax effect of temporary differences is immaterial to the Target Group.

8. Loss for the period

The Target Group's loss for the Relevant Period is stated after charging the following:

	Period from 20 October 2009 to 31 December 2009 HK\$
Directors' emoluments	—
Salaries, bonus and allowances	—

9. Loss attributable to equity holder of Sunlight Rise Limited

The loss attributable to equity holder of Sunlight Rise Limited included a loss of HK\$16,618 which has been dealt with in the financial statements of Sunlight Rise Limited.

10. Investments in subsidiaries

	As at 31 December 2009	
	Group	Company
	HK\$	HK\$
Unlisted investments, at cost	35,000,000	10,000

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

Particulars of the subsidiaries as at 31 December 2009 are as follows:

Name of subsidiary	Note	Place and date of incorporation/ establishment	Issued and fully paid share/ registered capital	Attributable equity interest of the Target Group		Principal activity
				Direct	Indirect	
Pride Treasure Limited		Hong Kong 27 March 2009	HK\$10,000	100%	–	Investment holding
Ontop Finance Limited		Hong Kong 29 April 2009	HK\$1	–	100%	Investment holding
Shanxi Zhong Kai Lingshi Heat & Power Company Limited	(a)&(b)	PRC 31 December 2005	Registered capital of RMB115,000,000	–	60%	Generation and supplying of electricity and heat

Notes:

- (a) The financial statements of this subsidiary are not consolidated in the Financial Information as in the opinion of the directors the consolidation of the financial statements would involve expense or delay out of proportion to the value to the purpose of this Financial Information.
- (b) No disclosures are made in the Financial Information in respect of the profit and loss of the unconsolidated subsidiary for the Relevant Period, and for the aggregate of the profits less losses for the period since it becomes a subsidiary as required by paragraph 18(4) of the Tenth Schedule of the Hong Kong Companies Ordinance.

11. Due from/(to) a subsidiary/a director/ultimate parent

The amounts due are unsecured, interest-free and have no fixed terms of repayment.

12. SHARE CAPITAL

**As at
31 December 2009**

Authorised:

50,000 ordinary shares of US\$1 each US\$50,000

Issued and fully paid:

1 ordinary share of US\$1 each US\$1

Equivalent to HK\$8

Sunlight Rise Limited was incorporated on 20 October 2009 with an authorised share capital of US\$50,000 divided into 50,000 ordinary shares of US\$1 each.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

During the period 1 ordinary share of US\$1 was issued at par for cash to incorporate the Target Group and provide initial working capital.

The Target Group's objectives when managing capital are to safeguard the Target Group's ability to continue as a going concern and to maximise the return to the shareholders through the optimisation of the debt and equity balance.

The Target Group currently does not have any specific policies and processes for managing capital.

13. Reserves – Sunlight Rise Limited

	Accumulated losses HK\$
Total comprehensive income for the period and at 31 December 2009	<u>16,618</u>

14. Capital commitments

The Target Group's capital commitments at the end of the reporting period is as follows:

	As at 31 December 2009 HK\$
Capital expenditure contracted but not provided for in the Financial Information in respect of unpaid balance of capital contributions to a subsidiary	<u>78,636,364</u>

On 6 May 2009, one of the Target Group's subsidiaries (the "Subsidiary") entered into an agreement with third parties to acquire 60% equity interest in a subsidiary, Shanxi Zhong Kai Lingshi Heat & Power Company Limited (the "Project Company"), which was established in the People's Republic of China ("PRC") on 31 December 2005. The Project Company is principally engaged in the business of generation and supplying of electricity and heat. Pursuant to the agreement, the total investments of the Subsidiary in the Project Company is RMB100,000,000 (equivalent to HK\$113,636,364) which is to be financed in the form of cash by the Subsidiary. At the end of the reporting period, the Subsidiary had contributed an amount of HK\$35,000,000 to the Project Company.

APPENDIX I ACCOUNTANTS' REPORT OF THE TARGET GROUP

15. Subsequent events

Apart from the capital commitments as mentioned in note 14 above, no significant subsequent event took place subsequent to 31 December 2009.

16. Subsequent financial statements

No audited financial statements have been prepared by the Target Group in respect of any period subsequent to 31 December 2009.

Yours faithfully

RSM Nelson Wheeler
Certified Public Accountants
Hong Kong

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

The following is the text of a report, prepared for the sole purpose of inclusion in this circular, from the independent reporting accountants, RSM Nelson Wheeler, Certified Public Accountants, Hong Kong.

RSM Nelson Wheeler
中瑞岳華 (香港) 會計師事務所
Certified Public Accountants

29th Floor,
Caroline Centre,
Lee Gardens Two,
28 Yun Ping Road,
Hong Kong

28 June 2010

The Board of Directors
Xian Yuen Titanium Resources Holdings Limited

Dear Sirs,

We set out below our report on the financial information (the “Financial Information”) of Shanxi Zhong Kai Lingshi Heat & Power Company Limited (“Shanxi Zhong Kai”) for each of the three years ended 31 December 2007, 2008 and 2009 (the “Relevant Periods”) for inclusion in the circular dated 28 June 2010 issued by Xian Yuen Titanium Resources Holdings Limited (the “Company”) in connection with the proposed acquisition of the 60% equity interest in Shanxi Zhong Kai (the “Circular”).

Shanxi Zhong Kai was incorporated on 31 December 2005 in the People’s Republic of China (the “PRC”) with limited liability and engaged in the business of generation and supplying of electricity and heat.

The financial year end of Shanxi Zhong Kai is 31 December and the statutory audited financial statements of Shanxi Zhong Kai for the years ended 31 December 2007 and 2008 were prepared in accordance with accounting principles and regulations applicable in the PRC and audited by Shanxi Jinhe Certified Public Accountants (山西晉和會計師事務所). No audited financial statements have been prepared for the year ended 31 December 2009.

For the purpose of this report, the directors of Shanxi Zhong Kai have prepared the financial statements of the Shanxi Zhong Kai for the Relevant Periods in accordance with Hong Kong Financial Reporting Standards (“HKFRSs”) issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”) (the “HKFRS Financial Statements”).

We have performed our independent audit on the HKFRS Financial Statements in accordance with Hong Kong Standards on Auditing issued by the HKICPA and have examined the HKFRS Financial Statements in accordance with Auditing Guideline 3.340 “Prospectuses and the Reporting Accountant” issued by the HKICPA.

The Financial Information has been prepared from the HKFRS Financial Statements in accordance with HKFRSs. No adjustments were considered necessary for the purpose of preparing our report for inclusion in the Circular.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

The directors of Shanxi Zhong Kai are responsible for the preparation of the HKFRS Financial Statements. The directors of the Company are responsible for the contents of the circular in which this report is included. It is our responsibility to compile the Financial Information set out in this report from the HKFRS Financial Statements, to form an independent opinion on the Financial Information and to report our opinion to you.

In our opinion, for the purpose of this report, the Financial Information gives a true and fair view of the state of affairs of Shanxi Zhong Kai as at 31 December 2007, 2008 and 2009 and of the Shanxi Zhong Kai's results and cash flows for the Relevant Periods.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

I. FINANCIAL INFORMATION

STATEMENTS OF COMPREHENSIVE INCOME

		Year ended 31 December		
	<i>Note</i>	2007 <i>RMB</i>	2008 <i>RMB</i>	2009 <i>RMB</i>
Turnover	6	27,317,134	88,527,829	100,247,868
Cost of sales		<u>(25,521,622)</u>	<u>(52,952,237)</u>	<u>(58,944,401)</u>
Gross profit		1,795,512	35,575,592	41,303,467
Other income	7	3,008,722	9,153,917	27,633,057
Administrative expenses		(3,945,757)	(3,819,300)	(5,150,887)
Other operating expenses		(2,450,083)	(1,859,205)	(1,968,731)
Finance costs	8	<u>(5,555,050)</u>	<u>(9,232,686)</u>	<u>(4,934,728)</u>
(Loss)/profit before tax		(7,146,656)	29,818,318	56,882,178
Income tax credit/(expense)	9	<u>1,497,365</u>	<u>(8,555,995)</u>	<u>(10,772,810)</u>
(Loss)/profit for the year	10	(5,649,291)	21,262,323	46,109,368
Other comprehensive income for the year		<u>—</u>	<u>—</u>	<u>—</u>
Total comprehensive income for the year		<u><u>(5,649,291)</u></u>	<u><u>21,262,323</u></u>	<u><u>46,109,368</u></u>

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

STATEMENTS OF FINANCIAL POSITION

		As at 31 December		
	Note	2007 RMB	2008 RMB	2009 RMB
Non-current assets				
Property, plant and equipment	12	221,608,921	236,695,378	239,238,009
Prepaid land lease payments	13	26,714,593	26,158,039	25,601,485
Deferred tax assets	23	2,095,447	3,099,452	1,936,285
		<u>250,418,961</u>	<u>265,952,869</u>	<u>266,775,779</u>
Current assets				
Inventories	14	228,896	1,146,573	2,453,225
Trade and bills receivable	15	3,006,518	1,135,451	9,472,925
Prepayments, deposits and other receivables		5,600,000	7,522,671	11,027,128
Due from fellow subsidiaries	16	49,992	2,903,696	–
Due from a shareholder	16	–	–	5,500,000
Due from a related company	17	1,537,125	24,983,753	22,636,487
Bank and cash balances	18	2,086,172	1,692,810	32,117,277
		<u>12,508,703</u>	<u>39,384,954</u>	<u>83,207,042</u>
Current liabilities				
Trade payables	19	5,212,838	4,036,004	12,943,048
Accruals and other payables		44,244,402	44,799,307	47,287,294
Due to fellow subsidiaries	16	–	1,067,824	–
Due to a shareholder	16	2,000,000	–	–
Due to related companies	16	–	–	1,065,519
Due to former ultimate parent	16	51,638,516	85,280,457	–
Tax payables		–	9,560,000	19,169,643
Bank loans	20	42,800,000	32,300,000	20,900,000
		<u>145,895,756</u>	<u>177,043,592</u>	<u>101,365,504</u>
Net current liabilities		<u>(133,387,053)</u>	<u>(137,658,638)</u>	<u>(18,158,462)</u>
Total assets less current liabilities		<u>117,031,908</u>	<u>128,294,231</u>	<u>248,617,317</u>
Non-current liabilities				
Loan from a related company	21	–	–	6,317,004
Loan from a shareholder (the former ultimate parent)	22	–	–	47,896,714
Bank loans	20	40,000,000	30,000,000	20,000,000
		<u>40,000,000</u>	<u>30,000,000</u>	<u>74,213,718</u>
NET ASSETS		<u><u>77,031,908</u></u>	<u><u>98,294,231</u></u>	<u><u>174,403,599</u></u>
Capital and reserves				
Paid up capital	24	85,000,000	85,000,000	115,000,000
Reserves		<u>(7,968,092)</u>	<u>13,294,231</u>	<u>59,403,599</u>
TOTAL EQUITY		<u><u>77,031,908</u></u>	<u><u>98,294,231</u></u>	<u><u>174,403,599</u></u>

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

STATEMENTS OF CHANGES IN EQUITY

	Paid up capital <i>RMB</i>	(Accumulated losses)/ retained profits <i>RMB</i>	Statutory reserve (note a) <i>RMB</i>	Total <i>RMB</i>
At 1 January 2007	50,000,000	(2,318,801)	–	47,681,199
Capital injection	35,000,000	–	–	35,000,000
Total comprehensive income for the year	–	(5,649,291)	–	(5,649,291)
Transfer	–	(206,549)	206,549	–
At 31 December 2007	85,000,000	(8,174,641)	206,549	77,031,908
Total comprehensive income for the year	–	21,262,323	–	21,262,323
Transfer	–	(2,868,347)	2,868,347	–
At 31 December 2008	85,000,000	10,219,335	3,074,896	98,294,231
Capital injection	30,000,000	–	–	30,000,000
Total comprehensive income for the year	–	46,109,368	–	46,109,368
Transfer	–	(2,882,893)	2,882,893	–
At 31 December 2009	<u>115,000,000</u>	<u>53,445,810</u>	<u>5,957,789</u>	<u>174,403,599</u>

Note:

- (a) Shanxi Zhong Kai, established in the PRC, is required each year to transfer 10% of the profit after taxation as reported under the PRC statutory financial statements to a statutory surplus reserve until the balance reaches 50% of the registered capital. The statutory surplus reserve may be used to make up losses incurred or to increase registered capital.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

STATEMENTS OF CASH FLOWS

	Year ended 31 December		
	2007	2008	2009
	<i>RMB</i>	<i>RMB</i>	<i>RMB</i>
CASH FLOWS FROM			
OPERATING ACTIVITIES			
(Loss)/Profit before tax	(7,146,656)	29,818,318	56,882,178
Adjustments for:			
Amortisation of prepaid land			
lease payments	556,554	556,554	556,554
Depreciation	4,595,821	10,454,472	9,432,394
Interest expenses	5,554,517	9,199,888	4,730,224
Interest income	(33,722)	(5,281)	(4,843)
Imputed interest income on interest-free			
loan from a related company	–	–	(982,996)
Imputed interest income on interest-free			
loan from a shareholder			
(the former ultimate parent)	–	–	(7,211,205)
Loss/(gain) on disposal/written-off of			
property, plant and equipment	–	8,870	(27,690)
Operating profit before working			
capital changes	3,526,514	50,032,821	63,374,616
Increase in inventories	(228,896)	(917,677)	(1,306,652)
(Increase)/decrease in trade and			
bills receivables	(2,146,699)	1,871,067	(8,337,474)
Increase in other receivables,			
prepayments and deposits	(4,740,742)	(1,922,671)	(3,504,457)
Increase/(decrease) in trade payables	5,212,838	(1,176,834)	8,907,044
Increase in accruals and other payables	32,903,951	554,905	2,487,987
Net cash generated from operation	34,526,966	48,441,611	61,621,064
Interest paid	(5,554,517)	(9,199,888)	(4,730,224)
Net cash generated from			
operating activities	28,972,449	39,241,723	56,890,840
CASH FLOWS FROM			
INVESTING ACTIVITIES			
Purchases of property, plant and equipment	(116,510,410)	(25,549,799)	(12,571,110)
Bank interest income	33,722	5,281	4,843
Proceeds from disposals of property,			
plant and equipment	–	–	623,775
Net cash used in investing activities	(116,476,688)	(25,544,518)	(11,942,492)

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

	Year ended 31 December		
	2007	2008	2009
	RMB	RMB	RMB
CASH FLOWS FROM			
FINANCING ACTIVITIES			
Proceeds from capital injection	26,975,207	–	30,000,000
Increase/(decrease) in amounts due from/(to) related companies	(1,537,125)	(23,446,628)	3,412,785
Increase/(decrease) in amounts due from/(to) fellow subsidiaries	950,008	(1,785,880)	1,835,872
Increase/(decrease) in amount due to a shareholder	2,000,000	(2,000,000)	(5,500,000)
Increase/(decrease) in amount due to former ultimate parent	(18,777,255)	33,641,941	(85,280,457)
Bank loans raised	78,800,000	–	–
Bank loans repaid	–	(20,500,000)	(21,400,000)
Loan from a related company	–	–	7,300,000
Loan from a shareholder (the former ultimate parent)	–	–	55,107,919
	<u> </u>	<u> </u>	<u> </u>
Net cash generated from/(used in) financing activities	<u>88,410,835</u>	<u>(14,090,567)</u>	<u>(14,523,881)</u>
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	906,596	(393,362)	30,424,467
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>1,179,576</u>	<u>2,086,172</u>	<u>1,692,810</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u><u>2,086,172</u></u>	<u><u>1,692,810</u></u>	<u><u>32,117,277</u></u>
ANALYSIS OF CASH AND CASH EQUIVALENTS			
Bank and cash balances	<u><u>2,086,172</u></u>	<u><u>1,692,810</u></u>	<u><u>32,117,277</u></u>

II. NOTES TO THE FINANCIAL INFORMATION**1. General information**

Shanxi Zhong Kai was incorporated in the PRC with limited liability. The address of its registered office and its principal place of business is Nanwangzhong Village, Cuifeng Town, Lingshi County, Shanxi Province, the PRC.

Shanxi Zhong Kai is principally engaged in the business of generating and supplying electricity and heat.

In the opinion of the directors of Shanxi Zhong Kai, as at 31 December 2009, Ontop Finance Limited, a company incorporated in Hong Kong, is the immediate parent, Maycrown Capital Limited, a company incorporated in the British Virgin Islands, is the ultimate parent and Miss Ho Mee Kuen Karen is the ultimate controlling party of Shanxi Zhong Kai.

2. Adoption of new and revised Hong Kong Financial Reporting Standards

During the Relevant Periods, Shanxi Zhong Kai has adopted all the new and revised HKFRSs that are relevant to its operations and effective for its accounting period beginning on 1 January 2009. HKFRSs comprise Hong Kong Financial Reporting Standards; Hong Kong Accounting Standards; and Interpretations.

Shanxi Zhong Kai has not applied the new HKFRSs that have been issued but are not yet effective. Shanxi Zhong Kai has already commenced an assessment of the impact of these new HKFRSs but is not yet in a position to state whether these new HKFRSs would have a material impact on its results of operation and financial position.

3. Significant accounting policies

The Financial Information has been prepared in accordance with HKFRSs, accounting principles generally accepted in Hong Kong and the applicable disclosures required by the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

The Financial Information has been prepared under the historical cost convention.

The preparation of Financial Information in conformity with HKFRSs requires the use of certain key assumptions and estimates. It also requires the directors to exercise its judgements in the process of applying the accounting policies. The areas involving critical judgements and areas where assumptions and estimates are significant to the Financial Information, are disclosed in note 4 to the Financial Information.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

The significant accounting policies applied in the preparation of the Financial Information are set out below.

(a) Foreign currency translation

(i) Functional and presentation currency

Items included in the Financial Information are measured using the currency of the primary economic environment in which Shanxi Zhong Kai operates (the “functional currency”). The Financial Information is presented in Renminbi (“RMB”), which is Shanxi Zhong Kai’s functional and presentation currency.

(ii) Transactions and balances in Financial Information

Transactions in foreign currencies are translated into the functional currency on initial recognition using the exchange rates prevailing on the transaction dates. Monetary assets and liabilities in foreign currencies are translated at the exchange rates at the end of each reporting period. Gains and losses resulting from this translation policy are recognised in profit or loss.

(b) Property, plant and equipment

Land and buildings comprise mainly factories and offices. All property, plant and equipment are stated at cost less accumulated depreciation and impairment losses.

Subsequent costs are included in the asset’s carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to Shanxi Zhong Kai and the cost of the item can be measured reliably. All other repairs and maintenance are recognised in profit or loss during the period in which they are incurred.

Depreciation of property, plant and equipment is calculated at rates sufficient to write off their cost less their residual values over the estimated useful lives on a straight-line basis. The estimated useful lives are as follows:

	Years ended 31 December 2007 and 2008	Year ended 31 December 2009
Buildings	20 years	29 years
Plant and machinery	10 years	12 years
Electronic equipment	10 years	3 years
Furniture and fixtures	10 years	5 years
Motor vehicles	5 years	6 years

In 2009, Shanxi Zhong Kai has revised the estimated useful lives of certain property, plant and equipment. The change in depreciation estimate has increased the profit for the year ended 31 December 2009 by RMB5,444,325.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

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

Construction in progress represents buildings under construction and plant and machinery pending installation, and is stated at cost less impairment losses. Depreciation begins when the relevant assets are available for use.

The gain or loss on disposal of property, plant and equipment is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in profit or loss.

(c) *Inventories*

Raw materials are stated at the lower of cost and net realisable value. Cost of coke is determined using the weighted average basis. All other raw materials is determined using the first-in, first-out basis. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale.

(d) *Recognition and derecognition of financial instruments*

Financial assets and financial liabilities are recognised in the statement of financial position when Shanxi Zhong Kai becomes a party to the contractual provisions of the instruments.

Financial assets are derecognised when the contractual rights to receive cash flows from the assets expire; Shanxi Zhong Kai transfers substantially all the risks and rewards of ownership of the assets; or Shanxi Zhong Kai neither transfers nor retains substantially all the risks and rewards of ownership of the assets but has not retained control on the assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income is recognised in profit or loss.

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid is recognised in profit or loss.

(e) *Trade and other receivables*

Trade and other receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less allowance for impairment. An allowance for impairment of trade and other receivables is established when there is objective evidence that Shanxi Zhong Kai will not be able to collect all amounts due according to the original terms of receivables. The amount of the allowance is the difference between the receivables' carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate computed at initial recognition. The amount of the allowance is recognised in profit or loss.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

Impairment losses are reversed in subsequent periods and recognised in profit or loss when an increase in the receivables' recoverable amount can be related objectively to an event occurring after the impairment was recognised, subject to the restriction that the carrying amount of the receivables at the date the impairment is reversed shall not exceed what the amortised cost would have been had the impairment not been recognised.

(f) Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents represent cash at bank and on hand, demand deposits with banks and other financial institutions, and short-term highly liquid investments which are readily convertible into known amounts of cash and subject to an insignificant risk of change in value. Bank overdrafts which are repayable on demand and form an integral part of Shanxi Zhong Kai's cash management are also included as a component of cash and cash equivalents.

(g) Financial liabilities and equity instruments

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument under HKFRSs. An equity instrument is any contract that evidences a residual interest in the assets of Shanxi Zhong Kai after deducting all of its liabilities. The accounting policies adopted for specific financial liabilities and equity instruments are set out below.

(h) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred, and subsequently measured at amortised cost using the effective interest method.

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

(i) Trade and other payables

Trade and other payables are stated initially at their fair value and subsequently measured at amortised cost using the effective interest method unless the effect of discounting would be immaterial, in which case they are stated at cost.

(j) Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and is recognised when it is probable that the economic benefits will flow to Shanxi Zhong Kai and the amount of revenue can be measured reliably.

Revenues from sale of power is recognised upon the transmission of electricity and heat to the customer as determined based on the volume of electricity and heat transmitted and the applicable fixed tariff rates agreed with the respective customers annually.

Rental income is recognised on a straight-line basis over the lease term.

Interest income is recognised on a time-proportion basis using the effective interest method.

(k) Employee benefits

(i) Employee leave entitlements

Employee entitlements to long service leave are recognised when they accrue to employees. A provision is made for the estimated liability for long service leave as a result of services rendered by employees up to the end of the reporting period.

Employee entitlements to sick leave and maternity leave are not recognised until the time of leave.

(ii) Retirement benefits

The full-time employee are covered by various government-sponsored retirement plans under which the employees are entitled to a monthly pension based on certain formulas. The relevant government agencies are responsible for the pension liability to these retired employees. Shanxi Zhong Kai contributes on a monthly basis to these retirement plans. Under these plans, Shanxi Zhong Kai has no obligation for the post-retirement benefits beyond the contributions made. Contributions to these plans are expensed as incurred.

(l) Borrowings costs

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

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

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

With effective from 1 January 2009, to the extent that funds are borrowed generally and used for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation is determined by applying a capitalisation rate to the expenditures on that asset. The capitalisation rate is the weighed average of the borrowing costs applicable to the borrowings of Shanxi Zhong Kai that are outstanding during the relevant periods, other than borrowings made specifically for the purpose of obtaining a qualifying asset.

(m) Government grants

A government grant is recognised when there is reasonable assurance that Shanxi Zhong Kai will comply with the conditions attaching to it and that the grant will be received.

Government grants relating to income are deferred and recognised in profit or loss over the period to match them with the costs they are intended to compensate.

Government grants that become receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to Shanxi Zhong Kai with no future related costs are recognised in profit or loss in the period in which they become receivable.

Government grants relating to the purchase of assets are recorded as deferred income and recognised in profit or loss on a straight-line basis over the useful lives of the related assets.

(n) Taxation

Income tax represents the sum of the current tax and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit recognised in profit or loss because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. Shanxi Zhong Kai's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of each reporting period.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the Financial Information and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences, unused tax losses or unused tax credits can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

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 profits will be available to allow all or part of the asset to be recovered.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised, based on tax rates that have been enacted or substantively enacted by the end of each reporting period. Deferred tax is recognised in profit or loss, except when it relates to items recognised in other comprehensive income or directly in equity, in which case the deferred tax is also recognised in other comprehensive income or directly in equity.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and Shanxi Zhong Kai intends to settle its current tax assets and liabilities on a net basis.

(o) *Related parties*

A party is related to Shanxi Zhong Kai if:

- (i) directly or indirectly through one or more intermediaries, the party controls, is controlled by, or is under common control with, Shanxi Zhong Kai; has an interest in Shanxi Zhong Kai that gives it significant influence over Shanxi Zhong Kai; or has joint control over Shanxi Zhong Kai;
- (ii) the party is an associate;
- (iii) the party is a joint venture;
- (iv) the party is a member of the key management personnel of Shanxi Zhong Kai or its parent;
- (v) the party is a close member of the family of any individual referred to in (i) or (iv);
- (vi) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (iv) or (v); or
- (vii) the party is a post-employment benefit plan for the benefit of employees of Shanxi Zhong Kai, or of any entity that is a related party of Shanxi Zhong Kai.

