THIS CIRCULAR IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION

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

If you have sold or transferred all your Shares, you should at once hand this circular and the accompanying proxy form to the purchaser(s) or the transferee(s) or to the bank, licensed securities dealer, registered institution in securities or other agent through whom the sale or transfer was effected for transmission to the purchaser(s) or transferee(s).

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

AVIC International Holding (HK) Limited
中國航空工業國際控股(香港)有限公司

(Incorporated in Bermuda with limited liability)

(Stock Code: 232)

VERY SUBSTANTIAL ACQUISITION AND CONNECTED TRANSACTION
APPLICATION FOR WHITEWASH WAIVER
CONTINUING CONNECTED TRANSACTION
CLAWBACK OFFER BY AVIC INTERNATIONAL (HK) GROUP LIMITED
RE-ELECTION OF DIRECTOR
NOTICE OF SPECIAL GENERAL MEETING

Financial Adviser to the Company

ANGLO CHINESE
CORPORATE FINANCE, LIMITED
英高

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

SOMERLEY CAPITAL LIMITED

The letter from the Board is set out on pages 8 to 31 of this circular. The letter from the Independent Board Committees are set out on pages 32 to 35 of this circular. The letter from the Independent Financial Adviser is set out on pages 36 to 83 of this circular, which contains its advice to the Independent Board Committees and Independent Shareholders.

A notice convening the SGM to be held at Monaco Room, Basement 1, Regal Hongkong Hotel, 88 Yee Wo Street, Causeway Bay, Hong Kong on Tuesday, 23 January 2018 at 3:00 p.m. is set out on pages SGM-1 to SGM-3 of this circular. A proxy form for use at the SGM is enclosed. Whether or not you intend to attend the SGM, you are requested to complete the enclosed proxy form in accordance with the instructions printed thereon and return the same to the branch share registrar and transfer office of the Company in Hong Kong, Computershare Hong Kong Investor Services Limited at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong as soon as possible but in any event not less than 48 hours before the time appointed for the holding of the SGM or any adjournment thereof. Completion and return of the proxy form shall not preclude you from attending and voting in person at the SGM or any adjournment thereof should you so wish.

29 December 2017

CONTENTS

In this circular, the following words and expressions shall have the meanings set out below, unless the context otherwise requires:

"1H2016"	the six months ended 30 June 2016;
"1H2017"	the six months ended 30 June 2017;
"Acquisition"	the proposed acquisition contemplated under the Acquisition Agreement;
"Acquisition Agreement"	the agreement dated 19 September 2017 entered into between AVIC HK, AVIC International and the Company relating to the acquisition of the entire issued share capital of the Target Company and the shareholder's loan note(s) owing by the Target Company to AVIC HK as at Acquisition Completion, as amended by the Amendment Deed;
"Acquisition Completion"	the completion of the sale and purchase of the entire share capital of the Target Company and the shareholder's loan note(s) owing by the Target Company to AVIC HK in accordance with the provisions of the Acquisition Agreement;
"Acquisition Completion Date"	the date on which Acquisition Completion occurs;
"acting in concert"	has the meaning ascribed to it under the Takeovers Code;
"Amendment Deed"	the amendment deed dated 27 October 2017 entered into between AVIC HK, AVIC International and the Company to amend the payment terms regarding the deferred consideration under the Acquisition Agreement which was announced on 19 September 2017;
"associate(s)"	has the meaning ascribed to it under the Listing Rules;
"Assured Entitlement(s)"	the entitlement(s) of the Qualifying Shareholder(s) to apply for the Offer Shares under the Offering on the basis described in this circular;
"Aviation Industry"	Aviation Industry Corporation of China (中國航空工業集團公司), a state-owned enterprise (全民所有制企業) established in the PRC and holds 62.52% of the equity interest in AVIC International as at the Latest Practicable Date, a controlling shareholder of the Company;
"AVIC Group"	Aviation Industry and its subsidiaries;
"AVIC HK"	AVIC International (HK) Group Limited (中航國際(香港)集團有限公司), a company incorporated in Hong Kong and a direct wholly owned subsidiary of AVIC International;

"AVIC International"	AVIC International Holding Corporation (中國航空技術國際控股有限公司), a company incorporated with limited liability in the PRC and owned as to 62.52% by Aviation Industry;
"Board"	the board of Directors;
"Business Day"	a day (other than a Saturday or Sunday or public holiday in Hong Kong and any day on which a tropical cyclone warning no.8 or above or a "black" rain warning signal is hoisted in Hong Kong at any time between 9:00 a.m. and 5:00 p.m.) on which banks are open in Hong Kong for general commercial business;
"BVI"	the British Virgin Islands;
"CMB"	Continental Motors (Beijing) Co., Ltd., a company incorporated in the PRC with limited liability and an indirect wholly-owned subsidiary of the Target Company as at the Latest Practicable Date;
"CMD"	Continental Motors Deutschland Limited, a company incorporated in BVI with limited liability and an indirect wholly-owned subsidiary of the Target Company as at the Latest Practicable Date;
"CMG"	Continental Motors Group Limited, a company incorporated in Hong Kong with limited liability and an direct wholly-owned subsidiary of the Target Company as at the Latest Practicable Date;
"CMI"	Continental Motors, Inc., a company incorporated under the Laws of Delaware of USA with limited liability and an indirect wholly-owned subsidiary of the Target Company as at the Latest Practicable Date;
"CMS"	Continental Motors Services, Inc., a company incorporated under the Laws of Delaware of USA with limited liability and an indirect wholly-owned subsidiary of the Target Company as at the Latest Practicable Date;
"Code IBC"	the independent board committee comprising all the independent non-executive Directors, namely Mr. Chu Yu Lin, David, Mr. Li Ka Fai, David and Mr. Zhang Ping, and the sole non-executive Director, namely Mr. Chow Wai Kam, which has been established in accordance with the Takeovers Code to advise the Code Independent Shareholders on the Acquisition and the Whitewash Waiver;

"Code Independent Shareholders"	the Shareholders other than the Concert Group and other Shareholders who are involved in, or interested in the Acquisition and the Whitewash Waiver;
"Company"	AVIC International Holding (HK) Limited, a company incorporated in Bermuda with limited liability and whose shares are listed on the Main Board of the Stock Exchange (stock code: 232);
"Concert Group"	AVIC HK and AVIC International and parties acting in concert with each of them;
"connected person(s)"	has the meaning ascribed to it under the Listing Rules;
"Consideration Shares"	a total of 3,783,783,783 