(p) *Impairment of assets*

At the end of each reporting period, Shanxi Zhong Kai reviews the carrying amounts of its tangible assets except inventories and receivables to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of any impairment loss. Where it is not possible to estimate the recoverable amount of an individual asset, Shanxi Zhong Kai estimates the recoverable amount of the cash-generating unit to which the asset belongs.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

Recoverable amount is the higher of fair value less costs to sell and value in use. 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.

If the recoverable amount of an asset or cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset or cash-generating unit is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset or cash-generating unit in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

(q) Provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when Shanxi Zhong Kai has a present legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow is remote.

(r) Events after the reporting period

Events after the reporting period that provide additional information about Shanxi Zhong Kai's position at the end of each reporting period or those that indicate the going concern assumption is not appropriate are adjusting events and are reflected in the Financial Information. Events after the reporting period that are not adjusting events are disclosed in the notes to the Financial Information when material.

4. Critical judgements and key estimates***Key sources of estimation uncertainty***

The key assumptions concerning the future, and other key sources of estimation uncertainty at the end of each 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 discussed below.

(a) Property, plant and equipment and depreciation

Shanxi Zhong Kai determines the estimated useful lives, residual values and related depreciation charges for its property, plant and equipment. This estimate is based on the historical experience of the actual useful lives and residual values of property, plant and equipment of similar nature and functions. Shanxi Zhong Kai will revise the depreciation charge where useful lives and residual values are different to those previously estimated, or it will write-off or write-down technically obsolete or non-strategic assets that have been abandoned or sold.

(b) Income taxes

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

5. Financial risk management

Shanxi Zhong Kai's activities expose it to a variety of financial risks: foreign currency risk, credit risk, interest rate risk and liquidity risk. Shanxi Zhong Kai's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on Shanxi Zhong Kai's financial performances.

(a) Foreign currency risk

Shanxi Zhong Kai has minimal exposure to foreign currency risk as most of its business transactions, assets and liabilities are principally denominated in Renminbi, which is the functional currency of Shanxi Zhong Kai. Shanxi Zhong Kai currently does not have a foreign currency hedging policy in respect of foreign currency transactions, assets and liabilities. Shanxi Zhong Kai will monitor its foreign currency exposure closely and will consider hedging significant foreign currency exposure should the need arise.

(b) Credit risk

The carrying amount of trade and other receivables and bank and cash balances included in the statement of financial position represent Shanxi Zhong Kai's maximum exposure to credit risk in relation to Shanxi Zhong Kai's financial assets.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

(c) Interest rate risk

Majority of Shanxi Zhong Kai's bank borrowings bear interests at fixed interest rates and therefore are subject to fair value interest rate risk.

(d) Liquidity risk

At 31 December 2009, Shanxi Zhong Kai had net current liabilities of RMB18,158,462. The liquidity of Shanxi Zhong Kai is primarily dependent on its ability to maintain adequate cash inflows from operations to meet its debt obligations and to obtain ongoing support from its controlling shareholders.

The maturity analysis of Shanxi Zhong Kai's financial liabilities is as follows:

	Less than 1 year RMB	Between 1 and 2 years RMB	Between 2 and 5 years RMB	Over 5 years RMB
At 31 December 2009				
Trade payables	12,943,048	—	—	—
Other payables	36,984,345	—	—	—
Loan from a related company	—	—	7,300,000	—
Loan from a shareholder (the former ultimate parent)	—	—	55,107,919	—
Bank loans	<u>22,824,620</u>	<u>11,684,800</u>	<u>12,527,200</u>	<u>—</u>
At 31 December 2008				
Trade payables	4,036,004	—	—	—
Other payables	33,443,693	—	—	—
Due to a fellow subsidiary	1,067,824	—	—	—
Due to former ultimate parent	85,280,457	—	—	—
Bank loans	<u>36,379,226</u>	<u>11,684,800</u>	<u>25,896,800</u>	<u>—</u>
At 31 December 2007				
Trade payables	5,212,838	—	—	—
Other payables	42,664,632	—	—	—
Due to a shareholder	2,000,000	—	—	—
Due to former ultimate parent	51,638,516	—	—	—
Bank loans	<u>47,684,060</u>	<u>11,684,800</u>	<u>40,108,800</u>	<u>—</u>

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

(e) Categories of financial instruments

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Financial assets			
– Loan and receivables (including cash and cash equivalents)	12,229,807	36,265,711	74,282,480
Financial liabilities			
– Amortised cost	184,315,986	186,127,978	146,106,631

(f) Fair values

The carrying amounts of Shanxi Zhong Kai's financial assets and financial liabilities as reflected in the statement of financial position approximate their respective fair values.

6. Turnover and segment information

Shanxi Zhong Kai is principally engaged in generation and supply of heat and electricity to customers. Turnover represents the aggregate of the invoiced value of goods sold.

No segment information is presented as Shanxi Zhong Kai operates in one single industry, generating and supplying electricity and heat; and trade and operates within one geographic location which is also the same basis as financial information that is reported internally to the chief operating decision maker, the directors of Shanxi Zhong Kai. Substantially all of Shanxi Zhong Kai's assets and liabilities are located in Shanxi Province, the PRC and therefore no geographical information has been disclosed for the Relevant Periods.

Turnover from major customers:

	Year ended 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Customer a	4,579,908	–	10,572,947
Customer b	4,736,053	11,383,092	14,285,474
Customer c	6,055,235	–	–
Customer d	4,329,480	11,257,046	–
Customer e	4,829,238	11,230,890	25,934,498
Customer f	–	29,729,196	32,380,516
Customer g	–	9,563,443	–
	24,529,914	73,163,667	83,173,435

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

7. Other income

	Year ended 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Bank interest income	33,722	5,281	4,843
Gain on disposals of property, plant and equipment	–	–	27,690
Government grants	1,500,000	3,300,000	3,000,000
Imputed interest income on interest-free loan from a related company	–	–	982,996
Imputed interest income on interest-free loan from a shareholder (the former ultimate parent)	–	–	7,211,205
Rental income	–	4,955,399	12,900,000
Sundry income	1,475,000	893,237	3,506,323
	<u>3,008,722</u>	<u>9,153,917</u>	<u>27,633,057</u>

8. Finance costs

	Year ended 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Bank charges	533	32,798	204,504
Interest expenses	5,554,517	9,199,888	4,730,224
	<u>5,555,050</u>	<u>9,232,686</u>	<u>4,934,728</u>

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

9. Income tax (credit)/expense

(a)

	Year ended 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Current tax:			
PRC Enterprise Income Tax	–	9,560,000	9,609,643
Deferred tax (note 23)	(1,497,365)	(1,004,005)	1,163,167
	<u>(1,497,365)</u>	<u>8,555,995</u>	<u>10,772,810</u>

No provision for PRC Enterprise Income Tax for the year ended 31 December 2007 is required since Shanxi Zhong Kai has no assessable profit for the year.

Shanxi Zhong Kai is subject to the PRC Enterprise Income Tax at the rate of 33% for the year ended 31 December 2007.

On 16 March 2007, the PRC promulgated the Law of the PRC on Enterprise Income Tax (the “New Law”) by Order No. 63 of the President of the PRC. On 6 December 2007, the State Council of the PRC issued Implementation Regulation of the New Law. Under the New Law and Implementation Regulation, the Enterprise Income Tax rate of Shanxi Zhong Kai was reduced from 33% to 25% from 1 January 2008 onwards. Accordingly, the relevant tax rate for Shanxi Zhong Kai is 25% for the years ended 31 December 2008 and 2009.

(b) The reconciliation between the income tax (credit)/expense and the product of (loss)/profit before tax multiplied by the PRC Enterprise Income Tax rate is as follows:

	Year ended 31 December		
	2007	2008	2009
	RMB	RMB	RMB
(Loss)/profit before tax	<u>(7,146,656)</u>	<u>29,818,318</u>	<u>56,882,178</u>
Domestic tax rate	33%	25%	25%
Tax at the domestic tax rate	(2,358,397)	7,454,580	14,220,545
Tax effect of income that is not taxable	(24,750)	(1,250)	(3,915,540)
Tax effect of expenses that are not deductible	1,088,237	690,360	392,805
Under/(over) provision of taxation in current year	(202,455)	614,760	(337,305)
Under/(over) provision of taxation in prior years	<u>–</u>	<u>(202,455)</u>	<u>412,305</u>
Income tax (credit)/expense	<u>(1,497,365)</u>	<u>8,555,995</u>	<u>10,772,810</u>

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

10. (Loss)/profit for the year

Shanxi Zhong Kai's (loss)/profit for the year is stated after charging the following:

	Year ended 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Auditor's remuneration	–	5,000	205,000
Amortisation of prepaid land lease payments	556,554	556,554	556,554
Cost of inventories sold	25,521,622	52,952,237	58,944,401
Depreciation of property, plant and equipment	4,595,821	10,454,472	9,432,394
Directors' emoluments	–	–	–
Loss on disposals of property, plant and equipment	–	8,870	–
Retirement benefits scheme contributions	754,881	1,394,865	1,236,454
Salaries, bonus and allowances	5,278,713	6,457,437	7,464,509
Staff costs including directors' emoluments	6,033,594	7,852,302	8,700,963

11. Five highest paid individuals

The five individuals whose emoluments were the highest in Shanxi Zhong Kai for the Relevant Periods are as follows:

	Year ended 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Salaries and allowances	130,828	153,074	178,477
Contribution to pension plans	40,688	46,075	53,722
	171,516	199,149	232,199

During the Relevant Periods, the emoluments for each of the above individuals were within the emoluments band of less than HK\$1,000,000 (equivalent to RMB880,980).

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

12. Property, plant and equipment

	Buildings <i>RMB</i>	Construction in progress <i>RMB</i>	Plant and machinery <i>RMB</i>	Electronic equipment <i>RMB</i>	Furniture and fixtures <i>RMB</i>	Motor vehicles <i>RMB</i>	Total <i>RMB</i>
Cost							
At 1 January 2007	–	101,055,998	–	25,699	–	587,842	101,669,539
Additions	33,232,166	55,751,883	33,318,392	653,686	229,136	1,349,940	124,535,203
Transfers	–	(4,100,000)	4,100,000	–	–	–	–
At 31 December 2007	33,232,166	152,707,881	37,418,392	679,385	229,136	1,937,782	226,204,742
Additions	4,027,912	4,622,029	16,035,609	80,663	168,487	615,099	25,549,799
Transfers	15,741,975	(103,238,819)	87,467,044	29,800	–	–	–
Disposals/Written off	–	–	–	(8,832)	(332)	–	(9,164)
At 31 December 2008	53,002,053	54,091,091	140,921,045	781,016	397,291	2,552,881	251,745,377
Additions	–	10,070,508	2,009,541	45,632	–	445,429	12,571,110
Transfers	–	(893,000)	650,000	–	–	243,000	–
Disposals/Written off	–	–	–	–	–	(762,639)	(762,639)
At 31 December 2009	53,002,053	63,268,599	143,580,586	826,648	397,291	2,478,671	263,553,848
Accumulated depreciation and impairment							
At 1 January 2007	–	–	–	–	–	–	–
Charge for the year	559,690	–	3,832,779	67,938	20,933	114,481	4,595,821
At 31 December 2007	559,690	–	3,832,779	67,938	20,933	114,481	4,595,821
Charge for the year	2,537,826	–	7,194,022	66,235	(11,805)	668,194	10,454,472
Disposals/Written off	–	–	–	(283)	(11)	–	(294)
At 31 December 2008	3,097,516	–	11,026,801	133,890	9,117	782,675	15,049,999
Charge for the year	719,012	–	7,896,498	610,711	165,677	40,496	9,432,394
Disposals/Written off	–	–	–	–	–	(166,554)	(166,554)
At 31 December 2009	3,816,528	–	18,923,299	744,601	174,794	656,617	24,315,839
Carrying amount							
At 31 December 2009	49,185,525	63,268,599	124,657,287	82,047	222,497	1,822,054	239,238,009
At 31 December 2008	49,904,537	54,091,091	129,894,244	647,126	388,174	1,770,206	236,695,378
At 31 December 2007	32,672,476	152,707,881	33,585,613	611,447	208,203	1,823,301	221,608,921

It is Shanxi Zhong Kai's policy to lease out certain buildings and plant and machinery under operating leases. The average lease term is two years. All leases are on a fixed rental basis and do not include contingent rentals.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

Shanxi Zhong Kai's total future minimum lease payments under non-cancellable operating leases are receivable as follows:

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Within one year	<u>–</u>	<u>12,900,000</u>	<u>–</u>

13. Prepaid land lease payments

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Opening carrying amount	27,271,147	26,714,593	26,158,039
Amortisation charge	<u>(556,554)</u>	<u>(556,554)</u>	<u>(556,554)</u>
Closing carrying amount	<u>26,714,593</u>	<u>26,158,039</u>	<u>25,601,485</u>

Shanxi Zhong Kai's prepaid land lease payments for land use rights are situated in the PRC under medium term leases.

14. Inventories

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Raw materials	<u>228,896</u>	<u>1,146,573</u>	<u>2,453,225</u>

15. TRADE RECEIVABLES

Shanxi Zhong Kai's trading terms with its customers are mainly on credit. The credit period is generally for a period of two months, extending up to three months for certain well-established customers.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

As at the end of each reporting period, the ageing analysis of the Shanxi Zhong Kai's trade receivables, based on the date of transmission of electricity and heat to the customers, was as follows:

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Up to 1 month	2,906,518	835,451	4,903,400
1 to 3 months	—	—	3,791,723
3 to 6 months	—	—	523,267
	<u>2,906,518</u>	<u>835,451</u>	<u>9,218,390</u>

Impairment losses in respect of trade receivables are recorded using an allowance account unless Shanxi Zhong Kai is satisfied that recovery of the amount is remote, in which case the impairment loss is written off against trade receivables directly. There was no impairment provision as at the end of each reporting period.

As at the end of each reporting period, the following trade receivables were past due but not impaired. These relate to a number of independent customers for whom there is no recent history of default. The ageing analysis of these trade receivables is as follows:

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Up to 3 month	<u>—</u>	<u>—</u>	<u>523,266</u>

Receivables that were past due but not impaired related to amounts receivable from customers that have a good track record with Shanxi Zhong Kai. Based on past experience, the management believes that no 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. Due from/(to) fellow subsidiaries/related companies/former ultimate parent/ a shareholder

The amounts due are unsecured, interest-free and have no fixed terms of repayment.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

17. Due from a related company

Amount due from a related company disclosed pursuant to section 161B of the Hong Kong Companies Ordinance are as follows:

Name	Name of director has beneficial interest	Balance at 31 December 2007 RMB	Balance at 1 January 2007 RMB	Maximum amount outstanding during the year RMB
山西中凱集團靈石能源開發有限公司	Mr. Li Jin Xu	1,537,125	–	1,537,125

Name	Name of director has beneficial interest	Balance at 31 December 2008 RMB	Balance at 1 January 2008 RMB	Maximum amount outstanding during the year RMB
山西中凱集團靈石能源開發有限公司	Mr. Li Jin Xu	24,983,753	1,537,125	24,983,753

Name	Name of director has beneficial interest	Balance at 31 December 2009 RMB	Balance at 1 January 2009 RMB	Maximum amount outstanding during the year RMB
山西中凱集團靈石能源開發有限公司	Mr. Li Jin Xu	22,636,487	24,983,753	24,983,753

The amount due is unsecured, interest-free and has no fixed repayment terms.

18. Bank and cash balances

Bank and cash balances of RMB2,086,172, RMB1,692,810 and RMB2,117,277 as at 31 December 2007, 2008 and 2009 were denominated in RMB. Conversion of RMB into foreign currencies is subject to the PRC's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations.

As at 31 December 2009, an amount of US\$4,512,407 (equivalent to RMB30,000,000) included in the bank and cash balances represented a capital injection from immediate parent. Since capital injection verification report has not yet been prepared as at 31 December 2009, the amount was restricted by a bank.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

19. Trade payables

An aging analysis of trade payables of Shanxi Zhong Kai is as follows:

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Up to 1 month	5,212,838	325,838	1,871,510
1 to 3 months	–	3,153,100	3,661,868
3 to 6 months	–	528,482	2,033,870
6 months to one year	–	28,584	5,375,800
	<u>5,212,838</u>	<u>4,036,004</u>	<u>12,943,048</u>

20. Bank loans

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Bank loans	<u>82,800,000</u>	<u>62,300,000</u>	<u>40,900,000</u>

The bank loans are repayable as follows:

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
On demand or within one year	42,800,000	32,300,000	20,900,000
In the second year	10,000,000	10,000,000	10,000,000
In the third to fifth years, inclusive	<u>30,000,000</u>	<u>20,000,000</u>	<u>10,000,000</u>
	82,800,000	62,300,000	40,900,000
Less: Amount due for settlement within 12 months (shown under current liabilities)	<u>(42,800,000)</u>	<u>(32,300,000)</u>	<u>(20,900,000)</u>
Amount due for settlement after 12 months	<u>40,000,000</u>	<u>30,000,000</u>	<u>20,000,000</u>

The average interest rates were as follows:

	As at 31 December		
	2007	2008	2009
Bank loans	10.88%	12.45%	9.5%

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

All bank loans are arranged at floating rates, thus exposing Shanxi Zhong Kai to cash flow interest rate risk.

Bank loans of RMB50,000,000, RMB40,000,000 and RMB33,000,000 as at 31 December 2007 and 2008 and 31 December 2009 are secured by a charge over the property of a former fellow subsidiary of Shanxi Zhong Kai and the former fellow subsidiary has become a related company of Shanxi Zhong Kai since August 2009.

21. Loan from a related company

The loan is unsecured, interest-free and matures in 7 September 2012.

22. Loan from a shareholder (the former ultimate parent)

The loan is unsecured, interest-free and matures in 31 August 2012.

23. Deferred tax

The following are the major deferred tax liabilities and assets recognised by Shanxi Zhong Kai.

	<i>RMB</i>
At 1 January 2007	(598,082)
Charge to profit or loss for the year (<i>note 9</i>)	<u>(1,497,365)</u>
At 31 December 2007	(2,095,447)
Charge to profit or loss for the year (<i>note 9</i>)	<u>(1,004,005)</u>
At 31 December 2008	(3,099,452)
Credit to profit or loss for the year (<i>note 9</i>)	<u>1,163,167</u>
At 31 December 2009	<u><u>(1,936,285)</u></u>

The following is an analysis of the deferred tax balances (after offset) for statement of financial position:

	As at 31 December		
	2007	2008	2009
	<i>RMB</i>	<i>RMB</i>	<i>RMB</i>
Deferred tax assets	<u>2,095,447</u>	<u>3,099,452</u>	<u>1,936,285</u>

The deferred tax assets represent the temporary differences in respect of the recognition of incomes and expenses between HKFRSs and the PRC Tax Authority.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

24. Paid up capital

	As at 31 December		
	2007 RMB	2008 RMB	2009 RMB
Registered	<u>85,000,000</u>	<u>85,000,000</u>	<u>185,000,000</u>
Paid up	<u>85,000,000</u>	<u>85,000,000</u>	<u>115,000,000</u>

Shanxi Zhong Kai was incorporated on 31 December 2005 with a registered capital of RMB50,000,000.

By a special resolution passed on 28 July 2007 the registered capital of Shanxi Zhong Kai was increased from RMB50,000,000 to RMB85,000,000. As per the capital injection verification report dated 25 August 2007, the capital increase was satisfied by injection of cash, tangible assets and prepaid land lease payments.

Pursuant to a shareholders' agreement dated on 6 May 2009, the registered capital of Shanxi Zhong Kai was increased from RMB85,000,000 to RMB185,000,000. An amount of RMB30,000,000 (equivalent to HK\$35,000,000) of the registered capital had been injected on 9 November 2009. However, the capital injection verification report has not yet been prepared.

Pursuant to a joint venture agreement dated on 6 May 2009, RMB30,000,000 of the registered capital of RMB185,000,000 should be injected within three months from 11 August 2009, a further sum of RMB30,000,000 shall be injected within the following three months; and the remaining balance shall be injected within one year. However, Shanxi Zhong Kai will procure and obtain from the PRC government authority to extend the time of fully paying up the registered capital to a date not earlier than 1 July 2011.

Shanxi Zhong Kai's objectives when managing capital are to safeguard Shanxi Zhong Kai's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders, and to provide an adequate return to shareholders.

Shanxi Zhong Kai manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, Shanxi Zhong Kai may adjust the amount of dividends paid to shareholders, if any, return capital to shareholders, issue new shares, or sell assets to reduce debts. No changes were made in the objectives, policies and processes during the Relevant Periods.

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

25. Related party transactions

- (a) In addition to those related party transactions and balances disclosed elsewhere in the Financial Information, Shanxi Zhong Kai had the following transactions with its related parties during the year:

	Year ended 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Acquisition of property, plant and equipment from a shareholder	63,534,308	—	—
Sales to related companies	24,597	29,729,063	36,775,696
Sales to fellow subsidiaries	4,446,572	12,062,867	—
Sales to former ultimate parent	6,055,235	—	—
Purchases from a shareholder	5,330,200	—	—

Sales to and purchases from former ultimate parent, a shareholder, fellow subsidiaries and related companies were made in the normal course of business and accordingly to the prices and terms mutually agreed.

- (b) *Compensation of key management personnel of the Shanxi Zhong Kai*

	Year ended 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Salaries and allowances	115,630	111,972	54,364
Contribution to pension plan	35,961	34,823	16,907
	151,591	146,795	71,271

APPENDIX II ACCOUNTANTS' REPORT OF THE PROJECT COMPANY

26. Capital commitments

Shanxi Zhong Kai's capital commitments at the end of the reporting period are as follows:

	As at 31 December		
	2007	2008	2009
	RMB	RMB	RMB
Property, plant and equipment			
Contracted but not provided for	23,168,814	11,787,696	3,615,674

27. Subsequent events

No significant subsequent event took place subsequent to 31 December 2009.

28. Subsequent financial statements

No audited financial statements have been prepared by Shanxi Zhong Kai in respect of any period subsequent to 31 December 2009.

Yours faithfully

RSM Nelson Wheeler
Certified Public Accountants
Hong Kong

APPENDIX III**FINANCIAL INFORMATION OF THE GROUP****THREE YEARS FINANCIAL SUMMARY**

Set out below is a summary of the audited consolidated results and assets and liabilities of the Group for each of the three years ended 31 December 2009 as extracted from the respective published audited financial statements:

AUDITED CONSOLIDATED RESULTS

	For the year ended 31 December		
	2009	2008	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
			(Restated)
Continuing operations:			
Revenue	10,332	12,846	28,851
Cost of sales	(10,020)	(10,883)	(22,042)
Gross profit	312	1,963	6,809
Other income	2,515	10,752	4,016
Selling and distribution expenses	–	(734)	(2,071)
Administrative expenses	(25,327)	(40,397)	(45,511)
Other operating expenses	(41,707)	(14,850)	(1,110)
Impairment loss recognised in respect of goodwill	(368,401)	(253,030)	(327)
Operating loss	(432,608)	(296,296)	(38,194)
Finance costs	(7,920)	(22,521)	(3,235)
Loss before income tax	(440,528)	(318,817)	(41,429)
Income tax expense	–	–	–
Loss after tax from continuing operations	(440,528)	(318,817)	(41,429)
Discontinued operations:			
Loss for the year from discontinued operations	8,341	(29,665)	(37,132)
Loss for the year	<u>(432,187)</u>	<u>(348,482)</u>	<u>(78,561)</u>
Attributable to:			
Equity holders of the Company	(432,187)	(341,321)	(79,129)
Non-controlling interests	–	(7,161)	568
Loss for the year	<u>(432,187)</u>	<u>(348,482)</u>	<u>(78,561)</u>

APPENDIX III**FINANCIAL INFORMATION OF THE GROUP**

	For the year ended 31 December		
	2009	2008	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i> (Restated)
Loss per share for loss attributable to the owners of the Company			
– Basic			
From continuing and discontinued operations	(HK8.2 cents)	(HK 13.4 cents)	(HK 9.4 cents)
From continuing operations	<u>(HK8.3 cents)</u>	<u>(HK 12.4 cents)</u>	<u>(HK 5.0 cents)</u>
– Diluted			
From continuing and discontinued operations	N/A	N/A	N/A
From continuing operations	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>
As at 31 December			
	2009	2008	2007
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
ASSETS AND LIABILITIES			
Non-current assets	554,799	747,086	702,176
Current assets	<u>114,775</u>	<u>93,511</u>	<u>168,012</u>
Total assets	<u>669,574</u>	<u>840,597</u>	<u>870,188</u>
Current liabilities	22,559	64,123	68,157
Non-current liabilities	<u>19,279</u>	<u>192,695</u>	<u>177,403</u>
Total liabilities	<u>41,838</u>	<u>256,818</u>	<u>245,560</u>
Equity			
Equity attributable to owner of the Company	627,736	582,491	591,047
Non-controlling interests	<u>–</u>	<u>1,288</u>	<u>33,581</u>
	<u>627,736</u>	<u>583,779</u>	<u>624,628</u>

The Company's auditors, Grant Thornton have not issued any qualified or modified opinion on the Group's financial statements for the three financial years ended 31 December 2009.

**AUDITED FINANCIAL STATEMENTS OF THE GROUP FOR THE TWO YEARS ENDED
31 DECEMBER 2009**

Please refer to the 2009 annual report of the Company as set out (i) on the website of the Stock Exchange (www.hkexnews.hk/listedco/listconews/sehk/20100516/LTN20100516025.pdf); and (ii) the Company's website at http://www.irasia.com/listco/hk/xianyuen/annual/ar57178-ew_00353ar_24052010.pdf for details of the audited financial statements of the Group for the year ended 31 December 2009.

The following is the management discussion and analysis of the Group's financial conditions and results of operations for each of the three years ended 31 December 2009.

FOR THE YEAR ENDED 31 DECEMBER 2007**Results**

The Group's turnover for the year ended 31 December 2007 was approximately HK\$55.6 million, which represented an increase of 110% compared to the previous year. The administrative expenses for the year ended 31 December 2007 were approximately HK\$50 million, which represented an increase of 29% compared to the expenses incurred in 2006. The consolidated loss attributable to equity holders of the Company for the year ended 31 December 2007 was increased to approximately HK\$79 million, as compared to HK\$46 million in the previous corresponding year.

Business Review

During the year of 2007, carpet manufacturing and trading were the core business of the Group. However, while the turnover of the core business was substantially increased, the Group suffered a loss of HK\$37.8 million in manufacturing and trading of carpet segments which include the deficits on revaluation of property, plant and equipment of HK\$27 million. The loss of HK\$10.8 million, excluding the deficits on revaluation of property, plant and equipment, was mainly due to the low profit margin of our goods as we faced very keen pricing competition in Hong Kong, PRC and overseas.

The Directors therefore considered that the disposal of part of the carpet manufacturing and trading business would allow the Group to focus on and to spare additional resources to fund its investment in the mining business. For further details, please refer to the Company's circular dated 21 April 2008.

Material acquisitions and disposals

The acquisition of 70% interest of Win Alliance, which was completed in March 2007, enables the Group to expand its source of income from the trading of seamless steel and other goods. For the year ended 31 December 2007, the turnover of this segment of our business was HK\$15 million (2006: Nil) and the loss of this segment is HK\$813,000 (2006: Nil). The Group will endeavour to improve the gross profit of trading and further explore the customer base to contribute a profit in the future.

The acquisition of 51% interests of Da Sheng was completed in July 2007. The principal business of Da Sheng is to support PRC enterprises by acting as the guarantor of the enterprise, and by providing guarantees to financial institutions to secure credit facilities to the enterprise, thereby allowing the enterprise to obtain additional credit limit. The business of Da Sheng has not yet been commenced and it is anticipated that further time and capital is required for developing the logistics and financial business of Da Sheng. During the year, Aurora Logistic Finance Group Inc. (“Aurora Logistic Finance”) and its subsidiaries including Da Sheng recorded a loss of HK\$5.1 million. The Directors considered that the disposal of partial interest in Da Sheng would allow the Company to focus on and to spare additional resources to fund its investments in the mining business. For further details, please refer to the Company’s circular dated 21 April 2008.

In November 2007, the Group acquired 51% equity interests of Kanson Development Limited (“Kanson”) from Ms. Leung Lai Ching, Margaret, through Smooth Way International Limited (“Smooth Way”), a wholly-owned subsidiary of the Company. Qinghai Forest Source Mining Industry Developing Company Limited (Kanson’s wholly-owned subsidiary), a wholly foreign owned enterprise established in the PRC, holds an exploration license of a mineral property in 2 km by 1 km rectangular area of Little Red Mountain located in Inner Mongolia (the “Mine”). The relevant key metallurgical tests on the samples from the Mine have been completed by the Changsha Research Institute of Mining and Metallurgy, the Changsha Central South University and the Sichuan University that are all leading testing facilities and institutes in the PRC with specialized expertise in the beneficiation processes of iron, titanium and phosphate products from ore rock. The test results have been reviewed by an external panel of PRC experts in the relevant fields and were considered to be appropriate and sufficient for use in the feasibility studies of the project. An additional diamond drilling program has been carried out at the Mine and the relevant geological report is being compiled. The feasibility study report which is required for the application of the mining license for the Mine is under preparation. Support letters for the provision of water, power and land for the mining development at the Little Red Mountain mine site (Inner Mongolia) and at the processing plant site at Yumen (Gansu) have been provided by the local government. Temporary site offices have been set up at the Little Red Mountain mine site.

Future plans and prospectus

The Board is encouraged by the continuing increase in the global demands for iron and titanium products. According to a summary report on the International Titanium Association (ITA) 23rd Annual Meeting and Conference, the overall demand for the use of titanium in all segments of the industry is expected to grow from 80,000 tonnes in 2006 to 107,000 tonnes in 2010, increasing by 34%. Strong global demands for iron ore come from Asia, particularly China. This has resulted in a significant world-wide price increase of iron ore. According to the information obtained from Chinaccm.com, in 2007, China has imported around 0.38 billion tonnes of iron ore which amounted to about 50% of its annual demand. Also, the Chinese government has continued to encourage the development of iron ore mines and the beneficiation of iron and associated products, resulting in a steady upward trend in the pricing of iron and titanium products in the domestic market in the PRC. Therefore, the Board is optimistic about the Company’s mining business.

The Company will dedicate more resources to the exploration and development of the Mine at Little Red Mountain, such as registration of the mineral resources, delineation of the approved mining area, project feasibility study and application of the mining license. It is anticipated that the above work will be completed within the third quarter of 2008. Upon acquisition of the mining license, detailed design and development work could commence. Apart from the future business plan as discussed above, the Company will continue to put efforts on the aspects of operational improvement and cost-effectiveness enhancement in order to achieve higher returns to Shareholders.

Segmental information

Business Segments for the year ended 31 December 2007

	Manufacturing of carpets <i>HK\$'000</i>	Trading of carpets <i>HK\$'000</i>	Exploration of mine <i>HK\$'000</i>	Trading of goods <i>HK\$'000</i>	Consolidated <i>HK\$'000</i>
Segment revenue:					
Sales to external customers	11,745	28,851	–	15,051	55,647
Segment results	(35,565)	(2,215)	(14,273)	(1,567)	(53,620)
Unallocated other operating income					2,611
Other unallocated expense					(24,317)
Finance costs					(3,235)
Loss before income tax					(78,561)
Income tax expense					–
Loss for the year					(78,561)
Segment assets	40,881	7,278	695,034	29,086	772,279
Unallocated assets	–	–	–	–	97,909
Total assets	40,881	7,278	695,034	29,086	870,188
Segment liabilities	15,760	22,556	147,382	13,569	199,267
Unallocated liabilities	–	–	–	–	46,293
Total liabilities	15,760	22,556	147,382	13,569	245,560
Amortisation of prepaid lease payments	119	–	–	180	299
Depreciation	6,406	173	144	136	6,859
Unallocated depreciation	–	–	–	–	1,542
	6,406	173	144	136	8,401

APPENDIX IV

MANAGEMENT DISCUSSION AND ANALYSIS OF THE GROUP

	Manufacturing of carpets <i>HK\$'000</i>	Trading of carpets <i>HK\$'000</i>	Exploration of mine <i>HK\$'000</i>	Trading of goods <i>HK\$'000</i>	Consolidated <i>HK\$'000</i>
Capital expenditure					
Property, plant and equipment	30	24	9	–	63
Unallocated capital expenditure	–	–	–	–	5,113
	<u>30</u>	<u>24</u>	<u>9</u>	<u>–</u>	<u>5,176</u>
Exploration and evaluation assets	–	–	8,572	–	8,572
Non cash expense					
Write-down of inventories to net realisable value	458	–	–	–	458
Provision for impairment loss of trade and other receivables	868	620	–	–	1,488
Deficits on revaluation of property, plant and equipment	26,976	–	–	–	26,976
Impairment loss of goodwill	–	–	–	754	754
Unallocated impairment loss of goodwill	–	–	–	–	327
	<u>–</u>	<u>–</u>	<u>–</u>	<u>754</u>	<u>1,081</u>
Unallocated gain on disposal of a subsidiary	–	–	–	–	281

Geographic Segments for the year ended 31 December 2007

	Hong Kong HK\$'000	Macau HK\$'000	PRC HK\$'000	Malaysia HK\$'000	USA HK\$'000	Japan HK\$'000	France HK\$'000	Consolidated HK\$'000
Segment revenue								
Sales to external customers	12,830	440	20,525	795	6,005	673	14,379	55,647
Segment assets	700,880	–	169,308	–	–	–	–	870,188
Capital expenditure								
Property, plant and equipment	5,137	–	39	–	–	–	–	5,176
Exploration and evaluation assets	–	–	8,572	–	–	–	–	8,572
	5,137	–	8,611	–	–	–	–	13,748

Financial resources, capital structure, gearing ratio and liquidity

The Group financed its operations through a combination of funds generated from operations, placement and issue of Shares upon exercise of Share options of the Company.

As at 31 December 2007, the Group has total assets of approximately HK\$870 million (2006: HK\$101 million), total liabilities of HK\$246 million (2006: HK\$38 million), indicating a gearing ratio 0.28 (2006: 0.37) on the basis of total liabilities over total assets. As at 31 December, 2007, the Group had cash and cash equivalents of HK\$50,725,000. The current ratio of the Group for the year was 2.47 (2006: 0.49).

Charges on Assets

As at 31 December 2007, the Group had no interest-bearing bank borrowings and assets were pledged (2006: Nil).

Contingent Liabilities

As at 31 December 2007, the Group did not have any significant contingent liabilities (2006: Nil).

Employee Information

As at 31 December 2007, the Group employed approximately 191 full-time employees (2006: 139), mostly at the Group's subsidiary factories for manufacturing carpets. The staff costs, including the directors' emoluments were approximately HK\$19,495,000 during the year. The Group's emolument policies are formulated on the performance of individual employees and are reviewed annually in line with industry practice. The Group also provides provident fund schemes (as the case may be) to its employees depending on the location of such employees.

Dividend

The Directors do not recommend the payment of any dividend for the year ended 31 December 2007 (2006: Nil).

Foreign currency exposure

As a significant portion of the Group's sales and purchases were denominated in Hong Kong dollars and Renminbi, the directors considered the Group has no significant exposure to foreign exchange fluctuations in view of the stability of the exchange rates of Hong Kong dollars and Renminbi. During the year under review, the Group did not use any hedging instrument.

FOR THE YEAR ENDED 31 DECEMBER 2008**Results**

The Group's turnover for the year ended 31 December 2008 was approximately HK\$12.8 million. The administrative expenses for the year ended 31 December 2008 were approximately HK\$40 million, which represented a decrease of 11% compared to the expenses incurred last year. The loss attributable to equity holders of the Company for the year ended 31 December 2008 was increased to approximately HK\$341 million, as compared to HK\$79 million in the previous corresponding year. The loss was mainly resulted from the recognition of (i) non-cash imputed interest of approximately HK\$21.9 million; (ii) loss on discontinued operations of approximately HK\$29.7 million and (iii) impairment loss of goodwill of approximately HK\$253 million.

Business Review

For the year ended 31 December 2008, the Group recorded revenue from its continuing operations of approximately HK\$12.8 million (2007: HK\$28.9 million (restated)) and net loss from its continuing operations of approximately HK\$319 million (2007: HK\$41 million (restated)). The operating loss of the Group from its continuing operations was substantially increased by approximately HK\$258 million as compared to last year which included the impairment loss of goodwill of HK\$253 million and the loss of HK\$11.0 million on deemed disposal of Aurora Logistic Finance, Da Sheng and its subsidiaries. Moreover, the discontinued operations of carpet manufacturing and trading of goods incurred losses of HK\$15.5 million and HK\$14.2 million respectively.

During the year of 2008, there was a rise in manufacturing costs of products and an intense market competition on global products market. As a result, the Group recorded a net loss of its business. Furthermore, as the carpet manufacturing and some of carpet trading subsidiaries had been suffering loss for few years, the Group decided to dispose these subsidiaries to reduce the operating loss. The Group will still focus on carpet trading through a new wholly-owned subsidiary in coming years.

Material acquisitions and disposals

On 16 January 2008, the Company has entered into a non-binding memorandum of understanding with an independent third party to dispose of Orient Carpet Manufacturing (HK) Limited and Hui Zhou Orient Carpet Manufacturing Company Limited. Please refer to the announcement of the Company dated 16 January 2008 for further information.

On 10 March 2008, the Company has entered into a share sale agreement with an independent third party to dispose of International Carpet Company Limited for a total consideration of HK\$200,000. For details, please refer to the circular of the Company dated 21 April 2008.

In May 2008, the Group disposed 80.4% interest of Aurora Logistic Finance, which included the interest of Da Sheng. The Directors considered that the disposal of partial interest in logistics and financial business would allow resources relocation to enhance the efficiency in a more potential project in the mining sector. The Board will depend on the return of such investment to determine whether the Group will maintain the remaining 19.6% interest of Aurora Logistic Finance and review the performance and results of Da Sheng from time to time. Details of disposed interest in Aurora Logistic Finance is set out in the notes to the financial statements of 2008 Annual Report.

In July 2008, the Group acquired an additional 49% equity interests of Kanson from Ms. Leung Lai Ching, Margaret through Smooth Way. After the completion, Kanson is currently a wholly-owned subsidiary of the Company which indirectly holds an exploration license of a mineral property in 2 km by 1 km rectangular area of Little Red Mountain located in Inner Mongolia ("Xiao Hong Shan Project"). Current status of Xiao Hong Shan Project Application for the registration of the mineral resources of Xiao Hong Shan Project has been submitted to the Ministry of Land and Resources of the PRC. The application has been preliminarily approved pending some revisions to the supporting documents and the issuance of the official approval document regarding the actual quantity of resources. Given the global financial turmoil and the drastic decline in global commodity prices, the Company has decided to slow down the integrated utilization plan and the license application for the Xiao Hong Shan Project until further funding is secured.

As a result of world-wide commodities price has been decreased during the second half year of 2008, the valuation of the Mine – first portion in Xiao Hong Shan Project recorded a substantially decrease at the year end. The Group would impair the goodwill of Xiao Hong Shan Project and reflects the impairment loss in the financial statement.

Future Plan and Prospects

The recent significant price decline of global commodities will have negative impacts on the realisable selling price of titanium, iron and other products of Xiao Hong Shan Project while infrastructure costs and mineral resources tax payable to the Ministry of Land Management will remain largely unchanged. This puts more pressure on the near term cash requirement. The current global financial turmoil limits the ways of fund raising. Even though most of the relevant exploration tests for the reserves of Xiao Hong Shan Project have approached the final stage, the Company believes it is financially prudent to slow down the progress of the project until the Company secures new funds to meet the future funding requirement of the project.

Segmental information***Business Segments for the year ended 31 December 2008***

	Continuing operations		Discontinued operations		
	Exploration of mine HK\$'000	Trading of carpets HK\$'000	Manufacturing of carpets HK\$'000	Trading of goods HK\$'000	Consolidated HK\$'000
Segment revenue:					
Sales to external customers	–	12,846	6,418	–	19,264
Segment results	(266,235)	(9,896)	(15,465)	(14,200)	(305,796)
Unallocated other operating income					7,352
Other unallocated expense					(27,517)
Finance costs					(22,521)
Loss before income tax					(348,482)
Income tax expense					–
Loss for the year					(348,482)
Segment assets	774,902	1,275	35,341	14,928	826,446
Unallocated assets	–	–	–	–	14,151
Total assets	774,902	1,275	35,341	14,928	840,597
Segment liabilities	199,629	8,643	27,883	13,610	249,765
Unallocated liabilities	–	–	–	–	7,053
Total liabilities	199,629	8,643	27,883	13,610	256,818

APPENDIX IV

MANAGEMENT DISCUSSION AND ANALYSIS OF THE GROUP

	Continuing operations		Discontinued operations		
	Exploration of mine <i>HK\$'000</i>	Trading of carpets <i>HK\$'000</i>	Manufacturing of carpets <i>HK\$'000</i>	Trading of goods <i>HK\$'000</i>	Consolidated <i>HK\$'000</i>
Amortisation of prepaid lease payments	–	–	64	180	244
Depreciation	937	50	1,068	117	2,172
Unallocated depreciation	–	–	–	–	1,277
	<u>937</u>	<u>50</u>	<u>1,068</u>	<u>117</u>	<u>3,449</u>
Capital expenditure					
Property, plant and equipment	1,030	61	153	–	1,244
Unallocated capital expenditure	–	–	–	–	85
	<u>1,030</u>	<u>61</u>	<u>153</u>	<u>–</u>	<u>1,329</u>
Additions to exploration and evaluation assets	6,566	–	–	–	6,566
Non cash expense					
Bad debts written off	–	–	–	11,720	11,720
Unallocated loss on deemed disposals of subsidiaries	–	–	–	–	11,027
Assets in disposal group classified as held for sale – loss on re-measurement to fair value less costs to sell	1,730	–	11,540	2,140	15,410
Impairment loss of goodwill	253,030	–	–	–	253,030
Gain on disposal of a subsidiary	–	5,438	–	–	5,438
Unallocated gain on disposal of a subsidiary	–	–	–	–	842
	<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>842</u>

Geographic Segments for the year ended 31 December 2008

	Hong Kong HK\$'000	Macau HK\$'000	PRC HK\$'000	USA HK\$'000	Consolidated HK\$'000
Segment revenue					
Sales to external customers					
– continuing operations	7,810	135	3,117	1,784	12,846
– discontinued operations	–	–	6,418	–	6,418
	<u>7,810</u>	<u>135</u>	<u>9,535</u>	<u>1,784</u>	<u>19,264</u>
Segment assets	<u>729,897</u>	<u>–</u>	<u>110,700</u>	<u>–</u>	<u>840,597</u>
Capital expenditure					
Property, plant and equipment	134	–	1,195	–	1,329
Exploration and evaluation assets	–	–	6,566	–	6,566
	<u>134</u>	<u>–</u>	<u>7,761</u>	<u>–</u>	<u>7,895</u>

Financial resources, capital structure, gearing ratio and liquidity

The Group financed its operations through funds generated from operations the proceeds from the placements in 2007.

As at 31 December 2008, the Group has total assets of approximately HK\$841 million (2007: HK\$870 million), total liabilities of approximately HK\$257 million (2007: HK\$246 million), indicating a gearing ratio 0.31 (2007: 0.28) on the basis of total liabilities over total assets. As at 31 December 2008, the Group had cash and cash equivalents of HK\$881,000. The current ratio of the Group for the year was 1.46 (2007: 2.47).

Charges on Assets

As at 31 December 2008, the Group had no interest-bearing bank borrowings and assets which was pledged (2007: Nil).

Contingent Liabilities

As at 31 December 2008, the Group did not have any significant contingent liabilities (2007: Nil).

Employee Information

As at 31 December 2008, the Group employed approximately 165 full-time employees (2007: 191), mostly at the Group's subsidiary factory for manufacturing carpet. The staff costs, including Directors' emoluments were approximately HK\$22,307,000 during the year. The Group's emolument policies are formulated on the performance of individual employees and are reviewed annually in line with industry practice. The Group also provides provident fund schemes (as the case may be) to its employees depending on the location of such employees.

Dividend

The Directors do not recommend the payment of any dividend for the year ended 31 December 2008 (2007: Nil).

Foreign currency exposure

As a significant portion of the Group's sales and purchases were denominated in Hong Kong dollars and Renminbi, the Directors considered the Group has no significant exposure to foreign exchange fluctuations in view of the stability of the exchange rates of Hong Kong dollars and Renminbi. During the year under review, the Group did not use any hedging instrument.

FOR THE YEAR ENDED 31 DECEMBER 2009**Results**

The Group's turnover for the year ended 31 December 2009 was approximately HK\$10.3 million. The administrative expenses for the year ended 31 December 2009 were approximately HK\$25 million, which represented a decrease of 37.3% compared to the administrative expenses incurred last year. The loss attributable to the owners of the Company for the year ended 31 December 2009 was increased to approximately HK\$432 million, as compared to HK\$341 million in the previous corresponding year. The loss was mainly resulted from the recognition of (i) non-cash imputed interest of approximately HK\$6.4 million; (ii) impairment loss of other receivable of approximately HK\$31 million and (iii) impairment loss of goodwill of approximately HK\$368 million.

Business review

For the year ended 31 December 2009, the Group recorded revenue from its continuing operations of approximately HK\$10.3 million (2008: HK\$12.8 million) and net loss from its continuing operations was approximately HK\$441 million (2008: HK\$319 million). The loss before income tax of the Group from its continuing operations was substantially increased by approximately HK\$122 million as compared to last year which included the impairment of goodwill of HK\$368 million and impairment of other receivable of HK\$31 million. Moreover, the discontinued operations recorded gain of HK\$8.3 million (2008: loss of HK\$30 million).

Carpet trading

Turnover of the carpet trading operation decreased by 19.6%, or HK\$2.5 million, to HK\$10.3 million in 2009, which was attributable to the global economic downturn and intense market competition and incurred a loss HK\$1.6 million in carpets trading business. The Group will take more effort to source more orders from both new and existing customers to improve the results.

Exploration and mining business

Regarding the Xiao Hong Shan project, the Group is still in the process of preparing for the application for the mining license of the mineral resources of the titanium mine. The Group is currently preparing the feasibility report and the integrated utilisation plan, and the application for the approval of the delineation of the mining zone. Upon receipt of the approval of the delineation of the mining plan, and subject to review of the status reports and other relevant information on the titanium mine to be provided by Qinghai Forest Source Mining Industry Developing Company Limited with reference to the expected amount of return on investment and economic benefit of the project, the Company will consider whether the application of the mining license of the mineral resources in the titanium mine should be. It is expected that certain amount of work will still need to be completed before the mining license will be issued.

Material acquisitions and disposals**(i) Oil and gas business**

On 25 September 2009, Cheerful Dragon Limited, a wholly owned subsidiary of the Company, entered into a conditional agreement with Greater Finance Limited (“**Greater Finance**”), pursuant to which Cheerful Dragon Limited has agreed to purchase and Greater Finance has agreed to sell the entire issued share capital of China International Energy Investments (Hong Kong) Limited (“**China International Energy**”) at an aggregate consideration of HK\$1,500 million (subject to the adjustment). The principal asset in China International Energy and its subsidiaries is its participating interest in Target Oil Field pursuant to the Cooperation Contract with China National Petroleum Corporation (“**CNPC**”). The details of the proposed acquisition are set out in the Company’s announcement dated 22 October 2009.

The Company takes initiative in identifying investment opportunities that will broaden its revenue sources. The acquisition represents a good opportunity for the Company to diversify its business into the Petroleum Businesses in cooperation with CNPC, one of the leading state-owned petroleum enterprise in the PRC. With the anticipated continued growth of the PRC economy which will fuel the demand for oil as basis of the acquisition cost, the Board believes that the oil business under the proposed acquisition is beneficial to the Group’s profile.

(ii) Electricity and heat business

On 5 November 2009, Precious New Limited, a wholly owned subsidiary of the Company, entered into a conditional agreement with Maycrown Capital Limited (“**Maycrown Capital**”), pursuant to which Precious New Limited has agreed to purchase and Maycrown Capital has agreed to sell the entire issued share capital of Sunlight Rise Limited (“**Sunlight Rise**”) at an aggregate consideration of HK\$350.86 million (subject to the adjustment) and assume the obligation to contribute to and pay up the remaining balance of the registered capital of Shanxi Zhong Kai Group Lingshi Heat & Power Company Limited (山西中凱集團靈石熱電有限公司) (“**Shanxi Zhong Kai**”) in the sum of approximately RMB69.55 million. The principal asset in Sunlight Rise and its subsidiaries is owned 60% equity interest in Shanxi Zhong Kai. The details of the proposed acquisition are set out in the Company’s announcement dated 23 November 2009. As at the date of 2009 annual report, the proposed acquisition is still not yet completed and the Company is still finalising the information to be included in the circular.

The Company intends to expand its existing business to generating and supplying electricity and heat by using coke oven gas in the PRC, which, the Directors believed has ample growth opportunities due to the increased demand for electricity caused by the continued growth of the PRC economy. The use of coke oven gas to create electricity and heat can not only help to reduce this hazardous gas, but it also benefits the environment. In addition, coke oven gas is of lower cost when compared with other fuel such as natural gas or heavy oil. The Board considered that the acquisition represents an opportunity for the Group to enter into the power generation industry, and believed that the Group could broaden its source of income by vertically diversifying into such industry.

Future Plan and Prospects

The year of 2010 will still be a year with great challenges. However, the Board believes that whenever there is a crisis, there is an opportunity. In the future, the Group will strive to combat the adverse impact arising from the financial crisis, and will adjust its business strategies to meet the changes of economic environment. It will also seek to capture any favorable opportunities for prudent investment in order to ensure a continuous, stable and healthy growth, and generate greater value for the shareholders.

Segment information

Business Segments for the year ended 31 December 2009

	Exploration of mine 2009 HK\$'000	Trading of carpets 2009 HK\$'000	Consolidated 2009 HK\$'000
Reportable segment revenue:			
From external customers	–	10,332	10,332
Reportable segment loss	(406,344)	(1,571)	(407,915)
Bank interest income	1	–	1
Depreciation	811	–	811
Impairment loss on goodwill	368,401	–	368,401
Provision for impairment loss of other receivables	30,965	–	30,965
Gain on disposals of subsidiaries	668	33	701
Reportable segment assets	369,990	958	370,948
Additions to non-current segment assets during the year	4,497	–	4,497
Reportable segment liabilities	39,220	51	39,271

Geographic Segment for the year ended 31 December 2009

	Hong Kong (Domicile) 2009 HK\$'000	PRC 2009 HK\$'000	Consolidated 2009 HK\$'000
Reportable segment revenue:			
From external customers	10,332	–	10,332
Non-current assets	185,027	369,772	554,799

Financial resources, capital structure, gearing and liquidity

The Group financed its operations through funds generated from the fund raising exercises as mentioned below.

(i) **Placement of Shares**

A placement agreement dated 6 August 2009 and supplemental agreement dated 10 August 2009 made between the Company and Mayfair Securities Limited (“**Mayfair Securities**”) as placing agent, pursuant to which an aggregate of 809,280,000 new ordinary shares were placed by Mayfair Securities on behalf of the Company, at the price of HK\$0.137 per placing share with the independent investors. After the completion of the placing, the Company issued 809,280,000 new ordinary shares at HK\$0.137 per share on 20 August 2009. Net proceeds from the placing was approximately of HK\$108.1 million.

(ii) **Open Offer of Shares**

A conditional underwriting agreement dated 25 August 2009 entered into between Kingston Securities Limited (“**Kingston Securities**”) as the underwriter and the Company, in relation to the open offer of 2,452,500,000 offer shares at the subscription price of HK\$0.08 per offer share on the basis of one offer share for every two shares held on 15 September 2009. The subscription was completed on 5 October 2009 and the net proceeds from the open offer was approximately of HK\$191.9 million.

Deposits for the proposed acquisitions

As at 31 December 2009, a refundable deposit of HK\$150 million was paid to Greater Finance by the Company. Details of the acquisition of the China International Energy are set out in the Company’s announcement dated on 22 October 2009.

As at 31 December 2009, a refundable deposit of HK\$35 million was paid to the Vendor by the Company. Details of the Acquisition are set out in the letter from the Board in this circular.

As at 31 December 2009, the Group had total assets of approximately HK\$670 million (2008: HK\$841 million), total liabilities of HK\$42 million (2008: HK\$257 million), indicating a gearing ratio 0.06 (2008: 0.31) on the basis of total liabilities over total assets. The current ratio of the Group for the year was 5.09 (2008: 1.46).

Charges on assets

As at 31 December 2009, the Group had no interest-bearing bank borrowings and assets pledged (2008: Nil).

Contingent liabilities

As at 31 December 2009, the Group did not have any significant contingent liabilities (2008: Nil).

Employee information

As at 31 December 2009, the Group employed approximately 31 full-time employees (2008: 165). The substantial drop in number of employees is mainly due to the discontinued operations which were disposed in 2009. The Group's emolument policies are formulated on the performance of individual employees and are reviewed annually in line with industry practice. The Group also provides provident fund schemes (as the case may be) to its employees depending on the location of such employees.

Dividend

The Directors do not recommend the payment of any dividend for the year ended 31 December 2009 (2008: Nil).

Foreign currency exposure

As a significant portion of the Group's sales and purchases were denominated in Hong Kong dollars and Renminbi, the Directors considered the Group has no significant exposure to foreign exchange fluctuations in view of the stability of the exchange rates of Hong Kong dollars and Renminbi. During the year under review, the Group did not use any hedging instrument.

A. UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP**1. Introduction**

The following unaudited pro forma consolidated statement of financial position, unaudited pro forma consolidated income statement and unaudited pro forma consolidated statement of cash flows of the Enlarged Group (the “Unaudited Pro Forma Financial Information”) have been prepared by the directors of the Company in accordance with Rule 4.29 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”) and on the basis of the notes set out below for the purpose of illustrating the effect of the Acquisition on the financial position of the Group as at 31 December 2009 and the results and cash flows of the Group for the year ended 31 December 2009.

The unaudited pro forma consolidated statement of financial position of the Enlarged Group is prepared, in accordance with the accounting policies of the Group under Hong Kong Financial Reporting Standards (“HKFRS”), based on the audited consolidated statement of financial position of the Group as at 31 December 2009 extracted from the published annual report of the Group for the year ended 31 December 2009 as set out in Appendix III to this circular and the audited statements of financial position of each of the Target Group (as defined in Note (a)) (where one of the Target Group’s subsidiary, the Project Company, only was not consolidated) and the Project Company as at 31 December 2009 as extracted from the accountants’ reports set out in Appendices I to II to this circular (translated into HK\$ at exchange rate of HK\$1 = RMB0.88) as if the Acquisition had been completed on 31 December 2009.

The unaudited pro forma consolidated income statement and the unaudited pro forma consolidated statement of cash flows of the Enlarged Group are prepared, in accordance with the accounting policies of the Group under HKFRS, based on the audited consolidated income statement and the audited consolidated statement of cash flows of the Group for the year ended 31 December 2009 extracted from the published annual report of the Group for the year ended 31 December 2009 as set out in Appendix III to this circular and the audited statements of comprehensive income and the audited statements of cash flows of each of the Target Group (where one of the Target Group’s subsidiary, the Project Company only was not consolidated) for the period from 20 October 2009 (date of incorporation) to 31 December 2009 and the Project Company for the year ended 31 December 2009 as extracted from the accountants’ reports set out in Appendices I to II to this circular (translated into HK\$ at exchange rate of HK\$1 = RMB0.88) as if the Acquisition had been completed on 1 January 2009 and the Project Company had become a subsidiary of the Target Group since 1 January 2009.

The Unaudited Pro Forma Financial Information is based on the aforesaid historical data after giving effect to the pro forma adjustments described in the accompanying notes. A narrative description of the pro forma adjustments of the Acquisition that are (i) directly attributable to the transactions; and (ii) factually supportable, is summarised in the accompanying notes.

The accompanying Unaudited Pro Forma Financial Information has been prepared by the directors of the Company for illustrative purpose only and is based on certain assumptions, estimates, uncertainties and other currently available information. Accordingly, and because of its nature, the Unaudited Pro Forma Financial Information may not give a true picture of the financial position, results and cash flows of the Enlarged Group following the completion of the Acquisition. Further, the Unaudited Pro Forma Financial Information of the Enlarged Group does not purport to predict the Enlarged Group’s future financial position, results of operations and cash flows.

APPENDIX V

UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

2. Unaudited pro forma consolidated statement of financial position of the enlarged group

	As at 31 December 2009					
	The Group (Audited) HK\$'000	The Target Group* (Audited) HK\$'000	The Project Company (Audited) HK\$'000	Pro forma adjustments (Unaudited) HK\$'000	Notes	Pro forma Enlarged Group (Unaudited) HK\$'000
ASSETS AND LIABILITIES						
Non-current assets						
Property, plant and equipment	3,605	–	271,861			275,466
Prepaid land lease payments	–	–	29,093			29,093
Goodwill	327,632	–	–	253,683	(b)	581,315
Investment in subsidiaries	–	35,000	–	(35,000)	(f)	–
Deposits for acquisitions of subsidiaries	185,000	–	–	(35,000)	(b)(i)	150,000
Intangible assets	–	–	–	52,148	(d)	52,148
Exploration and evaluation assets	38,562	–	–			38,562
Deferred tax assets	–	–	2,200			2,200
	<u>554,799</u>	<u>35,000</u>	<u>303,154</u>			<u>1,128,784</u>
Current assets						
Inventories	–	–	2,788			2,788
Trade receivables	–	–	10,765			10,765
Prepayments, deposits and other receivables	1,393	–	12,531	25,724	(i)	39,648
Amounts due from a shareholder	–	–	6,250	(6,250)	(i)	–
Amounts due from a related company	–	–	25,724	(25,724)	(i)	–
Amounts due from non-controlling investor of a subsidiary	–	–	–	6,250	(i)	6,250
Cash at banks and in hand	<u>113,382</u>	<u>6</u>	<u>36,497</u>	<u>(35,000)</u>	<u>(b)(i)</u>	<u>114,885</u>
	<u>114,775</u>	<u>6</u>	<u>94,555</u>			<u>174,336</u>
Current liabilities						
Trade payables	–	–	14,708			14,708
Deposits received, other payables and accruals	22,559	48	53,738	1,211	(i)	77,556
Amounts due to related companies	–	–	1,211	(1,211)	(i)	–
Amounts due to a director	–	12	–	(12)	(c)	–
Amounts due to ultimate holding company	–	35,000	–	(35,000)	(c)	–
Bank loans	–	–	23,750			23,750
Tax payables	–	–	21,784			21,784
	<u>22,559</u>	<u>35,060</u>	<u>115,191</u>			<u>137,798</u>
Net current assets/ (liabilities)	<u>92,216</u>	<u>(35,054)</u>	<u>(20,636)</u>			<u>36,538</u>
Total assets less current liabilities	<u>647,015</u>	<u>(54)</u>	<u>282,518</u>			<u>1,165,322</u>

APPENDIX V

UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

As at 31 December 2009						
	The Group (Audited) HK\$'000	The Target Group* (Audited) HK\$'000	The Project Company (Audited) HK\$'000	Pro forma adjustments (Unaudited) HK\$'000	Notes	Pro forma Enlarged Group (Unaudited) HK\$'000
Non-current liabilities						
Convertible bonds	19,279	–	–			19,279
Bank loans	–	–	22,727			22,727
Loan from a related company	–	–	7,178	(7,178)	(i)	–
Loan from a shareholder (former ultimate holding company)	–	–	54,428	(54,428)	(i)	–
Loan from a company related to non-controlling investor of a subsidiary	–	–	–	7,178	(i)	7,178
Loan from non-controlling investor of a subsidiary	–	–	–	54,428	(i)	54,428
Deferred tax liabilities	–	–	–	13,037	(d)	13,037
	<u>19,279</u>	<u>–</u>	<u>84,333</u>			<u>116,649</u>
Net assets/(liabilities)	<u>627,736</u>	<u>(54)</u>	<u>198,185</u>			<u>1,048,673</u>
EQUITY						
Share capital	73,610	–	131,592	15,100 (131,592)	(b)(ii) (e),(f)	88,710
Reserves	554,126	(54)	66,593	163,080 147,839 (101,551) 35,012	(b)(ii) (b)(iii) (k) (c)	865,045
	<u>554,126</u>	<u>(54)</u>	<u>66,593</u>			<u>865,045</u>
Equity/(Capital deficiencies) attributable to owners of the Company	<u>627,736</u>	<u>(54)</u>	<u>198,185</u>			<u>953,755</u>
Non-controlling interests	–	–	–	94,918	(e)	94,918
Total equity/(Capital deficiencies)	<u>627,736</u>	<u>(54)</u>	<u>198,185</u>			<u>1,048,673</u>

* where the Project Company only was not consolidated

APPENDIX V

UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

3. Unaudited pro forma consolidated income statement of the enlarged group

	The Group For the year ended 31 December 2009 (Audited) HK\$'000	The Target Group* For the period from 20 October 2009 to 31 December 2009 (Audited) HK\$'000	The Project Company For the year ended 31 December 2009 (Audited) HK\$'000	Pro forma adjustments (Unaudited) HK\$'000	Notes	Pro forma Enlarged Group (Unaudited) HK\$'000
Continuing operations:						
Revenue	10,332	–	113,918			124,250
Cost of sales	(10,020)	–	(66,982)			(77,002)
Gross profit	312	–	46,936			47,248
Other income	2,515	–	31,401			33,916
Administrative expenses	(25,327)	(54)	(5,853)			(31,234)
Other operating expenses	(41,707)	–	(2,238)	(17,880)	(g)	(61,825)
Impairment loss recognised in respect of goodwill	(368,401)	–	–			(368,401)
Operating (loss)/profit	(432,608)	(54)	70,246			(380,296)
Finance costs	(7,920)	–	(5,608)			(13,528)
(Loss)/Profit before income tax	(440,528)	(54)	64,638			(393,824)
Income tax expense	–	–	(12,242)	4,470	(g)	(7,772)
(Loss)/Profit after income tax from continuing operations	(440,528)	(54)	52,396			(401,596)
Discontinued operations:						
Profit for the year from discontinued operations	8,341	–	–			8,341
(Loss)/Profit for the year	<u>(432,187)</u>	<u>(54)</u>	<u>52,396</u>			<u>(393,255)</u>
(Loss)/Profit for the year attributable to:						
Owners of the Company	(432,187)	(54)	31,438	(8,046)	(g)	(408,849)
Non-controlling interests	–	–	20,958	(5,364)	(g)	15,594
(Loss)/Profit for the year	<u>(432,187)</u>	<u>(54)</u>	<u>52,396</u>			<u>(393,255)</u>

* where the Project Company only was not consolidated

APPENDIX V

UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

4. Unaudited pro forma consolidated statement of cash flows of the enlarged group

	The Group For the year ended 31 December 2009 (Audited) HK\$'000	The Target Group* For the period from 20 October 2009 to 31 December 2009 (Audited) HK\$'000	The Project Company For the year ended 31 December 2009 (Audited) HK\$'000	Pro forma adjustments (Unaudited) HK\$'000	Notes	Pro forma Enlarged Group (Unaudited) HK\$'000
Cash flows from operating activities of continuing and discontinued operations						
(Loss)/Profit before income tax						
Continuing operations	(440,528)	(54)	64,638	(17,880)	(g)	(393,824)
Discontinued operations	8,341	—	—			8,341
	(432,187)	(54)	64,638			(385,483)
Adjustments for:						
Depreciation	1,021	—	10,718			11,739
Amortisation of prepaid land lease payments	—	—	633			633
Amortisation of intangible assets	—	—	—	17,880	(g)	17,880
Impairment loss of goodwill	368,401	—	—			368,401
Provision for impairment loss of other receivables	30,965	—	—			30,965
Gain on disposals of subsidiaries	(9,044)	—	—			(9,044)
Loss on disposals of subsidiaries	10,534	—	—			10,534
Loss/(Gain) on disposals of property, plant and equipment	10	—	(32)			(22)
Interest income	(1,787)	—	(9,317)			(11,104)
Interest expenses	7,920	—	5,375			13,295
Operating (loss)/profit before working capital changes	(24,167)	(54)	72,015			47,794
Increase in inventories	—	—	(1,485)			(1,485)
Decrease/(Increase) in trade receivables	43	—	(9,474)			(9,431)
Increase in prepayments, deposits and other receivables	(1,847)	—	(3,982)			(5,829)
Increase in trade payables	—	—	10,122			10,122
Increase in deposits received, other payables and accruals	6,463	48	2,828			9,339
Cash (used in)/generating from operations	(19,508)	(6)	70,024			50,510
Interest paid	(1,523)	—	(5,375)			(6,898)
Net cash (used in)/generated from operating activities	<u>(21,031)</u>	<u>(6)</u>	<u>64,649</u>			<u>43,612</u>

APPENDIX V

UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

	The Group For the year ended 31 December 2009 (Audited) HK\$'000	The Target Group* For the period from 20 October 2009 to 31 December 2009 (Audited) HK\$'000	The Project Company For the year ended 31 December 2009 (Audited) HK\$'000	Pro forma adjustments (Unaudited) HK\$'000	Notes	Pro forma Enlarged Group (Unaudited) HK\$'000
Cash flows from investing activities of continuing and discontinued operations						
Purchases of property, plant and equipment	(32)	–	(14,285)			(14,317)
Purchases of exploration and evaluation assets	(4,465)	–	–			(4,465)
Payments for the deposits for acquisitions of subsidiaries	(185,000)	–	–	35,000	(j)	(150,000)
Net cash inflow arising from disposals of subsidiaries	18,664	–	–			18,664
Capital injected to a subsidiary	–	(35,000)	–	35,000	(f)	–
Proceeds from disposals of property, plant and equipment	–	–	709			709
Acquisition of subsidiaries, net of cash and cash equivalents acquired	–	–	–	(68,077)	(j)	(68,077)
Interest received	1,787	–	6			1,793
Net cash used in investing activities	(169,046)	(35,000)	(13,570)			(215,693)

APPENDIX V

UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

	The Group For the year ended 31 December 2009 (Audited) HK\$'000	The Target Group* For the period from 20 October 2009 to 31 December 2009 (Audited) HK\$'000	The Project Company For the year ended 31 December 2009 (Audited) HK\$'000	Pro forma adjustments (Unaudited) HK\$'000	Notes	Pro forma Enlarged Group (Unaudited) HK\$'000
Cash flows from financing activities of continuing and discontinued operations						
Proceeds from issue of shares upon placement	110,872	–	–			110,872
Proceeds from issue of shares upon open offer	196,200	–	–			196,200
Repayments of other borrowings	(5,964)	–	–			(5,964)
Capital element of finance lease payments	(64)	–	–			(64)
Advances from a director	–	12	–	(12)	(i)	–
Decrease in amount due to a shareholder	–	–	(6,250)	6,250	(i)	–
Advances from ultimate holding company	–	35,000	–	(35,000)	(i)	–
Proceeds from capital injection	–	–	35,000	(35,000)	(f)	–
Decrease in amount due to former ultimate parent	–	–	(96,910)	96,910	(i)	–
Loan from a shareholder (former ultimate holding company)	–	–	62,623	(62,623)	(i)	–
Repayments of bank loans	–	–	(24,318)			(24,318)
Increase in amount due to related companies	–	–	3,878	(3,878)	(i)	–
Loan from a related company	–	–	8,295	(8,295)	(i)	–
Increase in amount due to fellow subsidiaries	–	–	2,086	(2,086)	(i)	–
Decrease in loans from related companies and fellow subsidiaries of non-controlling investor of a subsidiary	–	–	–	(5,525)	(i)	(5,525)
Increase in amount due to non-controlling investor of a subsidiary	–	–	–	14,259	(i)	14,259
Net cash generated from/(used in) financing activities	<u>301,044</u>	<u>35,012</u>	<u>(15,596)</u>			<u>285,460</u>
Net increase in cash and cash equivalents	110,967	6	35,483			113,379
Cash and cash equivalents at beginning of the year	2,387	–	1,923	(1,923)	(h)	2,387
Effect on foreign exchange rate changes	<u>28</u>	<u>–</u>	<u>(909)</u>			<u>(881)</u>
Cash and cash equivalents at end of the year	<u>113,382</u>	<u>6</u>	<u>36,497</u>			<u>114,885</u>
Analysis of balances of cash and cash equivalents						
Cash and bank balances of continuing operations	<u>113,382</u>	<u>6</u>	<u>36,497</u>	(35,000)	(j)	<u>114,885</u>

* where the Project Company only was not consolidated

Notes to unaudited pro forma financial information of the enlarged group

- (a) On 5 November 2009, a wholly-owned subsidiary of the Company entered into the acquisition agreement (the “Acquisition Agreement”) with the Vendor and the Warrantor to acquire the entire issued share capital of the Target Company (the “Acquisition”) at a total consideration of HK\$350,860,000 (the “Consideration”). The Consideration shall be satisfied in the following manners:

	<i>HK\$'000</i>
Cash consideration*	70,000
Upon Completion	
– Allotment and issuance of 1,510,000,000 Consideration Shares of the Company	140,430
– Issue of Convertible Notes	140,430
	<u>350,860</u>

* *The partial consideration settled by cash of HK\$35,000,000 was injected into the Project Company eventually and treated as loans from ultimate holding company. Then, this loan shall be capitalised immediately prior to the Completion (note c).*

Upon Completion, the Target Company and its subsidiaries, Ontop Finance Limited, Pride Treasure Limited and the Project Company (collectively referred to as the “Target Group”) are considered by the directors of the Company as subsidiaries of the Company as the Target Group will be controlled by the Group after Completion. The consolidated statements of financial positions of the Target Group will be consolidated into those of the Group from the date on which control is transferred to the Group, which is assumed to be the date of Completion.

- (b) The adjustments are to reflect the effect of the Acquisition on the unaudited pro forma consolidated statement of financial position of the Enlarged Group as if the Acquisition had been completed on 31 December 2009.

The fair value of the investment cost at completion of the Acquisition which is to be satisfied in the following manners:

	<i>Notes</i>	<i>HK\$'000</i>
Cash consideration	<i>(i)</i>	70,000
Upon Completion		
– Allotment and issuance of 1,510,000,000 Consideration Shares of the Company	<i>(ii)</i>	178,180
– Issue of Convertible Notes	<i>(iii)</i>	147,839
		<u>396,019</u>

- (i) In November 2009, the Group paid a deposit of HK\$35,000,000 to the Vendor. The remaining cash consideration of HK\$35,000,000 will be paid before the Completion.
- (ii) The fair value of HK\$0.118 per share for the Consideration Shares is for illustrative purpose only. As the par value of the Consideration Share is HK\$0.01 per share, the issue and allotment of 1,510,000,000 Consideration Shares at the fair value of HK\$0.118 per share as at 31 December 2009 for the unaudited pro forma consolidated statement of financial position purpose, credited as fully paid, result in the increase of share capital and share premium account by HK\$15,100,000 and HK\$163,080,000 respectively. The actual fair value will be based on the market price of the shares of the Company upon Completion which may be different from HK\$0.118 per share. Accordingly, the actual goodwill at the date of Completion may be different from the amount presented below.
- (iii) The adjustment represents the estimated fair value of the Convertible Notes issued for the Acquisition as if they were issued on 31 December 2009. The Company has no obligation to repay the principal amount of the Convertible Bonds or pay interest and therefore the whole amount of the Convertible Notes is classified as equity. The valuation of the Convertible Notes was carried out by LCH (Asia-Pacific) Surveyors Limited, a firm of independent professional qualified valuers, and the valuation date is on 31 December 2009. The fair value of the Convertible Notes of approximately HK\$147,839,000 is determined using income approach. On Completion, the fair value of the Convertible Notes will have to be reassessed as at the date of Completion.

Details of goodwill arising on the Acquisition as if the Acquisition was completed on 31 December 2009 are as follows:

	<i>HK\$'000</i>
Fair value of cost of investment at Completion	396,019
<i>Less:</i>	
Fair value of net identifiable assets of the Target Group (including the Project Company) to be acquired (<i>note</i>)	142,336
Goodwill	253,683

APPENDIX V**UNAUDITED PRO FORMA FINANCIAL
INFORMATION OF THE ENLARGED GROUP**

Note:

HK\$'000

Net identifiable liabilities of the Target Group (where the Project Company only was not consolidated) as extracted from the accountants' report set out in Appendix I)	(54)
Net identifiable assets of the Project Company as extracted from the accountants' report set out in Appendix II (translated into HK\$ at exchange rate of HK\$1 = RMB0.88)	198,185
Elimination of cost of investment in the Project Company made by the Target Group	(35,000)
Capitalisation of shareholder's loans immediately prior to the Completion (<i>note c</i>)	35,012
Fair value of the intangible assets, net of deferred tax (<i>note d</i>)	39,111
Non-controlling interests (<i>note e</i>)	(94,918)
	142,336

On Completion, the fair values of the cost of investment and the net identifiable assets to be acquired will have to be reassessed and accordingly, their fair values at the date of Completion will be different from those for the preparation of the Unaudited Pro Forma Financial Information. As a result, the amount of goodwill may be different from that estimation based on the basis, as stated above, used in the preparation of the Unaudited Pro Forma Financial Information. Accordingly, the actual goodwill at the date of Completion may be different from that presented above.

- (c) The adjustment represents the capitalisation of amounts due to a director/shareholder and ultimate holding company of the Target Group (including the Project Company) immediately prior to the Completion of the Acquisition. Prior to the Completion, the amounts due to a director/shareholder and ultimate holding company will be different from those for the preparation of the Unaudited Pro Forma Financial Information. As a result, the amount of capitalisation may be different from those amounts used in the preparation of the Unaudited Pro Forma Financial Information.
- (d) For the purpose of the unaudited pro forma consolidated statement of financial position, the adjustment represents the fair value of the sale contracts signed prior to the date of Completion. The valuation was carried out by LCH (Asia-Pacific) Surveyors Limited, a firm of independent professional qualified valuers, and the valuation date is on 31 December 2009. The fair value of the signed sales contracts is HK\$52,148,000. Deferred tax liability arising from this intangible asset is HK\$13,037,000 calculated based on income tax rate of 25% accordingly. As at 31 December 2009, the Project Company entered into 1 sales contract with a related company and 5 sales contracts with third parties.

APPENDIX V**UNAUDITED PRO FORMA FINANCIAL
INFORMATION OF THE ENLARGED GROUP**

- (e) The adjustment represents that the non-controlling interests which hold 40% equity interests in the Project Company.

As at 31 December 2009 *HK\$'000*

Net assets value of the Project Company as at 31 December 2009	198,185
Intangible assets, net of tax (<i>note d</i>)	39,111

	237,296
Non-controlling interests (40%)	94,918

As at 1 January 2009 *HK\$'000*

Net assets value of the Project Company as at 1 January 2009	111,699
Intangible assets, net of tax (<i>note g</i>)	23,455

	135,154
Non-controlling interests (40%)	54,062

- (f) The adjustment is to eliminate the capital contribution of HK\$35,000,000 from the Target Group to the Project Company.

- (g) As at 1 January 2009, the Project Company entered into 1 sales contract with a related company and 4 sales contracts with third parties. These signed sales contracts are treated as intangible asset in accordance with HKFRS 3. HKFRS 3 B31 provides that the acquirer shall recognise, separately from goodwill, the identifiable intangible assets acquired in a business combination. An intangible asset is identifiable if it meets either the separability criterion or the contractual-legal criterion. HKFRS 3 IE26 further provides that if an entity establishes relationships with its customers through contracts, those customer relationships arise from contractual rights. Therefore, customers contracts and the related customer relationships acquired in a business combination meet the contractual-legal criterion.

For the purpose of preparing the unaudited pro forma consolidated income statement, the adjustment represents the amortisation of intangible assets and the related deferred tax impact for the year ended 31 December 2009 as mentioned in note (d). The valuation was carried out by LCH (Asia-Pacific) Surveyors Limited, a firm of independent professional qualified valuers, and the valuation date is on 1 January 2009. The fair value of the signed sales contracts is HK\$31,273,000. Deferred tax liability arising from this intangible asset is HK\$7,818,000 calculated based on income tax rate of 25% accordingly. The amortisation, net of tax for the year ended 31 December 2009 is HK\$13,410,000 of which HK\$8,046,000 attributable to the owners of the Company and HK\$5,364,000 attributable to the non-controlling interests.

These adjustments have continuing income statement effect to the Enlarged Group, and the actual amount may vary according to the fair value of the signed sale contracts signed prior to the date of Completion.

- (h) For the purpose of the unaudited pro forma consolidated statement of cash flows presentation, the beginning balance of cash and cash equivalent of the Project Company of approximately HK\$1,923,000 has been adjusted to reflect the net cash flow effect on the Acquisition as if the Acquisition had been completed on 1 January 2009 and the Project Company had become a subsidiary of the Target Group since 1 January 2009.

APPENDIX V

UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

- (i) The adjustments represent the re-classifications of the balances due from/(to) a non-controlling shareholder and fellow subsidiaries of the Target Group and companies related to this non-controlling shareholder upon the Completion.
- (j) The adjustment is to reflect the effect on cash flows arising from the Acquisition on the unaudited pro forma consolidated statement of cash flows of the Group as if the Acquisition had taken place on 1 January 2009 and is detailed as follows:

HK\$'000

Cash consideration paid to the Vendor	(35,000)
Cash consideration to be paid to the Vendor	(35,000)
Cash and cash equivalents in the Project Company as at 1 January 2009 (as extracted in Appendix II (translated into HK\$ at exchange rate of HK\$1 = RMB0.88))	1,923
	<u>(68,077)</u>

- (k) The adjustment represents the elimination of the pre-acquisition reserves of the Target Group as if the Acquisition had been completed on 31 December 2009.

HK\$'000

the Target Group (where the Project Company only was not consolidated) (<i>note</i>)	(54)
the Project Company (<i>note</i>)	66,593
Capitalisation of amounts due to a director/shareholder and ultimate holding company (<i>note c</i>)	35,012
	<u>101,551</u>

Note: These figures are extracted from the Accountants' Reports set out in Appendices I to II (translated into HK\$ at exchange rate of HK\$1 = RMB0.88).

- (l) The adjustments are to reflect the effect of the Acquisition on the unaudited pro forma consolidated income statement of the Enlarged Group as if the Acquisition had been completed on 1 January 2009.

The fair value of the investment cost at completion of the Acquisition which is to be satisfied in the following manners:

	<i>Notes</i>	<i>HK\$'000</i>
Cash consideration		70,000
Upon Completion		
– Allotment and issuance of 1,510,000,000 Consideration Shares of the Company	<i>(i)</i>	51,340
– Issue of Convertible Notes	<i>(ii)</i>	34,372
		<u>155,712</u>

APPENDIX V

**UNAUDITED PRO FORMA FINANCIAL
INFORMATION OF THE ENLARGED GROUP**

- (i) The fair value of HK\$0.034 per share for the Consideration Shares is for illustrative purpose only. As the par value of the Consideration Share is HK\$0.01 per share, the issue and allotment of 1,510,000,000 Consideration Shares at the fair value of HK\$0.034 per share as at 1 January 2009 for the unaudited pro forma consolidated income statement purpose, credited as fully paid, result in the increase of share capital and share premium account by HK\$15,100,000 and HK\$36,240,000 respectively. The actual fair value will be based on the market price of the shares of the Company upon Completion which may be different from HK\$0.034 per share. Accordingly, the actual goodwill at the date of Completion may be different from the amount presented below.
- (ii) The adjustment represents the estimated fair value of the Convertible Notes issued for the Acquisition as if they were issued on 1 January 2009. The Company has no obligation to repay the principal amount of the Convertible Bonds or pay interest and therefore the whole amount of the Convertible Notes is classified as equity. The valuation of the Convertible Notes was carried out by LCH (Asia-Pacific) Surveyors Limited, a firm of independent professional qualified valuers, and the valuation date is on 1 January 2009. The fair value of the Convertible Notes of approximately HK\$34,372,000 is determined using income approach. On Completion, the fair value of the Convertible Notes will have to be reassessed as at the date of Completion.

Details of goodwill arising on the Acquisition as if the Acquisition was completed on 1 January 2009 and the Project Company had become a subsidiary of the Target Group since 1 January 2009 are as follows:

	<i>HK\$'000</i>
Fair value of cost of investment at Completion	155,712
<i>Less:</i>	
Fair value of net identifiable liabilities of the Project Company to be acquired as extracted from the accountants' report set out in Appendix II (translated into HK\$ at exchange rate of HK\$1 = RMB0.88) (note: all entities within the Target Group (excluding the Project Company) were incorporated after 1 January 2009)	111,699
Capitalisation of shareholder's loan immediately prior to the Completion (<i>note c</i>)	35,000
Fair value of intangible assets, net of deferred tax (<i>note g</i>)	23,455
Non-controlling interests (<i>note e</i>)	(54,062)
	116,092
Goodwill	39,620

Accordingly, there is no effect on the unaudited pro forma consolidated income statement for the year ended 31 December 2009.

On Completion, the fair values of the cost of investment and the net identifiable assets to be acquired will have to be reassessed and accordingly, their fair values at the date of Completion will be different from those for the preparation of the Unaudited Pro Forma Financial Information. As a result, the amount of goodwill may be different from that estimation based on the basis, as stated above, used in the preparation of the Unaudited Pro Forma Financial Information. Accordingly, the actual goodwill at the date of Completion may be different from that presented above.

- (m) In addition to the acquisition of the Target Company mentioned above, on 25 September 2009, the Group entered into an agreement with another vendor, Greater Finance Limited (“Greater Finance”) to acquire the entire equity interests in China International Energy Investments (Hong Kong) Limited (together with its subsidiaries collectively referred to as the “China International Group”) for a consideration of HK\$1,500,000,000 (subject to adjustments). The China International Group is principally established in the People’s Republic of China and investing in oil and gas business.

The consideration shall be satisfied in the following manners:

	<i>HK\$’000</i>
Cash consideration paid to Greater Finance as at 31 December 2009	150,000
Upon Completion	
– Allotment and issuance of consideration shares of the Company	246,240
– issue of 2% interest bearing promissory notes	50,000
– Issue of Tranche 1 Bonds	526,880
After Completion – upon the outstanding litigation released or settled by Greater Finance	
– Issue of Tranche 2 Bonds	526,880
	<u>1,500,000</u>

Details of the acquisition of the China International Group are set out in the Company’s announcement dated on 22 October 2009. As at the date of this circular, the acquisition of the China International Group is still in progress.

Except for the deposit of HK\$150,000,000 which had been paid to Greater Finance prior to 31 December 2009 and had been reflected in the Group’s statement of financial position as at 31 December 2009, the impact of the above acquisition has not yet been reflected in the Unaudited Pro Forma Financial Information.

**ACCOUNTANTS' REPORT ON UNAUDITED PRO FORMA FINANCIAL INFORMATION
OF THE ENLARGED GROUP**

The following is the text of an accountants' report, prepared for the sole purpose of inclusion in this circular, received from the independent reporting accountants, Grant Thornton, Certified Public Accountants, Hong Kong, in respect of the Unaudited Pro Forma Financial Information of the Enlarged Group.



Member of Grant Thornton International Ltd

28 June 2010

The Directors
Xian Yuen Titanium Resources Holdings Limited
Room 1102B, 11/F, Tower 1
Admiralty Centre
18 Harbour Road
Hong Kong

Dear Sirs

XIAN YUEN TITANIUM RESOURCES HOLDINGS LIMITED

We report on the unaudited pro forma financial information (the “Unaudited Pro Forma Financial Information”) of Xian Yuen Titanium Resources Holdings Limited (the “Company”) and its subsidiaries (collectively referred to as the “Group”) which has been prepared by the directors of the Company, solely for illustrative purposes only, to provide information about how the proposed acquisition (the “Acquisition”) of the entire equity interests in Sunlight Rise Limited (the “Target Company”) and its subsidiaries (including Shanxi Zhong Kai Lingshi Heat & Power Company Limited) (collectively known as the “Target Group”) by the Group might have affected the financial information presented, for inclusion in Appendix V of the Company’s circular dated 28 June 2010 (the “Circular”). The basis of preparation of the Unaudited Pro Forma Financial Information is set out in the section headed “Unaudited Pro Forma Financial Information of the Enlarged Group” on page 135 in Appendix V to the Circular.

Respective Responsibilities of Directors of the Company and Reporting Accountants

It is the responsibility solely of the directors of the Company to prepare the Unaudited Pro Forma Financial Information in accordance with paragraph 29 of Chapter 4 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”) and with reference to Accounting Guideline 7 “Preparation of Pro Forma Financial Information for Inclusion in Investment Circulars” issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”).

It is our responsibility to form an opinion, as required by paragraph 29 of Chapter 4 of the Listing Rules on the Unaudited Pro Forma Financial Information and to report our opinion to you. We do not accept any responsibility for any reports previously given by us on any financial information used in the compilation of the Unaudited Pro Forma Financial Information beyond that owed to those to whom those reports were addressed by us at the dates of their issue.

Basis of opinion

We conducted our engagement in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 300 “Accountants’ Reports on Pro Forma Financial Information in Investment Circulars” issued by HKICPA. Our work consisted primarily of comparing the unadjusted financial information with source documents, considering the evidence supporting the adjustments and discussing the Unaudited Pro Forma Financial Information with the directors of the Company. This engagement did not involve independent examination of any of the underlying financial information.

We planned and performed our work so as to obtain the information and explanations we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Unaudited Pro Forma Financial Information has been properly compiled by the directors of the Company on the basis stated, that such basis is consistent with the accounting policies of the Group and that the adjustments are appropriate for the purposes of the Unaudited Pro Forma Financial Information as disclosed pursuant to paragraph 29(1) of Chapter 4 of the Listing Rules.

Our work did not constitute an audit or review made in accordance with Hong Kong Standards on Auditing or Hong Kong Standards on Review Engagements issued by the HKICPA, and accordingly, we did not express any such assurance on the Unaudited Pro Forma Financial Information.

The Unaudited Pro Forma Financial Information is for illustrative purposes only, based on the judgements and assumptions of the directors of the Company, and because of its hypothetical nature, does not give any assurance or indication that any event will take place in the future and may not be indicative of:

- the financial position of the Enlarged Group as at 31 December 2009 had the Acquisition actually been completed on that date or any future date; or
- the results and cash flows of the Enlarged Group for the year ended 31 December 2009 had the Acquisition actually been completed on 1 January 2009 or any future periods.

Opinion

In our opinion:

- (a) the Unaudited Pro Forma Financial Information has been properly compiled by the directors of the Company on the basis stated;
- (b) such basis is consistent with the accounting policies of the Group; and
- (c) the adjustments are appropriate for the purposes of the Unaudited Pro Forma Financial Information as disclosed pursuant to paragraph 29(1) of Chapter 4 of the Listing Rules.

Yours faithfully

Grant Thornton

Certified Public Accountants

6th Floor, Nexxus Building
41 Connaught Road Central
Hong Kong

C. INDEBTEDNESS

As at the close of business on 30 April 2010, being the latest practicable date for the purpose of this indebtedness statement prior to the despatch of this circular, the Enlarged Group (as further enlarged by Petroleum Development Acquisition) had the following outstanding indebtedness:

(a) Borrowings

As at 30 April 2010, the Enlarged Group (as further enlarged by Petroleum Development Acquisition) had outstanding secured fixed term loan approximately of HK\$22.7 million and unsecured bank loan of approximately HK\$9 million.

(b) Securities

As at 30 April 2010, the Enlarged Group (as further enlarged by Petroleum Development Acquisition) are secured by a charge over the property of a former fellow subsidiary of the Project Company. In addition to this, to the best knowledge of the Directors, the Enlarged Group and Petroleum Development Acquisition did not have any outstanding debt securities as at 30 April 2010.

(c) Contingent Liabilities

As at 30 April 2010, to the best knowledge of the Directors, the Enlarged Group (as further enlarged by Petroleum Development Acquisition) did not have any contingent liabilities.

(d) Capital Commitment

As at 30 April 2010, to the best knowledge of the Directors, the Enlarged Group and Petroleum Development Acquisition had the following capital commitment. The Enlarged Group (as further enlarged by Petroleum Development Acquisition) had an outstanding commitment of RMB69,550,000 for injection the remaining registered capital into the Project Company.

Save as aforesaid, and apart from intra-group liabilities, the Enlarged Group (as further enlarged by Petroleum Development Acquisition) did not have any outstanding mortgages, charges, debentures, loan capital, bank overdrafts, loans debt securities or other similar indebtedness, finance leases or hire purchases commitments, liabilities under acceptance or acceptance credits or any guarantee or other material contingent liabilities outstanding as at 30 April 2010.

For the purpose of this indebtedness statement, foreign currency amounts have been translated into Hong Kong dollars at the approximate rate of exchange prevailing as at 30 April 2010.

D. WORKING CAPITAL

The Directors are of the opinion that following completion of the Acquisition, taking into account the financial resources available to the Enlarged Group (as further enlarged by Petroleum Development Acquisition) including the internally generated funds, the Enlarged Group (as further enlarged by Petroleum Development Acquisition) will have sufficient working capital for at least twelve months from the date of this circular.

The following is the text of a letter, summary of values and valuation certificate, prepared for the purpose of incorporation in this circular received from LCH (Asia-Pacific) Surveyors Limited, an independent valuer, in connection with its valuation as at 31 March 2010 of the properties held or rented by the Group.

(A) PROPERTY INTEREST HELD BY THE GROUP



利駿行測量師有限公司

LCH (Asia-Pacific) Surveyors Limited

PROFESSIONAL SURVEYOR

PLANT AND MACHINERY VALUER

BUSINESS & FINANCIAL SERVICES VALUER

The readers are reminded that the report which follows has been prepared in accordance with the guidelines set by the International Valuation Standards, Eighth Edition, 2007 (the “IVS”) published by the International Valuation Standards Committee as well as the HKIS Valuation Standards on Properties, First Edition, 2005 (the “HKIS Standards”) published by the Hong Kong Institute of Surveyors (the “HKIS”). Both standards entitle the valuer to make assumptions which may on further investigation, for instance by the readers’ legal representative, prove to be inaccurate. Any exception is clearly stated below. Headings are inserted for convenient reference only and have no effect in limiting or extending the language of the paragraphs to which they refer. It is emphasised that the findings and conclusion presented below are based on the documents and facts known to the valuer at the date of this report. If additional documents and facts are made available, the valuer reserves the right to amend this report and its conclusions.

17th Floor
Champion Building
287-291 Des Voeux Road Central
Hong Kong

28 June 2010

The Directors
Xian Yuen Titanium Resources Holdings Limited
Room 1102B, 11th Floor
Tower 1, Admiralty Centre
No. 18 Harcourt Road
Hong Kong

Dear Sirs,

In accordance with the instructions given by the management of Xian Yuen Titanium Resources Holdings Limited (hereinafter referred to as the “Company”) and its subsidiaries (hereinafter together with the Company referred to as the “Group”) to us to report the existing status of certain properties in which the Group has short term leasehold interests in Hong Kong, we confirm that we have made relevant enquiries and obtained such further information as we consider necessary to support our findings of the properties as at 31 March 2010 (hereinafter referred to as the “Relevant Date”) for the Company’s internal management reference.

We understand that the use of our work product (regardless of form of presentation) would form part of the Company’s business due diligence to the properties and we have not been engaged to make specific sale or purchase recommendations. We further understand that the use of our work product will not supplant other due diligence which a rational investor should conduct in reaching business decisions regarding the properties.

Findings

We have assigned no commercial values to the properties which are held by the Group under various operating leases in Hong Kong due mainly to the short-term nature of the tenancy agreements or prohibition against assignment or sub-letting or lack of substantial profit rents.

As at the Latest Practicable Date of this circular, we were unable to identify any adverse news against the properties which may affect the reported findings in our work product. Thus, we are not in the position to report and comment on its impact (if any) to the properties. However, should it be established subsequently that such news did exist at the Relevant Date, we reserve the right to adjust the findings reported herein.

Establishment of titles

For the sake of this engagement, we have been provided with copies of tenancy agreements regarding the properties. We have caused searches to be made at the Land Registry of Hong Kong regarding the properties. However, we have not examined the original documents to verify the ownership and encumbrances or to ascertain the existence of any lease amendments, which may not appear on the copies handed to us. All documents disclosed (if any) are for reference only and no responsibility is assumed for any legal matters concerning the legal title and the rights (if any) to the properties. Any responsibility for our misinterpretation of the documents cannot be accepted. We need to state that we are not legal professionals and are not qualified to ascertain the titles and to report any encumbrances that may be registered against the properties. No responsibility or liability is assumed from our part.

Inspections and investigations of the properties in accordance with VS4 of the HKIS Standards

We have inspected the exterior, where possible, the interior, of the properties in respect of which we have been provided with such information as we have requested for the purpose of our work. We have not inspected those parts of the properties which were covered, unexposed or inaccessible and such parts have been assumed to be in reasonable condition. We cannot express an opinion about or advice upon the condition of the properties and our work product should not be taken as making any implied representation or statement about the condition of the properties. No structural survey, investigation or examination has been made, but in the course of our inspections, we did not note any serious defects in the properties inspected. We are not, however, able to report that the properties are free from rot, infestation or any other structural defects. No tests were carried out to the utilities (if any) and we are unable to identify those utilities covered, unexposed or inaccessible.

We have not carried out on-site measurements to verify the correctness of the areas of the properties, but have assumed that the areas shown on the documents and handed to us are correct. All dimensions, measurements and areas are approximations.

Sources of information and its verification in accordance with VS5 of the HKIS Standards

We have relied solely on the information provided by the management of the Company or its appointed personnel without further verification and have fully accepted advice given to us on such matters as planning approvals or statutory notices, locations, titles, easements, tenure, occupation, lettings, rental, floor areas and all other relevant matters.

The scope of our work has been determined by reference to the properties list provided by the management of the Company. Properties on the list have been included in our work. The management of the Company has confirmed to us that it has no property interests other than the one specified on the list supplied to us.

Information furnished by others, upon which all or portions of our work product are based, is believed to be reliable but has not been verified in all cases. Our procedures to work do not constitute an audit, review, or compilation of the information provided. Thus, no warranty is made nor liability assumed for the accuracy of any data, advice, opinions, or estimates identified as being furnished by others which have been used in formulating our work product.

When we adopted the work products from other professions, external data providers and the management of the Company in our work, the assumptions and caveats that adopted by them in arriving at their figures also applied in our work. The procedures we have taken do not provide all the evidence that would be required in an audit and, as we have not performed an audit, accordingly, we do not express an audit opinion.

To the best of our knowledge, all data set forth in the attached valuation certificate are true and accurate. Although gathered from reliable sources, no warranty is made nor liability assumed for the accuracy of any data, opinions, or estimates identified as being furnished by others which have been used in formulating the attached valuation certificate.

We are unable to accept any responsibility for the information that has not been supplied to us by the management of the Company or its appointed personnel. Also, we have sought and received confirmation from the management of the Company or its appointed personnel that no materials factors have been omitted from the information supplied. Our analysis is based upon full disclosure between us and the Company of material and latent facts that may affect our findings.

Unless otherwise stated, all monetary amounts are in Hong Kong dollars (HK\$).

Limiting conditions

Our findings of the properties in this report are valid only for the stated purpose and only for the Relevant Date, and for the sole use of the named Company. We or our personnel shall not be required to give testimony or attendance in court or to any government agency by reason of this report, and the valuer accepts no responsibility whatsoever to any other person.

No responsibility is taken for changes in market conditions and local government policy and no obligation is assumed to revise the attached valuation certificate to reflect events or conditions, which occur or make known to us subsequent to the date hereof.

Neither the whole nor any part of this report or any reference made hereto may be included in any published documents, circular or statement, or published in any way, without our written approval of the form and context in which it may appear. Nonetheless, we consent to the publication of this report in this circular to the Company's shareholders' reference.

Statements

The attached valuation certificate is prepared in line with the requirements contained in Chapter 5 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited as well as the guidelines contained in the IVS and the HKIS Standards. The work has been undertaken by valuer (*see End Note*), acting as external valuer, qualified for the purpose of this engagement.

We retain a copy of this report together with the data from which it was prepared, and these data and documents will, according to the Laws of Hong Kong, keep for a period of 6 years from the date of this report and to be destroyed thereafter. We considered these records confidential, and we do not permit access to them by anyone, with the exception for law enforcement authorities or court order, without the Company's authorisation and prior arrangement made with us. Moreover, we will add the Company's information into our client list for our future reference.

We hereby certify that the fee for this service is not contingent upon our conclusion of value and we have no significant interest in the properties or the Group.

Our findings are summarised below and the valuation certificate is attached.

Yours faithfully,
For and on behalf of
LCH (Asia-Pacific) Surveyors Limited

Elsa Ng Hung Mui
B.Sc. M.Sc. RPS (GP)
Director

Contributing valuer:
Eugene Lai Chung Yee A.Sc

Note:

Ms Elsa Ng Hung Mui has been conducting valuation of real estate properties in Hong Kong since 1994 and has more than 11 years of experience in valuing properties in mainland China. She obtained a Master Degree of Science in Finance and involved in various financial assets valuations, mining companies, natural and man-made forests in the past years. At present, she is a Member of The HKIS and a valuer in the List of Property Valuers for Undertaking Valuation for Incorporation or Reference in Listing Particulars and Circulars and Valuations in Connection with Takeovers and Mergers published by the HKIS.

SUMMARY OF VALUES**Properties occupied by the Group under various operating leases in Hong Kong**

		Amount of Valuations in its existing state attributable to the Group as at 31 March 2010
Property		
1.	Room 1508 on 15th Floor The Centre No. 99 Queen's Road Central Hong Kong	No Commercial Value
2.	Room 1102 B-C on 11th Floor of Tower 1 Admiralty Centre No. 18 Harcourt Road Hong Kong	No Commercial Value
Total		Nil

VALUATION CERTIFICATE

Properties occupied by the Group under various operating leases in Hong Kong

Property	Description and occupancy	Amount of valuation in its existing state attributable to the Group as at 31 March 2010
1. Room 1508 on 15th Floor The Centre No. 99 Queen's Road Central Hong Kong	The property comprises an office unit on the 15th Floor of a 79-storeyed office building which was completed in 1998. The property has a gross floor area of approximately 1,730 sq.ft. The property is rented to the Group for a term of 3 years commencing from 1 January 2010 and expiring on 31 December 2012 at a monthly rental of HK\$55,500, exclusive of Government Rates and Rent, management fee and air-conditioning charges. The property is currently occupied by the Group for office purpose.	No Commercial Value

Notes:

1. The registered owner of the property is Supreme Goal Investments Limited, an independent party to the Group.
2. The tenant of the property is Treasure Tone Limited, which is a wholly-owned subsidiary of the Company.

APPENDIX VI**PROPERTY VALUATION OF THE ENLARGED GROUP**

			Amount of valuation in its existing state attributable to the Group as at 31 March 2010
	Property	Description and occupancy	
2.	Room 1102 B-C on 11th Floor Tower 1, Admiralty Centre No. 18 Harcourt Road Hong Kong	The property comprises 2 office units on the 11th Floor of a 32-storeyed office building which was completed in 1980. The property has a total gross floor area of approximately 1,853 sq.ft. The property is rented to the Group for a term of 2 years commencing from 15 October 2009 and expiring on 14 October 2011 at an annual rental of HK\$689,316, exclusive of Rates, Government rent and management fee. The property is currently occupied by the Group for office purpose.	No Commercial Value

Notes:

1. The registered owner of the property is Everich Century Limited, an independent party to the Group.
2. The tenant of the property is Ho Fai Carpet Trading Limited, which is a subsidiary of the Company.

The following is the text of a letter and valuation certificates prepared for the purpose of incorporation in this circular received from LCH (Asia-Pacific) Surveyors Limited, an independent valuer, in connection with its valuation as at 31 March 2010 of the property interests of the Target Group.

(B) PROPERTY INTERESTS HELD BY THE TARGET GROUP



利駿行測量師有限公司

LCH (Asia-Pacific) Surveyors Limited

PROFESSIONAL SURVEYOR

PLANT AND MACHINERY VALUER

BUSINESS & FINANCIAL SERVICES VALUER

The readers are reminded that the report which follows has been prepared in accordance with the guidelines set by the International Valuation Standards, Eighth Edition, 2007 (the “IVS”) published by the International Valuation Standards Committee as well as the HKIS Valuation Standards on Properties, First Edition, 2005 (the “HKIS Standards”) published by the Hong Kong Institute of Surveyors (the “HKIS”). Both standards entitle the valuer to make assumptions which may on further investigation, for instance by the readers’ legal representative, prove to be inaccurate. Any exception is clearly stated below. Headings are inserted for convenient reference only and have no effect in limiting or extending the language of the paragraphs to which they refer. It is emphasised that the findings and conclusion presented below are based on the documents and facts known to the valuer at the date of this report. If additional documents and facts are made available, the valuer reserves the right to amend this report and its conclusions.

17th Floor
Champion Building
287-291 Des Voeux Road Central
Hong Kong

28 June 2010

The Directors
Xian Yuen Titanium Resources Holdings Limited
Room 1102B, 11th Floor
Tower 1, Admiralty Centre
No. 18 Harcourt Road
Hong Kong

Dear Sirs,

In accordance with the instructions given by the management of Xian Yuen Titanium Resources Holdings Limited (hereinafter referred to as the “Company”) to us to value a property in which the Company and its subsidiaries (hereinafter together with the Company referred to as the “Group”) have intention to acquire in the People’s Republic of China (hereinafter referred to as the “PRC” or “China”), we confirm that we have inspected the property, made relevant enquiries and obtained such further information as we consider necessary to support our opinion of value of the property as at 31 March 2010 (hereinafter referred to as the “Date of Valuation”) for the Company’s internal management reference and for the Company’s shareholders’ reference purposes. We are given to understand the property is currently held by the Target Group (as defined in this circular).

We understand that the use of our work product (regardless of form of presentation) would form part of the Company's business due diligence to the property and we have not been engaged to make specific sale or purchase recommendations. We further understand that the use of our work product will not supplant other due diligence which a rational investor should conduct in reaching business decisions regarding the property. Our work is designed solely to provide information that will give a reference to the management of the Company as part of its due diligence process, and should not be the only factor to be referenced by the Company.

Basis of valuation and assumptions

According to the IVS which the HKIS Standards also follows, there are two valuation bases, namely market value basis and valuation bases other than market value.

The term "Market Value" is defined by the IVS and the HKIS Standards as "the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion".

Due to the purpose of this engagement, the management of the Company was requested to provide us the necessary title documents to support that the legally interested party in the property i.e. the Target Group has free and uninterrupted rights to assign, to mortgage and to let the property interests (in this instance, an absolute title) for the whole of the unexpired terms as granted and any premiums payable have already been paid in full. Should this not be the case or only a restricted title was available (i.e. has a right to use but further application procedures are required) as at the Date of Valuation, no market value will be assigned to the particular property for it is difficult to us to estimate the actual disposal cost and to deduct it from the valuation to arrive at the market value.

According to the information provided by the management of the Company and its appointed personnel, the land use rights of the property is administratively allocated in nature and is not allowed to freely assign the property. Thus, for the sake of this valuation, we have assigned no market value to the property. The readers are reminded to have their own legal due diligence on the transferability of the property.

Matters that might affect the value reported

No allowance has been made in our valuation for any charges, mortgages, outstanding premium or amounts owing on the property. Unless otherwise stated, it is assumed that the property is free from all encumbrances, restrictions, and outgoings of an onerous nature which could affect its value.

As at the Latest Practicable Date of this circular, we were unable to identify any adverse news against the property which may affect the reported value in our work product. Thus, we are not in the position to report and comment on its impact (if any) to the property. However, should it be established subsequently that such news did exist at the Date of Valuation, we reserve the right to adjust the value reported herein.

Establishment of titles

The management of the Company provided us the necessary documents to support that the legally interested party in the property (i.e. the Target Group) has the right to occupy the property. However, our procedures to value, as agreed with the management of the Company, did not require us to conduct legal due diligence on the legality and formality on the way that the legally interested party obtained the property from the relevant authorities.

For the sake of valuation, we have been provided with copies of the title documents of the property and legal opinions dated 24 June 2010 and issued by Shanxi Jiajing Law Firm (山西佳鏡律師事務所), lawyer qualified to practice in China (the “Legal Opinion”) regarding the property. However, we have not examined the original documents to verify the ownership and encumbrances or to ascertain the existence of any amendments, which may not appear on the copies handed to us. All documents disclosed (if any) are for reference only and no responsibility is assumed for any legal matters concerning the legal title and the rights (if any) to the property valued. In the course of preparing our report, we have relied solely on the copy of the Legal Opinion with regard to the existing legally interested party in the property being valued. All documents disclosed (if any) are for reference only and no responsibility is assumed for any legal matters concerning the legal titles and the rights (if any) to the property valued. Any responsibility for our misinterpretation of the documents cannot be accepted.

The inherent defects in the land registration system of China forbidden us to inspect the original documents of the property that filed in the relevant authorities and to verify ownership or to verify any amendment which may not appear on the copies handed to us. We need to state that we are not legal professionals and are not qualified to ascertain the titles and to report any encumbrances that may be registered against the property. We are not in the legal profession and we are unable to ascertain the titles and to report on any encumbrances that may be registered against the property. No responsibility or liability from our part is assumed.

In our valuation, we have assumed that the legally interested party in the property (i.e. the Target Group) has obtained all the approval and/or endorsement from the relevant authorities, and that there would have no legal impediment (especially from the regulators) for the legally interested party to continue the ownership of the property. Should this not be the case, it will affect our conclusion in this report significantly. The readers are reminded to have their own legal due diligence work on such issues. No responsibility or liability from our part is assumed.

Inspections and investigations of the property in accordance with VS4 of the HKIS Standards

We have conducted inspection to the exterior, and where possible, the interior of the property in respect of which we have been provided with such information as we have requested for the purpose of our valuation. We have not inspected those parts of the property which were covered, unexposed or inaccessible and such parts have been assumed to be in reasonable condition. We cannot express an opinion about or advice upon the condition of the property and our work product should not be taken as making any implied representation or statement about the condition of the property. No structural survey, investigation or examination has been made, but in the course of our inspections, we did not note any serious defects in the property inspected. We are not, however, able to report that the property is free from rot, infestation or any other structural defects. No tests were carried out to the utilities (if any) and we are unable to identify those utilities covered, unexposed or inaccessible.

Our valuation has been made on the assumption that no unauthorised alteration, extension or addition has been made in the property, and that the inspection and the use of this report do not purport to be a building survey of the property. We have assumed that the property is free of rot and inherent danger or unsuitable materials and techniques.

We have not carried out on-site measurements to verify the correctness of the areas of the property, but have assumed that the areas shown on the documents and handed to us are correct. All dimensions, measurements and areas are approximations.

Our engagement and the agreed procedures to value the property did not include an independent land survey to verify the legal boundaries of the property. We need to state that we are not in the land survey profession, therefore, we are not in the position to verify or ascertain the correctness of the legal boundaries of such property that appeared on the documents handed to us. No responsibility from our part is assumed. The management of the Company or interested party in the property should conduct their own legal boundaries due diligence work.

We have not arranged for any investigation to be carried out to determine whether or not any deleterious or hazardous material has been used in the construction of the property, or has since been incorporated, and we are therefore unable to report that the property is free from risk in this respect. For the purpose of the valuation, we have assumed that such investigation would not disclose the presence of any such material to any significant extent.

We are not aware of the content of any environmental audit or other environmental investigation or soil survey which may have been carried out on the property and which may draw attention to any contamination or the possibility of any such contamination. In undertaking our work, we have been instructed to assume that no contaminative or potentially contaminative uses have ever been carried out in the property. We have not carried out any investigation into past or present uses, either of the property or of any neighbouring land, to establish whether there is any contamination or potential for contamination to the property from these uses or sites, and have therefore assumed that none exists. However, should it be established subsequently that contamination, seepage or pollution exists at the property or on any neighbouring land, or that the property has been or is being put to a contaminative use, this might reduce the value now reported.

Sources of information and its verification in accordance with VS5 of the HKIS Standards

We have relied solely on the information provided by the management of the Company or its appointed personnel without further verification and have fully accepted advice given to us on such matters as planning approvals or statutory notices, locations, titles, easements, tenure, occupation, site and floor areas and all other relevant matters.

The scope of valuation has been determined by reference to the property list provided by the management of the Company. The management of the Company has confirmed to us that the Target Group has no property interests other than those disclosed in the attached valuation certificate.

Unless otherwise stated, we have not carried out any valuation on a redevelopment basis and the study of possible alternative development options and the related economics do not come within the scope of our work product.

Our valuation has been made only based on the advice and information made available to us. While a limited scope of general inquiries had been made to the local property market practitioners, we are not in a position to verify and ascertain the correctness of the advice given by the relevant personnel. No responsibility or liability is assumed.

Information furnished by others, upon which all or portions of our work product are based, is believed to be reliable but has not been verified in all cases. Our procedures to value or work do not constitute an audit, review, or compilation of the information provided. Thus, no warranty is made nor liability assumed for the accuracy of any data, advice, opinions, or estimates identified as being furnished by others which have been used in formulating our work product.

When we adopted the work products from other professions, external data providers and the management of the Company or its appointed personnel in our valuation, the assumptions and caveats that adopted by them in arriving at their figures also applied in our valuation. The procedures we have taken do not provide all the evidence that would be required in an audit and, as we have not performed an audit, accordingly, we do not express an audit opinion.

We are unable to accept any responsibility for the information that has not been supplied to us by the management of the Company or its appointed personnel. Also, we have sought and received confirmation from the management of the Company or its appointed personnel that no materials factors have been omitted from the information supplied. Our analysis and valuation are based upon full disclosure between us and the Company of material and latent facts that may affect the valuation. We have had no reason to doubt the truth and accuracy of the information provided to us by the management of the Company or its appointed personnel. We consider that we have been provided with sufficient information to reach an informed view, and have had no reason to suspect that any material information has been withheld.

Unless otherwise stated, all monetary amounts are in Renminbi Yuan (“RMB”).

Limiting conditions

Our opinion of value of the property in this report is valid only for the stated purpose and only for the Date of Valuation, and for the sole use of the named Company. We or our personnel shall not be required to give testimony or attendance in court or to any government agency by reason of this report, and the valuer accepts no responsibility whatsoever to any other person.

No responsibility is taken for changes in market conditions and local government policy and no obligation is assumed to revise this report to reflect events or conditions, which occur or make known to us subsequent to the date hereof.

Neither the whole nor any part of this report or any reference made hereto may be included in any published documents, circular or statement, or published in any way, without our written approval of the form and context in which it may appear. Nonetheless, we consent to the publication of this report in this circular to the Company’s shareholders’ reference.

Our maximum liability relating to services rendered under this engagement (regardless of form of action, whether in contract, negligence or otherwise) shall be limited to the charges paid to us for the portion of its services or work products giving rise to liability. In no event shall we be liable for consequential, special, incidental or punitive loss, damage or expense (including without limitation, lost profits, opportunity costs, etc.), even if it has been advised of their possible existence.

The Company is required to indemnify and hold us and our personnel harmless from any claims, liabilities, costs and expenses (including, without limitation, attorney’s fees and the time of our personnel involved) brought against, paid or incurred by us at a time and in any way based on the information made available in connection with our work product except to the extent any such losses, expenses, damages or liabilities are ultimately determined to be the result of gross negligence of our engagement team in conducting its work. This provision shall survive even after the termination of this engagement for any reason.

Statements

Our report is prepared in line with the requirements contained in Chapter 5 and Practice Note 12 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited as well as the guidelines contained in the IVS and the HKIS Standards. The valuation has been undertaken by valuer (*see End Note*), acting as external valuer, qualified for the purpose of the valuation.

We retain a copy of this report together with the data from which it was prepared, and these data and documents will, according to the Laws of Hong Kong, keep for a period of 6 years from the date of this report and to be destroyed thereafter. We considered these records confidential, and we do not permit access to them by anyone, with the exception for law enforcement authorities or court order, without the Company's authorisation and prior arrangement made with us.

The valuation of the property depends solely on the assumptions made in this report and not all of which can be easily quantified or ascertained exactly. Should some or all of the assumptions prove to be inaccurate at a later date, it will affect the reported value significantly.

We hereby certify that the fee for this service is not contingent upon our conclusion of value and we have no significant interest in the property, the Group, the Target Group or the value reported.

The valuation certificate is attached.

Yours faithfully,

For and on behalf of

LCH (Asia-Pacific) Surveyors Limited

Elsa Ng Hung Mui

B.Sc. M.Sc. RPS (GP)

Director

Note:

Ms Elsa Ng Hung Mui has been conducting valuation of real estate properties in Hong Kong since 1994 and has more than 11 years of experience in valuing properties in mainland China. She obtained a Master Degree of Science in Finance and involved in various financial assets valuations, mining companies, natural and man-made forests in the past years. At present, she is a Member of The HKIS and a valuer in the List of Property Valuers for Undertaking Valuation for Incorporation or Reference in Listing Particulars and Circulars and Valuations in Connection with Takeovers and Mergers published by the HKIS.

VALUATION CERTIFICATE

Property occupied by the Target Group in the PRC under restricted title

Property	Description and tenure	Particulars of occupancy	Amount of valuation in existing state attributable to the Target Group as at 31 March 2010 RMB
A factory complex erected on a parcel of land and located at Nanwang Zhong Village Cuifeng Town Lingshi County Shanxi Province The People's Republic of China	The property comprises a parcel of land having a site area of approximately 76,666.67 sq.m. and there are 43 various buildings and structures erected thereon. The major buildings and structures comprise of factories, ancillary office and staff quarters, and various single to 2-storeyed supporting facilities. They have a total gross floor area of approximately 56,506.15 sq.m. and were completed between 2004 and 2007 (<i>see Notes 2 and 3 below</i>). The property is held under a State-owned Land Use Rights Certificate without a specified term for industrial usage (<i>see Note 1 below</i>).	As inspected and advised by the management of the Company that, as at the Date of Valuation, the property was occupied by the Target Group for workshop, ancillary office and staff quarters, and other supporting purposes.	No Commercial Value (<i>see Note 6 below</i>)

Notes:

- Pursuant to a copy of the State-owned Land Use Rights Certificate dated 6 February 2007 and issued by the People's Government of Lingshi County, the legally interested party in the land having a site area of approximately 76,666.67 sq.m. is 山西中凱集團靈石熱電有限公司 (Shanxi Zhong Kai Group Lingshi Heat & Power Company Limited and hereinafter referred to as the "Project Company"), a member of the Target Group. According to the certificate, the land use rights of the property is restricted for industrial usage without a specified term.
- Pursuant to a Building Ownership Certificate known as Lingshi County Fang Quan Zheng Zi Di 00005021 Hao 靈石縣房權證字第00005021號 issued by the People's Government of Lingshi County on 27 February 2009, the legally interested party in the 2 various buildings having a total gross floor area of approximately 11,376 sq.m. is the Project Company.
- According to our on site inspection and information made available to us, there are various buildings and structures without Building Ownership Certificates erected on the subject land of the property. The buildings and structures including factories, pump rooms, laboratory and electricity rooms and other supporting facilities having a total gross floor area of approximately 45,130.15 sq.m.
- The Project Company is a sino-foreign (Taiwan, Hong Kong and Macau) equity joint venture limited liability company established in China with a valid Enterprise Legal Person Business License.

5. According to the legal opinions as prepared by the Group's PRC legal adviser, Shanxi Jiajing Law Firm, the following opinions are noted:
- (i) The Project Company has obtained the right to use the land legally by way of administrative allocation and the relevant land use rights is legal; and
 - (ii) The Project Company is the only legally interested party in the property and has an absolute right to use the property for its own, but subject to restrictions on assignment, lease or mortgage.
6. According to the Listing Rules published by the Stock Exchange of Hong Kong Limited, property in China is required to have a transferable long term title certificate, i.e. State-owned Land Use Rights Certificate or Realty Title Certificate, prior the valuer can assign any commercial (market) value to the property. According to the information provided by the management of the Company and its appointed personnel, the land use rights of the property is administratively allocated in nature and is not allowed to freely assign on the market. Thus, for the sake of this valuation, we have assigned no market value to the property. For information purpose only, the depreciated replacement cost of the improvements erected on the subject land of the property as at the Date of Valuation was assessed as approximately RMB81,200,000.

The following is the text of a report prepared for the purpose of incorporation in this circular received from BMI Appraisals Limited, an independent valuer, in connection with its valuation as at 30 April 2010 of the market value of a 60% equity interest in 山西中凱集團靈石熱電有限公司 (Shanxi Zhong Kai Group Lingshi Heating & Power Company Limited) to be acquired by Precious New Limited, a wholly-owned subsidiary of Xian Yuen Titanium Resources Holdings Limited.

BMI APPRAISALS

BMI Appraisals Limited 中和邦盟評估有限公司

Suite 11-18, 31/F., Shui On Centre, 6-8 Harbour Road, Wanchai, Hong Kong

香港灣仔港灣道6-8號瑞安中心3111-18室

Tel電話：(852) 2802 2191 Fax傳真：(852) 2802 0863

Email電郵：info@bmintelligence.com Website網址：www.bmi-appraisals.com

28 June 2010

The Directors

Xian Yuen Titanium Resources Holdings Limited

Room 1102B, 11th Floor

Tower 1, Admiralty Centre

18 Harcourt Road

Hong Kong

Dear Sirs,

INSTRUCTIONS

We refer to the instructions from Xian Yuen Titanium Resources Holdings Limited (referred to as the “Company”) for us to provide our independent opinion on the market value of a 60% equity interest in 山西中凱集團靈石熱電有限公司 (Shanxi Zhong Kai Group Lingshi Heat and Power Company Limited) (referred to as the “Project Company”). The date of valuation is 30 April 2010.

This report describes the background of the Project Company, an industry overview, the basis of valuation, the source of information, the scope of works and the valuation assumptions. It also explains the valuation methodology utilized and presents our conclusion of value.

BASIS OF VALUATION

We have conducted our valuation in accordance with the Business Valuation Standards published by the Hong Kong Business Valuation Forum in 2005. This valuation has been carried out on the basis of market value. Market value is defined as “the estimated amount for which an asset should exchange on the date of valuation between a willing buyer and a willing seller in an arm’s length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion”.

BACKGROUND OF THE PROJECT COMPANY

The Project Company was incorporated under the laws of the People's Republic of China (referred to as the "PRC") on 31 December 2005 and commenced the business from September 2007. It is principally engaged in the business of generating and supplying electricity and heat by using coke oven gas and alternatively, burning coal gravel or gangue, in the PRC. In the two years ended 31 December 2009, the Project Company generated more than 210 million kWh of electricity and 1 million GJ of heat, and met the minimum production capacity requirements in the PRC.

The Project Company owns a piece of land situated in Nanwangzhong Village (南王中村), Cuifeng Town (翠峰鎮), Lingshi County (靈石縣), Shanxi Province (山西省), the PRC with a total site area of approximately 76,666.67 m². The land is free from any charge or mortgage. A power plant and factory with an area of approximately 56,506.15 m² was built on the land, and in which about 380 employees are employed.

The Project Company operates a combined heat and electricity generation plant using coal waste or gangue from many coal mines and processing plants in the area and coke oven gas from coking plants near the plant. During the initial stage of applying for a permit to construct and operate the combined heat and power generation plant, the Project Company had intended to utilize coal wastes from neighboring coal related industries.

The combined heat and electricity generation plant is located in Lingshi County, part of Jinzhong City (晉中市) of Shanxi Province, at the southern tip of the city, adjacent to Changzhi (長治市) City and Linfen City (臨汾市) about 150 km away from Jinzhong City (Yuci District (榆次區)) and Taiyuan City (太原市). It lies in the Chengdong Industrial Zone (城東工業區), Lingshi County and approximately 3 km away from the central area of the county, with good transportation conditions.

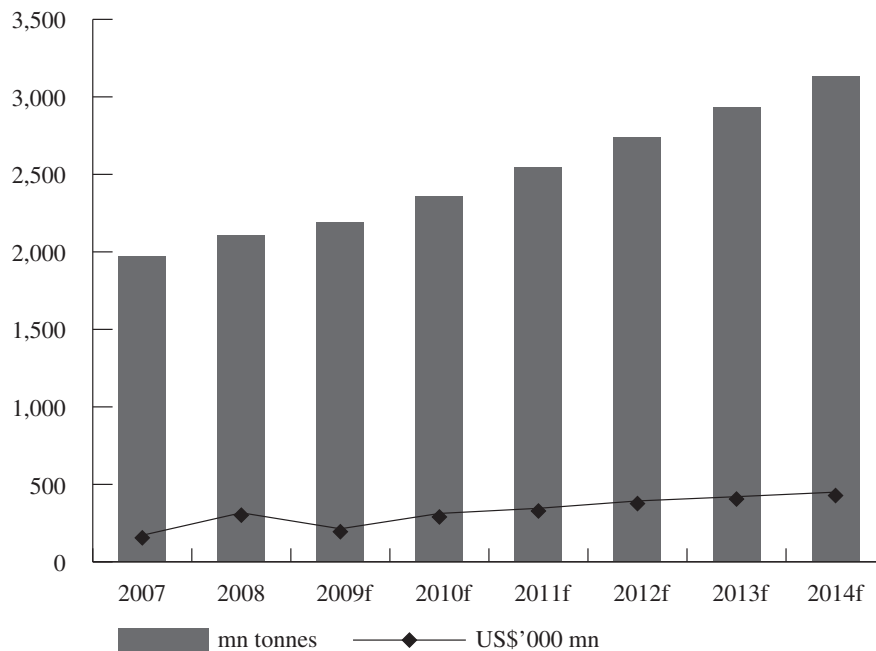
The combined heat and electricity generation plant consists of Thermal Plant I which began operation in year 2004 with 2 x 6 MW generators and two sets of 35 t/h circulating fluidised bed boilers fired by coal waste from local coal mining operations and Thermal Plant II which began operation in year 2007 with 2 x 12 MW generators and three sets of 85 t/h circulating fluidised bed boilers fired by coal waste and coke oven gas. In year 2008, a flue gas desulfurisation system was added to Thermal Plant I to reduce SO₂ emissions. Limestone is used in Thermal Plant II for the fluidised bed and it is not necessary to install any desulfurisation equipment in Thermal Plant II. With such arrangement, the Project Company is entitled to the tariff surcharge for desulphurised coal power generators. During the winter months from November to March, steam produced at Thermal Plant II is exported to a two million m² district heating system in the town of Lingshi County.

The majority of the Project Company's customers are private enterprises. Each of the six major customers of the Project Company has signed an electricity and heat supply agreement with the Project Company, some of these agreements last for a term of one year which will be automatically renewed for a further year at the end of each term.

INDUSTRY OVERVIEW

With a limited reserve of oil and natural gas in the PRC, coal continuously plays a critical role as the source of energy. From the research of Business Monitor International, about 69.5% of the primary energy demand in the PRC was dominated by coal fuel in year 2009, with an anticipated growth of 38.9% from year 2008 to year 2013. The graph below indicates the actual and forecasted coal consumption of the PRC from year 2007 to year 2014.

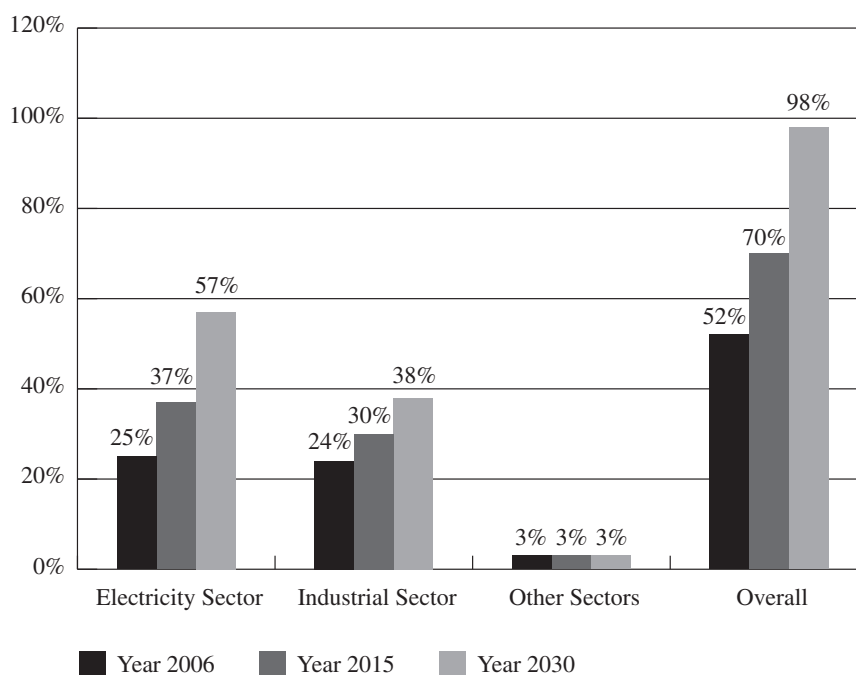
The Coal Consumption in the PRC, 2007-2014f



Source: Business Monitor International

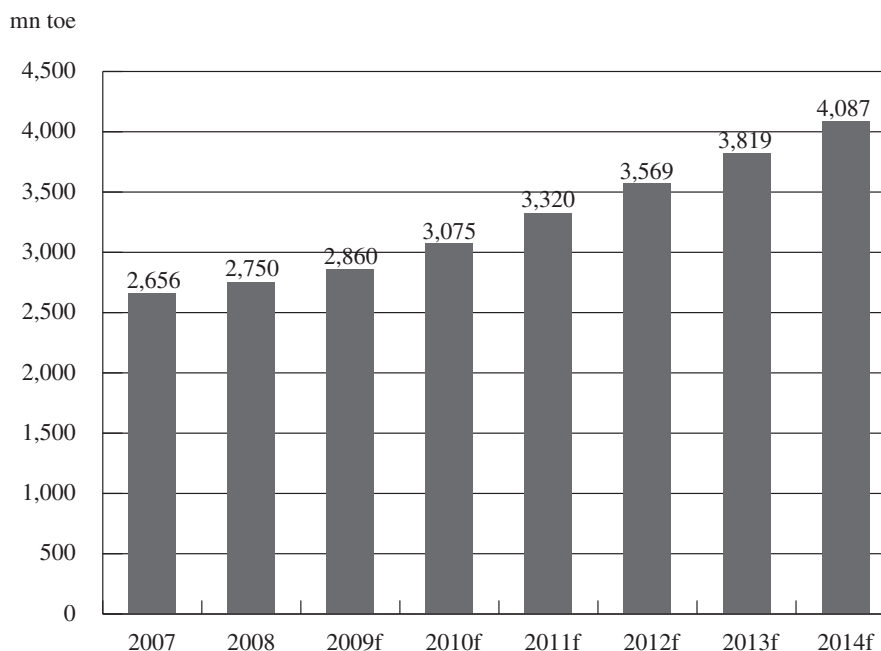
The PRC's coal use in electricity sector was recorded as 24.9 quadrillion British thermal unit (Btu) in year 2006 and was projected to be 57.3 quadrillion Btu in year 2030 by Energy Information Administration, with an average growth rate of 3.5% per annum.

The Coal Consumption in the PRC by Sector, 2006, 2015 and 2030



Source: Energy Information Administration

To meet the rapid economy growth, an additional 600 gigawatts of coal-fired capacity is expected to be set up for the power generation requirement in the PRC from year 2006 to year 2030. Large investment in new coal-fired power plants and related electricity systems is required. According to Energy Information Administration, there would be an increase of 55.1% for coal-fired generating capacity during the period from year 2006 to year 2010.

The Coal-fired Generation in the PRC, 2007-2014f (terawatt hours (TWh))

Source: Business Monitor International

SOURCE OF INFORMATION

For the purpose of our valuation, we were furnished with the financial and operational information in respect of the Project Company, which were provided by the senior management of the Company.

The valuation required the consideration of all pertinent factors affecting the economic benefits of the Project Company and its ability to generate future investment returns. The factors considered in the valuation included, but were not limited to, the following:

- The business nature and characteristics of the Project Company including the historical background, the overall industry sector and the geographical location in which the Project Company currently operates or will operate;
- The financial and operational information in respect of the Project Company, which were provided by the senior management of the Company;
- The specific economic environment and competition for the market in which the Project Company currently operates or will operate;
- Market-derived investment returns of entities engaged in similar lines of business; and
- The financial and business risks related to the Project Company including the continuity of the revenues and incomes being generated.

SCOPE OF WORKS

In the course of our valuation work, we have conducted the following processes to evaluate the reasonableness of the adopted bases and assumptions provided by the senior management of the Company:

- Interviewed with the senior management of the Company to understand the core business operations of the Project Company and obtained all relevant financial and operational information in respect of the Project Company from the senior management of the Company;
- Examined all relevant bases and assumptions of both the financial and operational information in respect of the Project Company, which were provided by the senior management of the Company;
- Conducted appropriate research and consultation in order to obtain sufficient industrial information and statistical figures and prepared a business financial model based on generally accepted valuation procedures and methodologies to derive our concluded value; and
- Presented all relevant information on the background of the Project Company, an industry overview, the basis of valuation, the source of information, the scope of works, the valuation assumptions, the valuation methodology and our conclusion of value in this report.

VALUATION ASSUMPTIONS

Due to the changing environment in which the Project Company currently operates or will operate, a number of assumptions had to be established in order to sufficiently support our concluded value. The major assumptions adopted in our valuation are:

- All licenses, permits, certificates and consents issued by any local, provincial or national government or other authorized entity or organization that will affect the continuity of the Project Company have been obtained or can be obtained upon request with an immaterial cost;
- The Project Company currently has, or will have, adequate human capital and production capacity required for the generation of electricity and heat; and the required human capital and production capacity will be acquired in a timely manner that will not affect the revenues and incomes being generated;
- There will be no material change in the existing political, legal, fiscal, technological, market and economic conditions in the jurisdiction where the Project Company currently operates or will operate, which will affect the revenues and incomes being generated;
- There will be no material change in the taxation laws and regulations in the jurisdiction where the Project Company currently operates or will operate, that the rates of tax payable remain unchanged and that all applicable laws and regulations will be complied with;

- The market return, market risk, interest rates and exchange rates will not differ materially from those presently prevailing and market and economic conditions will not differ materially from those of present or forecasted;
- The supply and demand of electricity and heat in the jurisdiction where the Project Company currently operates or will operate will not differ materially from those of present or expected;
- The core business operations of the Project Company will not differ materially from those of present or expected;
- The financial and operational information in respect of the Project Company have been prepared on a reasonable basis, reflecting estimates that have been arrived at after due and careful considerations by the senior management of the Company;
- The management of the Project Company will implement only those prospective financial and operational strategies that will maximize the efficiency of the operation of the business;
- The management of the Project Company has sufficient knowledge and experience in respect of the operation of the business, and the turnover of any director, management or key person will not significantly affect the operation of the business;
- The Project Company has adequate financial capital for the investments in projected capital expenditure and working capital from time to time, and any scheduled interest or repayment of loan and payable will be paid on time;
- The Project Company has adopted reasonable and appropriate contingency measures against any human disruption such as fraud, corruption and strike, and the occurrence of any human disruption will not significantly affect the operation of the business;
- The Project Company has adopted reasonable and appropriate contingency measures against any natural disaster such as fire, flood and hurricane, and the occurrence of any natural disaster will not significantly affect the operation of the business;
- The Project Company will not undergo public offering and shares of the Project Company will not be listed in any major stock exchange or be marketable in any over-the-counter market in the near future; and
- The Project Company can be freely disposed of and transferred free of all encumbrances for its existing or approved uses in the market to any third party without payment of any premium to any local, provincial or national government or other authorized entity or organization.

VALUATION METHODOLOGY**The Valuation Approaches**

Three generally accepted valuation approaches have been considered in the valuation. They are the cost approach, the market approach and the income approach.

The cost approach provides an indication of value based on the principle that an informed buyer would pay no more than the cost of producing a substitute asset with an equal utility as the subject asset. Under the cost approach, the historical cost method measures the cost incurred through the development of the subject asset at the time it was developed; the replication cost method measures the amount of investment that would be required to develop an asset similar to the subject asset; and the replacement cost method measures the amount of investment that would be required to develop the subject asset as it currently exists.

The market approach provides an indication of value by comparing the subject asset to similar businesses, business ownership interests or securities that have been sold in the market, with appropriate adjustments for the differences between the subject asset and the comparable assets. Under the market approach, the guideline company method computes a price multiple for publicly listed comparable companies and then applies the result to a base of the subject asset; and the sales comparison method computes a price multiple using recent sales and purchase transactions of comparable assets and then applies the result to a base of the subject asset.

The income approach provides an indication of value based on the principle that an informed buyer would pay no more than the present value of anticipated future economic benefits generated by the subject asset. The discounted cash flow (DCF) method is the most fundamental and prominent method of the income approach. In applying the DCF method, the expected cash flows of an asset in the future were determined. The results were then discounted using a discount rate, or the cost of capital, to determine the present value of the expected cash flows. The present value of the expected cash flows was computed using the following formula:

$$PVCF = CF1 / (1 + r)^1 + CF2 / (1 + r)^2 + \cdots + CFn / (1 + r)^n$$

Where:

PVCF	=	present value of expected cash flows
CF	=	expected cash flow
r	=	discount rate
n	=	number of year of projections

The Selected Valuation Approach

The selection of a valuation approach is based on, among other criteria, the quantity and quality of the information provided, access to available data, availability of relevant market transactions, type and nature of the subject asset, purpose and objective of the valuation and professional judgment and technical expertise.

The market approach was considered to be the most appropriate valuation approach in this valuation as it is the most direct valuation approach which reflects the value obtained as a result of a consensus of what others in the market place have judged it to be. Under the market approach, the guideline company method was adopted in the valuation.

The Comparable Companies

The market value of the Project Company was determined with reference to the financial and operational information of publicly listed companies that are considered to be comparable to the Project Company (referred to as the “Comparable Companies”).

The selection of the Comparable Companies was based on the comparability of the overall industry sector and geographical location. Although no two companies are ever exactly alike, behind the differences there are certain business universals such as projected sales growth rate, profit margin, required resources investment, overall perceived risk and uncertainties that guided the market in reaching the expected returns and risks. The Comparable Companies are as follows:

Comparable Company 1

Name of Company	:	Guangzhou Hengyun Enterprises Holdings Ltd. (廣州恒運企業集團股份有限公司)
Bloomberg Ticker	:	000531 CH
Core Businesses	:	Guangzhou Hengyun Enterprises Holdings Ltd. generates electric power and heat for Guangzhou City (廣州市) and the surrounding area in Guangdong Province (廣東省), the PRC.

Comparable Company 2

Name of Company	:	An Hui Wenergy Co., Ltd. (安徽省皖能股份有限公司)
Bloomberg Ticker	:	000543 CH
Core Businesses	:	An Hui Wenergy Co., Ltd. generates electric power. Through its subsidiaries, it also manufactures networking terminal products.

Comparable Company 3

Name of Company	:	Jiangxi Ganneng Co., Ltd. (江西贛能股份有限公司)
Bloomberg Ticker	:	000899 CH
Core Businesses	:	Jiangxi Ganneng Co., Ltd. generates electric power. It also invests in energy saving projects and provides boiler installation and maintenance services.

Comparable Company 4

Name of Company	:	Guangdong Electric Power Development Co., Ltd. (廣東電力發展股份有限公司)
Bloomberg Ticker	:	200539 CH
Core Businesses	:	Guangdong Electric Power Development Co., Ltd. operates and constructs electric power plants in Guangdong Province (廣東省), the PRC.

Comparable Company 5

Name of Company	:	Huadian Power International Corporation Limited (華電國際電力股份有限公司)
Bloomberg Ticker	:	600027 CH
Core Businesses	:	Huadian Power International Corporation Limited generates and sells electricity which is all fed into the provincial grid of Shandong Province (山東省) operated by Shandong Electric Power (Group) Corporation (山東電力集團公司), its immediate holding company. It also sells heat.

Comparable Company 6

Name of Company	:	Beijing Jingneng Thermal Power Co., Ltd. (北京京能熱電股份有限公司)
Bloomberg Ticker	:	600578 CH
Core Businesses	:	Beijing Jingneng Thermal Power Co., Ltd. generates electrical and thermal power. It also maintains and repairs electricity generation equipment.

Comparable Company 7

Name of Company	:	Top Energy Company Ltd. (山西通寶能源股份有限公司)
Bloomberg Ticker	:	600780 CH
Core Businesses	:	Top Energy Company Ltd. operates thermal power plants and generates electric power. The electric power generated is supplied to Shanxi Province (山西省), the PRC.

Comparable Company 8

Name of Company	:	Inner Mongolia MengDian HuaNeng Thermal Power Corp., Ltd. (內蒙古蒙電華能熱電股份有限公司)
Bloomberg Ticker	:	600863 CH
Core Businesses	:	Inner Mongolia MengDian HuaNeng Thermal Power Corp., Ltd. generates electric power and distributes heat and water. It serves western Inner Mongolia Autonomous Region (內蒙古自治區) and the surrounding area in the PRC.

Comparable Company 9

Name of Company	:	SDIC Huajing Power Holdings Co., Ltd. (國投華靖電力控股股份有限公司)
Bloomberg Ticker	:	600886 CH
Core Businesses	:	SDIC Huajing Power Holdings Co., Ltd. generates thermal electric and hydroelectric power. The electric power generated is supplied to Gansu Province (甘肅省) and the surrounding area in the PRC.

Comparable Company 10

Name of Company	:	Zhejiang Southeast Electric Power Co., Ltd. (浙江東南發電股份有限公司)
Bloomberg Ticker	:	900949 CH
Core Businesses	:	Zhejiang Southeast Electric Power Co., Ltd. generates electric power. The electric power generated is distributed throughout Zhejiang Province (浙江省), the PRC.

In the course of determining the Comparable Companies, we have considered the comparability of the Comparable Companies and the Projected Company including, but not limited to, the product segments, the geographic segments and the source of power and heat generation.

APPENDIX VII

VALUATION OF THE PROJECT COMPANY

In respect of the product segments, all of the Comparable Companies had over 85% of revenues derived from power and heat generation in years 2007, 2008 and 2009, respectively, as detailed in the following table:

	Name of Company	Product Segment	Revenue (year 2007, RMB million)	% of Total Revenue (%)
1.	Guangzhou Hengyun Enterprises Holdings Ltd.	Electric Power Generation	1,992.74	91.73%
		Steam Supply	147.34	6.78%
		Others	32.34	1.49%
2.	An Hui Wenergy Co., Ltd.	Electric Power Generation	2,631.07	99.86%
		Multimedia Terminals	3.68	0.14%
3.	Jiangxi Ganneng Co., Ltd.	Electric Power Generation	1,702.85	99.72%
		Other Operation – Utilities Services	4.75	0.28%
4.	Guangdong Electric Power Development Co., Ltd.	Electric Power Generation	10,229.73	98.43%
		Labor Services	92.62	0.89%
		Steam Supply	62.09	0.60%
		Others – Utilities Services	2.99	0.03%
		Rental Income	2.62	0.03%
		Coal Ashes	2.43	0.02%
		Sales of Fuel Material	0.60	0.01%
5.	Huadian Power International Corporation Limited	Sale of Electricity	20,008.80	98.37%
		Sales of Heat	332.33	1.63%
6.	Beijing Jingneng Thermal Power Co., Ltd.	Electricity	1,434.05	87.18%
		Heat Supply	189.64	11.53%
		Others – Utility Supply	9.80	0.60%
		Repair and Maintenance	10.68	0.65%
		Plaster	0.79	0.05%
7.	Top Energy Company Ltd.	Electric Power Generation	2,058.09	98.80%
		Sales of Scrap Mater	3.17	0.15%
		Heat Supply	5.90	0.28%
		Interest Income and Rental Income	15.98	0.77%
8.	Inner Mongolia MengDian HuaNeng Thermal Power Corp., Ltd.	Electric Power Generation	5,888.59	86.29%
		Others – Repair and Maintenance	723.53	10.60%
		Heat Supply	202.20	2.96%
		Water Supply	10.00	0.15%
9.	SDIC Huajing Power Holdings Co., Ltd.	Electricity	6,624.28	99.63%
		Other Operations	24.70	0.37%
10.	Zhejiang Southeast Electric Power Co., Ltd.	Electric Power Generation	6,253.50	99.65%
		Others – Utility Supply	21.88	0.35%

APPENDIX VII

VALUATION OF THE PROJECT COMPANY

	Name of Company	Product Segment	Revenue (year 2008, RMB million)	% of Total Revenue (%)
1.	Guangzhou Hengyun Enterprises Holdings Ltd.	Electric Power Generation	2,623.32	93.32%
		Steam Supply	147.10	5.23%
		Others	40.72	1.45%
2.	An Hui Wenergy Co., Ltd.	Electric Power Generation	2,820.61	100.00%
3.	Jiangxi Ganneng Co., Ltd.	Electric Power Generation	2,248.48	99.65%
		Other Operation – Utilities Services	7.60	0.34%
		Consulting Services	0.21	0.01%
4.	Guangdong Electric Power Development Co., Ltd.	Electric Power Generation	11,371.31	97.88%
		Labor Services	113.46	0.98%
		Steam Supply	107.58	0.93%
		Rental Income	16.23	0.14%
		Sales of Fuel Material	4.06	0.03%
		Others – Utilities Services	2.66	0.02%
		Coal Ashes	2.38	0.02%
5.	Huadian Power International Corporation Limited	Sale of Electricity	29,275.04	97.59%
		Sales of Heat	722.22	2.41%
6.	Beijing Jingneng Thermal Power Co., Ltd.	Electricity	1,466.09	86.42%
		Heat Supply	222.20	13.10%
		Others – Utility Supply	7.59	0.45%
		Repair and Maintenance	0.05	0.00%
		Plaster	0.47	0.03%
7.	Top Energy Company Ltd.	Electric Power Generation	1,887.60	97.89%
		Sales of Scrap Mater	33.08	1.72%
		Heat Supply	7.51	0.39%
8.	Inner Mongolia MengDian HuaNeng Thermal Power Corp., Ltd.	Electric Power Generation	6,119.48	83.97%
		Others – Repair and Maintenance	964.46	13.23%
		Heat Supply	195.35	2.68%
		Water Supply	8.51	0.12%
9.	SDIC Huajing Power Holdings Co., Ltd.	Electricity	10,872.74	98.97%
		Other	82.02	0.75%
		Other Operations	30.80	0.28%
10.	Zhejiang Southeast Electric Power Co., Ltd.	Electric Power Generation	7,094.35	98.94%
		Others – Utility Supply	76.05	1.06%

APPENDIX VII

VALUATION OF THE PROJECT COMPANY

	Name of Company	Product Segment	Revenue (year 2009, RMB million)	% of Total Revenue (%)
1.	Guangzhou Hengyun Enterprises Holdings Ltd.	Electric Power Generation	2,643.08	91.47%
		Steam Supply	194.88	6.74%
		Others	50.12	1.73%
		Desulfurizer	1.46	0.05%
2.	An Hui Wenergy Co., Ltd.	Electric Power Generation	3,210.55	97.09%
		Other Operating Revenue	96.39	2.91%
3.	Jiangxi Ganneng Co., Ltd.	Electric Power Generation	2,154.91	99.40%
		Other Operation – Utilities Services	12.99	0.60%
4.	Guangdong Electric Power Development Co., Ltd.	Electric Power Generation	12,083.09	98.76%
		Labor Services	74.11	0.61%
		Steam Supply	61.17	0.50%
		Others – Utilities Services	6.27	0.05%
		Rental Income	5.16	0.04%
		Coal Ashes	3.60	0.03%
		Sales of Fuel Material	1.32	0.01%
5.	Huadian Power International Corporation Limited	Sale of Electricity	35,197.00	96.57%
		Sales of Heat	1,252.00	3.43%
6.	Beijing Jingneng Thermal Power Co., Ltd.	Electricity	1,538.83	83.15%
		Heat Supply	299.83	16.20%
		Others – Utility Supply	8.07	0.44%
		Repair and Maintenance	3.05	0.16%
		Plaster	0.94	0.05%
7.	Top Energy Company Ltd.	Electric Power Generation	1,849.62	99.63%
		Heat Supply	6.80	0.37%
8.	Inner Mongolia MengDian HuaNeng Thermal Power Corp., Ltd.	Electric Power Generation	6,583.18	91.48%
		Others – Repair and Maintenance	473.34	6.58%
		Heat Supply	140.04	1.95%
9.	SDIC Huajing Power Holdings Co., Ltd.	Electricity	11,807.87	99.08%
		Others	73.27	0.61%
		Other Operations	35.98	0.30%
10.	Zhejiang Southeast Electric Power Co., Ltd.	Electric Power Generation	7,368.07	98.44%
		Others – Utility Supply	116.47	1.56%

In respect of the geographic segments, all of the Comparable Companies had 100% of revenues generated in the PRC in years 2007, 2008 and 2009, respectively, as detailed in the following table:

	Name of Company	Place of Domicile	% of Revenue from the PRC (years 2007, 2008 and 2009, %)
1.	Guangzhou Hengyun Enterprises Holdings Ltd.	The PRC	100.00%
2.	An Hui Wenenergy Co., Ltd.	The PRC	100.00%
3.	Jiangxi Ganneng Co., Ltd.	The PRC	100.00%
4.	Guangdong Electric Power Development Co., Ltd.	The PRC	100.00%
5.	Huadian Power International Corporation Limited	The PRC	100.00%
6.	Beijing Jingneng Thermal Power Co., Ltd.	The PRC	100.00%
7.	Top Energy Company Ltd.	The PRC	100.00%
8.	Inner Mongolia MengDian HuaNeng Thermal Power Corp., Ltd.	The PRC	100.00%
9.	SDIC Huajing Power Holdings Co., Ltd.	The PRC	100.00%
10.	Zhejiang Southeast Electric Power Co., Ltd.	The PRC	100.00%

Since all of the Comparable Companies and the Project Company had 100% of revenue generated in the PRC, international issues such as tariff, export tax, quota, treaty and voluntary export restraint agreement had no effect on the operations of the Comparable Companies and the Project Company.

In determining the Comparable Companies, those companies generate power and heat using sources other than coal such as hydropower, wind power and natural gas were excluded, and all of the Comparable Company use coal as the source to generate all, or nearly all, power and heat. Therefore, after considering the product segments, the geographic segments and the source of power and heat generation, the Comparable Companies were adopted to determine the market value of the Project Company. To the best of our knowledge, the list of the Comparable Companies is exhaustive that represents the overall industry sector and geographic location of the Project Company, and the results derived are fair, reasonable and reliable.

The Price Multiple

In the course of our valuation, we have considered various price multiples including, but not limited to, the price-to-earnings (P/E) multiple, price-to-sales (P/S) multiple and the price-to-book (P/B) multiple. The P/E multiple was not adopted as the volatile and transitory portion of earnings makes the interpretation of P/E multiples difficult, and management discretion within allowed accounting practices can distort reported earnings and thereby lessen the comparability of P/E multiples across firms. The P/S multiple was not adopted as it does not capture differences in cost structure across companies. The P/B multiple was also not adopted as it does not reflect the value of intangible economic assets such as human capital, and inflation and technological change can cause the book values and market values of assets to differ significantly.

APPENDIX VII

VALUATION OF THE PROJECT COMPANY

For our valuation, we adopted the enterprise value (EV) to earnings before interest, tax, depreciation and amortization (EBITDA) (referred to as the “EV/EBITDA”) multiple in assessing the market value of the Project Company. EV was calculated using the following formula:

$$\text{EV} = \text{Market Cap} + \text{PE} + \text{MI} + \text{ST Debt} + \text{LT Debt} - \text{Cash}$$

Where:

EV	=	enterprise value
Market Cap	=	market capitalization
PE	=	preferred equity
MI	=	minority interest
ST Debt	=	short-term debt
LT Debt	=	long-term debt
Cash	=	cash and cash equivalents

The EV/EBITDA multiple is commonly used to value capital-intensive businesses with high levels of depreciation and amortization expenses, such as the power and heat generating industry in which the Project Company currently operates. EV indicates the value of an overall company and is generally considered to be a better metric than market capitalization for transaction-related valuations, as it takes into account the amount of debt which the acquirer will have to assume. The EV/EBITDA multiple relates the total value of a company, as reflected in the market value of its capital from all sources, to a measure of operating earnings generated, which other price multiples such as the P/E multiple, the P/S multiple and the P/B multiple do not include.

The Market Cap, PE, MI, ST Debt, LT Debt and Cash of the Comparable Companies were extracted from Bloomberg Terminal® and the audited financial statements of the Comparable Companies. The EV of the Comparable Companies were calculated as follows:

Name of Company	Market Cap (as at the date of valuation, RMB Million)	PE (year 2009, RMB Million)	MI (year 2009, RMB Million)	ST Debt (year 2009, RMB Million)	LT Debt (year 2009, RMB Million)	Cash (year 2009, RMB Million)	EV (RMB Million)
1. Guangzhou Hengyun Enterprises Holdings Ltd.	3,401	0	1,202	1,568	2,096	621	7,645
2. An Hui Wenergy Co., Ltd.	6,370	0	1,286	1,995	2,261	537	11,374
3. Jiangxi Ganneng Co., Ltd.	4,225	0	9	1,138	3,578	316	8,634
4. Guangdong Electric Power Development Co., Ltd.	11,568	0	2,783	6,388	9,291	1,739	28,292
5. Huadian Power International Corporation Limited	30,808	0	5,219	24,360	45,410	1,242	104,556
6. Beijing Jingneng Thermal Power Co., Ltd.	5,160	0	306	1,971	1,653	294	8,795
7. Top Energy Company Ltd.	5,011	0	0	781	0	266	5,527
8. Inner Mongolia MengDian HuaNeng Thermal Power Corp., Ltd.	15,850	0	2,271	3,599	11,297	163	32,854
9. SDIC Huajing Power Holdings Co., Ltd.	16,120	0	7,121	16,341	50,083	2,084	87,582
10. Zhejiang Southeast Electric Power Co., Ltd.	1,166	0	399	1,175	3,613	626	5,727

Note: Figures may not add up due to rounding

APPENDIX VII

VALUATION OF THE PROJECT COMPANY

EBITDA is the earnings of a company excluding the interest expenses, tax expenses, as well as depreciation and amortization expenses. The interest expenses, tax expenses and depreciation and amortization expenses of the Comparable Companies were extracted from Bloomberg Terminal® and the audited financial statements of the Comparable Companies. The EBITDA of the Comparable Companies were calculated as follows:

Name of Company	Earnings Before Extraordinary Items (year 2009, RMB million)	Interest Expenses (year 2009, RMB Million)	Tax Expenses (year 2009, RMB Million)	Depreciation and Amortization Expenses (year 2009, RMB Million)	EBITDA (year 2009, RMB Million)
1. Guangzhou Hengyun Enterprises Holdings Ltd.	452	170	143	191	956
2. An Hui Wenergy Co., Ltd.	111	149	28	324	612
3. Jiangxi Ganneng Co., Ltd.	81	0	14	221	316
4. Guangdong Electric Power Development Co., Ltd.	1,364	522	298	1,255	3,438
5. Huadian Power International Corporation Limited	1,582	2,956	101	8,240	12,880
6. Beijing Jingneng Thermal Power Co., Ltd.	174	0	46	118	338
7. Top Energy Company Ltd.	7	0	3	302	312
8. Inner Mongolia MengDian HuaNeng Thermal Power Corp., Ltd.	835	864	76	1,270	3,046
9. SDIC Huajing Power Holdings Co., Ltd.	1,009	0	233	2,532	3,774
10. Zhejiang Southeast Electric Power Co., Ltd.	546	0	92	935	1,572

The EV/EBITDA multiples of the Comparable Companies are as follows:

Note: Figures may not add up due to rounding

Name of Company	EV (RMB million)	EBITDA (year 2009, RMB million)	EV/EBITDA Multiple
1. Guangzhou Hengyun Enterprises Holdings Ltd.	7,645	956	8.00
2. An Hui Wenergy Co., Ltd.	11,374	612	18.58
3. Jiangxi Ganneng Co., Ltd.	8,634	316	27.36
4. Guangdong Electric Power Development Co., Ltd.	28,292	3,438	8.23
5. Huadian Power International Corporation Limited	104,556	12,880	8.12
6. Beijing Jingneng Thermal Power Co., Ltd.	8,795	338	26.00
7. Top Energy Company Ltd.	5,527	312	17.69
8. Inner Mongolia MengDian HuaNeng Thermal Power Corp., Ltd.	32,854	3,046	10.79
9. SDIC Huajing Power Holdings Co., Ltd.	87,582	3,774	23.20
10. Zhejiang Southeast Electric Power Co., Ltd.	5,727	1,572	3.64
Median of the EV/EBITDA Multiples:			14.24

Note: Figures may not add up due to rounding

As the EV/EBITDA multiples of some of the Comparable Companies are higher or lower than the others, the median of the EV/EBITDA multiples of the Comparable Companies was adopted in our valuation. Median is considered to be a more appropriate method over other measures (i.e. average) as median is the middle value of a sample, and thus it provides a better indication of the industry average in the presence of a range of values. Moreover, median also provides a more prudent value of the Project Company since the median of the EV/EBITDA multiples of the Comparable Company of 14.24 is lower than the average the EV/EBITDA multiples of the Comparable Company of 15.16.

Although the size of the Comparable Companies varies, there is no significant trend in respect of the size of the Comparable Companies and the corresponding EV/EBITDA multiples (e.g. larger companies have higher EV/EBITDA multiples). Therefore, no adjustment has been made for the size differences of the Comparable Companies in determining the market value of the Project Company.

To determine the market value of the Project Company, the median of the EV/EBITDA multiples of the Comparable Companies of 14.24 was multiplied by the EBITDA of the Project Company to determine the EV of the Project Company. The basis of determining the EBITDA was consistently applied to the Comparable Companies and the Project Company. The EBITDA of the Project Company of RMB63,086,382 in year 2009 was determined with reference to the audited financial statements of the Project Company for the year 2009, with adjustment for non-recurring items, as follows:

Item	RMB
Profit Before Tax	56,882,178
– Non-recurring Items, in which:	
Gain on disposals of property, plant and equipment	27,690
Imputed interest income on interest-free loan from a related company	982,996
Imputed interest income on interest-free loan from a shareholder (the former ultimate parent)	7,211,205
Sundry income	293,077
= Profit Before Tax (excluding non-recurring items)	48,367,210
+ Interest Expenses	4,730,224
= EBIT	53,097,434
+ Depreciation Expense	9,432,394
+ Amortization Expense for Prepaid Land Lease Payments	556,554
= EBITDA	63,086,382

Note: Figures may not add up due to rounding

According to an operating agreement (責任制經營協議) entered into between the Project Company and Jiexiu Juyuan Carbon Co., Ltd. (介休市巨源炭素有限公司), a company incorporated in the PRC engages in the manufacturing of graphite and carbon products with a monthly production capacity of 2,500,000 kg, the Project Company agreed to rent two electricity-generating units to Jiexiu Juyuan Carbon Co., Ltd. for RMB12,000,000 per annum. The function of the two electricity-generating units is electricity generation, which is the core business operation of the Project Company. Instead of renting the two electricity-generating units to Jiexiu Juyuan Carbon Co., Ltd., the Project Company can otherwise utilize them itself to generate operating income. Therefore, the rental income was regarded as an operating income and was included in the EBITDA.

The calculated EV of the Project Company was then adjusted by subtracting the total debt, preferred equity and minority interest and adding back the cash and the cash equivalents. The result was then further adjusted by the lack of marketability discount to derive the market value of the Project Company.

The Discount for Lack of Marketability

The discount for lack of marketability is a downward adjustment to the value of an investment to reflect its reduced level of marketability. The concept of marketability deals with the liquidity of an ownership interest, that is, how quickly and easily it can be converted into cash if the owner chooses to sell. The discount for lack of marketability reflects the fact that there is no ready market for shares in a closely held company. Ownership interests in closely held companies are typically not readily marketable compared to similar interests in publicly listed companies. Therefore, a share of stock in a privately held company is usually worth less than an otherwise comparable share in a publicly listed company.

As the Project Company is unlikely to undergo public offering and shares of the Project Company is unlikely to be listed in any major stock exchange or be marketable in any over-the-counter market in the near future, a discount for lack of marketability of 30% has been adopted in determining the market value of the Project Company. The discount for lack of marketability was determined with reference to “Marketability and Value: Measuring the Illiquidity Discount” published by Professor Aswath Damodaran in July 2005 and “International Private Equity and Venture Capital Valuation Guidelines” jointly issued by the Association Française des Investisseurs en Capital (AFIC), the British Venture Capital Association (BVCA) and the European Private Equity and Venture Capital Association (EVCA).

The Control Premium

Control is the right to direct the strategies and activities of a firm, including the right to allocate resources and distribute the economic products. There is a tendency to regard the premium offered to pre-bid trading in a takeover as the value of the control right. As our valuation was carried out based on the market prices of publicly traded companies, in which producing a minority level value, and thus a control premium of 30% was adopted to reflect the value of the control right. The control premium was determined with reference to “Mergerstat Review 2006” published by FactSet Mergerstat, LLC.

REMARKS

For the purpose of this valuation and in arriving at our opinion of value, we have referred to the information provided by the senior management of the Company. We are unable to accept any responsibility and have had no reason to doubt the truth and accuracy of the information provided to us by the Company. We have also sought and received confirmation from the Company that no material facts have been omitted from the information supplied.

To the best of our knowledge, all data set forth in this report are true and accurate. Although gathered from reliable sources, no guarantee is made nor liability assumed for the accuracy of any data, opinions or estimates identified as being furnished by others, which have been used in formulating this analysis.

Unless otherwise stated, all money amounts stated herein are in Hong Kong Dollars (HK\$) and no allowances have been made for any exchange transfers.

CONCLUSION OF VALUE

Our conclusion of value is based on accepted valuation procedures and practices in accordance with the Business Valuation Standards published by the Hong Kong Business Valuation Forum in 2005, which rely substantially on the use of numerous assumptions and the consideration of a lot of uncertainties, not all of which can be easily ascertained or quantified.

Further, whilst the assumptions and consideration of such matters are considered by us to be reasonable, they are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond the control of the Company, the Project Company or us.

Based on our investigation and analysis outlined in this report, it is our independent opinion that the market value of the 60% equity interest in 山西中凱集團靈石熱電有限公司 (Shanxi Zhong Kai Group Lingshi Heat and Power Company Limited) (i.e. the “Project Company”) as at 30 April 2010 was **HK\$552,000,000 (HONG KONG DOLLARS FIVE HUNDRED AND FIFTY TWO MILLION ONLY)**.

We hereby certify that we have neither present nor prospective interest in the Company, the Project Company or the value reported.

Yours faithfully,
For and on behalf of
BMI APPRAISALS LIMITED

Dr. Tony C. H. Cheng

*BSc, MUD, MBA(Finance), MSc(Eng), PhD(Econ),
FCIM, FRSM, SICME, SIFM, MHKIS, MCI Arb, AFA,
MASCE, MIET, MIEEE, MASME, MIIIE, MASHRAE, MAIC
Managing Director*

Marco T. C. Sze

*B.Eng(Hon), PGD(Eng), MBA(Acct),
CFA, AICPA/ABV, RBV
Director*

Notes:

- 1. Dr. Tony C. H. Cheng serves as the Chairman of Institute of Mechanical Engineers, China and is a member of the Hong Kong Institute of Surveyors (General Practice), a member of the American Society of Civil Engineers, a member of the American Society of Mechanical Engineers and a member of Institute of Industrial Engineers (U.K.). He has over 5 years' experience in valuing similar assets or companies engaged in similar business activities as those of the Project Company worldwide.*
- 2. Mr. Marco T. C. Sze is a holder of Chartered Financial Analyst, a member of the American Institute of Certified Public Accountants (AICPA) and is accredited in Business Valuation (ABV) by the AICPA. In addition, he is a Registered Business Valuer under the Hong Kong Business Valuation Forum. He has over 4 years' experience in valuing similar assets or companies engaged in similar business activities as those of the Project Company worldwide.*

1. RESPONSIBILITY STATEMENT

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

2. SHARE CAPITAL

The authorised and issued share capital of the Company as at the Latest Practicable Date and immediately following the issue and allotment of the Consideration Shares and Conversion Shares (assuming that these is an immediate exercise in full of the conversion rights attaching to the Convertible Notes) will be as follows:

Authorised:

<u>20,000,000,000</u>	Shares	<u>HK\$200,000,000</u>
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Issued and fully paid or credited as fully paid:

7,364,586,614	Shares in issue as at the Latest Practicable Date	HK\$73,645,866
1,510,000,000	Consideration Shares to be issued	HK\$15,100,000
1,510,000,000	Conversion Shares to be issued and allotted after Completion in full	HK\$15,100,000
<u>10,384,586,614</u>	Shares in issue immediately following completion of the Acquisition	<u>HK\$103,845,866</u>

All of the Shares in issue and the Consideration Shares to be issued rank pari passu in all respects with each other, including in particular as to dividends, voting rights and capital.

As at the Latest Practicable Date, the Company has (i) 55,905,512 conversion shares to be issued and allotted pursuant to conversion of the tranche 1 zero coupon convertible bonds in the registered form comprising an aggregate principal amount of HK\$28.4 million issued by the Company on the basis of an exercise price of HK\$0.508 per Share; and (ii) 2,358,491 conversion shares to be issued and allotted pursuant to conversion of the tranche 3 zero coupon convertible bonds in the registered form comprising an aggregate principal amount of HK\$500,000 issued by the Company on the basis of an exercise price of HK\$0.212 per Share. Save as disclosed, the Company does not have any other outstanding derivatives, options, warrants and conversion rights or similar rights or securities in issue which are convertible or exchangeable into Shares.

The Shares in issue are listed on the Stock Exchange. No part of the share capital or any other securities of the Company is listed or dealt in on any stock exchange other than the Stock Exchange and no application is being made or is currently proposed or sought for the Shares or any other securities of the Company to be listed or dealt in on any other stock exchange. There is no arrangement under which future dividends are waived or agreed to be waived.

3. DISCLOSURE OF INTERESTS**Interest of Directors in the Company**

As at the Latest Practicable Date, none of the Directors or any chief executive of the Company had an interest or short position in any shares, underlying shares or debentures of the Company or any associated corporation (within the meaning of Part XV of the SFO) which would have to be notified to the Company and the Stock Exchange pursuant to Division 7 and 8 of Part XV of the SFO (including interests and short positions which he was taken or deemed to have under such provisions of the SFO) or which was required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or pursuant to the Model Code for Securities Transactions by Directors of Listed Companies in the Listing Rules to be notified to the Company and the Stock Exchange.

Interests of substantial Shareholders

As at the Latest Practicable Date, so far as was known to the Directors or chief executives of the Company, there is no person who had interests or short position in the Shares or underlying Shares of the Company which would fall to be disclosed to the Company under provisions of Divisions 2 and 3 of Part XV of the SFO or, who were, directly or indirectly interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any other member of the Group or had any option in respect of such capital.

Service Contracts

On 5 November 2007, Mr. Law Fei Shing entered into a service contract with the Company, under which the Company appointed Mr. Law Fei Shing and Mr. Law Fei Shing agreed to act as the chief executive officer, the executive director, the company secretary, the authorised representative and the qualified accountant of the Company for a term of 3 years at a fixed salary of HK\$1,800,000 per annum.

Save as the aforesaid, as at the Latest Practicable Date, none of the Directors had entered or was proposing to enter into any service contracts with any member of the Group (excluding contracts expiring or determinable by the employer within one year without payment of compensation other than statutory compensation).

Interests in other competing business

Each of the Directors has confirmed that he and their respective Associates do not have any interests in a business apart from the Group's business which directly competes with and will have material adverse impact on the Group.

Interests in assets

As at the Latest Practicable Date, none of the Directors has any direct or indirect interest in any assets acquired or disposed of by or leased to any member of the Enlarged Group (as further enlarged by the Petroleum Development Acquisition) or is proposed to be acquired or disposed of by or leased to any member of the Enlarged Group (as further enlarged by the Petroleum Development Acquisition) since 31 December 2009, being the date to which the latest published audited accounts of the Company were made up.

Interests in contract or arrangement

As at the Latest Practicable Date, none of the Directors is materially interested in contract or arrangement subsisting which is significant in relation to the business of the Enlarged Group (as further enlarged by the Petroleum Development Acquisition).

4. LITIGATION

Other than the Acquisition, the Company entered into a conditional share purchase agreement on 25 September 2009 in relation to the Petroleum Development Acquisition. As at the Latest Practicable Date, one of the Hong Kong subsidiaries of the target group of companies (the “**Hong Kong Subsidiary**”) was one of the defendants to the action no. 978 of 2009 which was commenced in the High Court of Hong Kong by Sican Petroleum PLC as plaintiff against, among other parties thereto, the Hong Kong Subsidiary as the second defendant (the “**Outstanding Litigation**”). The Outstanding Litigation alleges, among others, the Hong Kong Subsidiary’s breach of its equitable duty of confidence and/or fiduciary duties owed to the plaintiff by disclosing the confidential information owned or beneficially belonging to the plaintiff to another party and by knowingly causing, procuring or permitting the said other party to use the same to secure the conclusion of a contract for an exploration and exploitation project to the exclusion of the plaintiff in breach of an alleged joint venture agreement between the Hong Kong Subsidiary and the plaintiff in May 2007.

For further information on the Petroleum Development Acquisition and the Outstanding Litigation, please refer to the announcement of the Company dated 22 October 2009. As at the Latest Practicable, the Petroleum Development Acquisition has yet to be completed and the Hong Kong Subsidiary has yet to become a wholly-owned subsidiary of the Company.

Save as disclosed above, as at the Latest Practicable Date, the Enlarged Group was not engaged in any litigation or arbitration of material importance and no litigation or claim of material importance is known to the Directors to be pending or threatened against the Enlarged Group.

5. EXPERTS AND CONSENTS

The qualifications of the experts who have given opinion in this circular is as follows:

Name	Qualification
RSM Nelson Wheeler (“RSM”)	Certified Public Accountants
Grant Thornton (“GT”)	Certified Public Accountants
BMI Appraisal Limited (“BMI”)	Chartered Surveyors
LCH (Asia-Pacific) Surveyors Ltd. (“LCH”)	Professional Surveyor
Shanxi Jiajing Law Firm (“Shanxi Lawyers”)	Qualified PRC legal adviser

As at the Latest Practicable Date, none of RSM, GT, BMI, LCH and Shanxi Lawyers had any shareholding in any company in the Enlarged Group or the right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any company in the Enlarged Group and had any direct or indirect interest in any assets acquired or disposed of by or leased to any member of the Enlarged Group or is proposed to be acquired or disposed of by or leased to any member of the Enlarged Group since 31 December 2009, being the date to which the latest published audited accounts of the Company were made up.

Each of RSM, GT, BMI, LCH and Shanxi Lawyers has given and has not withdrawn its written consent to the issue of this circular with the inclusion herein of its letter and/or references to its name, in the form and context in which they respectively appear.

6. MATERIAL CONTRACTS

The following contracts (not being contracts in the ordinary course of business) have been entered into by members of the Enlarged Group (as further enlarged by the Petroleum Development Acquisition) within the two years preceding the date of this circular and are or may be material:

- (a) an equity transfer agreement dated 29 October 2008 made between Hong Kong Forest Source Mining Industry Holding Company Limited as vendor and Asiagoal Investment Limited as purchaser in relation to the disposal of 北京森源礦產品技術開發有限公司 (Beijing Forest Source Mining Industry Developing Company Limited) at a consideration of HK\$10,000,000;
- (b) a sale and purchase agreement dated 4 December 2008 made between the Company and Jackley China Limited as vendors and Winroy International Limited as purchaser in relation to Orient Carpet Manufacturing (HK) Limited at a consideration of HK\$19,300,000;
- (c) a sale and purchase agreement dated 4 December 2008 made between the Company and Aurora International Enterprises Limited as vendors and Ms. Peng Qui Feng as purchaser in relation to Wise Mount Management Limited at a consideration of HK\$30,000;
- (d) a placing agreement dated 6 August 2009 and supplemental agreement dated 10 August 2009 made between the Company and Mayfair Securities Limited for the placing of 809,280,000 new Shares at HK\$0.137 per placing share;
- (e) the conditional underwriting agreement dated 25 August 2009 entered into between Kingston Securities Limited as the underwriter and the Company in relation to the open offer 2,452,500,000 offer shares at the subscription price of HK\$0.08 per offer Share on the basis of one (1) offer share for every two (2) Shares;
- (f) the conditional agreement dated 25 September 2009 entered into between the Company, Cheerful Dragon Limited as purchaser, Greater Finance Limited as vendor and Mr. Li Weijun as warrantor in relation to the acquisition of the entire issued share capital of China International Energy Investments (Hong Kong) Limited (as supplemented by two supplemental agreements entered into between the Company, the purchaser, the vendor and the warrantor dated 15 October 2009 and 21 October 2009 respectively), details of which are set out in the announcement of the Company dated 22 October 2009; and
- (g) the Agreement.

7. MATERIAL CHANGE

The Directors are not aware of any material adverse changes in the financial or trading position or prospects of the Group since 31 December 2009, being the date to which the latest audited consolidated financial statements of the Group were made up.

8. GENERAL

- (a) The secretary of the Company is Mr. Law Fei Shing, AICPA, HKICPA (Practising).
- (b) The registered office of the Company is situated at Cricket Square, Hutchins Drive, P.O. Box 2681, Grand Cayman KY1-1111, Cayman Islands.
- (c) The head office and principal place of business in Hong Kong is Room 1102B, 11th Floor, Tower I, Admiralty Centre, 18 Harcourt Road, Hong Kong.
- (d) The Company's branch share registrars in Hong Kong is Tricor Tengis Limited at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong.

9. DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents will be available for inspection during 9:30 a.m. to 5:00 p.m. at the head office of the Company at Room 1102B, 11/F., Tower I, Admiralty Centre, 18 Harcourt Road, Hong Kong from the date of this circular up to and including the date of the EGM:

- (a) the memorandum and articles of association of the Company;
- (b) the annual reports of the Company for the two years ended 31 December 2008 and 31 December 2009;
- (c) the accountants' report of the Target Group, the text of which is set out in Appendix I of this circular;
- (d) the accountants' report of the Project Company, the text of which is set out in Appendix II of this circular;
- (e) the unaudited pro forma financial information of the Enlarged Group, the text of which is set out in Appendix V of this circular;
- (f) the property valuation report of the Enlarged Group, the text of which is set out in Appendix VI of this circular;
- (g) the valuation report of the Project Company, the text of which is set out in Appendix VII of this circular;
- (h) the material contracts referred to in the paragraph headed "Material Contracts" in this appendix;
- (i) the service contract referred to in the sub-paragraph headed "Service Contracts" in this appendix;
- (j) the written consents referred to in the paragraph headed "Experts and Consents" in this appendix; and
- (k) the circulars of the Company which have been issued since 31 December 2009.

NOTICE OF EGM



XIAN YUEN TITANIUM RESOURCES HOLDINGS LIMITED

森源鈦礦控股有限公司*

(Incorporated in the Cayman Islands with limited liability)

(Stock code: 353)

NOTICE OF EXTRAORDINARY GENERAL MEETING

NOTICE IS HEREBY GIVEN that an extraordinary general meeting of Xian Yuen Titanium Resources Holdings Limited (the “Company”) will be held at Room 1102B, 11/F., Tower I, Admiralty Centre, 18 Harcourt Road, Hong Kong on Friday, 16 July 2010 at 4:00 p.m. for the following purposes:

To consider and if thought fit, pass the following resolution as ordinary resolution:

ORDINARY RESOLUTION

1. “**THAT:**

- (a) the conditional share purchase agreement dated 5 November 2009 (the “Agreement”, a copy of which has been produced to the meeting marked “A” and signed by the chairman of the meeting for the purpose of identification) entered into between Precious New Limited, a wholly-owned subsidiary of the Company, as purchaser, the Company as the purchaser’s holding company, Maycrown Capital Limited as vendor and Ms. HO Mee Kuen Karen as guarantor in relation to the sale and purchase of the entire issued share capital of Sunlight Rise Limited (a company incorporated under the laws of Hong Kong) at a total consideration of HK\$350,860,000 which will be settled partly by cash and partly by the Company’s issue of consideration shares and convertible notes, further details of which are set out in the circular of the Company dated 28 June 2010 (the “Circular”, a copy of which has been produced to the meeting marked “B” and signed by the chairman of the meeting for the purpose of identification), and the transactions contemplated thereunder be and are hereby approved, confirmed and ratified;
- (b) the allotment and issue of the Consideration Shares (as defined in the Circular), on and subject to the terms of the Agreement, be and is hereby approved;
- (c) the creation of the Convertible Notes (as defined in the Circular), on and subject to the terms of the Agreement, be and is hereby approved;

* For identification purpose only

NOTICE OF EGM

- (d) the directors of the Company be and are hereby authorised to allot and issue the Conversion Shares (as defined in the Circular); and
- (e) the directors of the Company be and are hereby authorised to do all such acts and things and execute all such documents which they consider necessary, desirable or expedient for the purpose of, or in connection with, the implementation of and giving effect to the Agreement and the transactions contemplated thereunder, including but without limitation to the issue of the Convertible Notes, the allotment and issue of the Consideration Shares and the allotment and issue of the Conversion Shares upon conversion of the Convertible Notes.”

By Order of the board of
Xian Yuen Titanium Resources Holdings Limited
Law Fei Shing
Chief Executive Officer and Executive Director

Hong Kong, 28 June 2010

Notes:

1. The instrument appointing a proxy shall be in writing under the hand of the appointor or of his/her attorney duly authorized in writing or, if the appointor is a corporation, either under its seal or under the hand of any officer, attorney or other person duly authorised to sign the same.
2. Any member entitled to attend and vote at the meeting convened by the above notice is entitled to appoint one or more proxies to attend and, in the event of a poll, vote in his/her stead. A proxy need not be a registered shareholder of the Company.
3. In order to be valid, the form of proxy must be lodged with the Company's branch share registrar in Hong Kong, Tricor Tengis Limited at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong together with a power of attorney or other authority, if any, under which it is signed or a notarially certified copy of that power of attorney or authority, not later than 48 hours before the time appointed for holding the meeting or any adjournment thereof.
4. Completion and return of the form of proxy will not preclude members from attending and voting in person at the meeting or at any adjourned meeting (as the case may be) should they so wish, and in such event, the form of proxy shall be deemed to be revoked.
5. Where there are joint holders of any shares in the Company, any one of such joint holders may vote, either in person or by proxy, in respect of such shares as if he/she were solely entitled thereto, but if more than one of such joint holders are present at the meeting, the senior who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders, and for this purpose seniority shall be determined by the order in which the names stand in the register in respect of the joint holding.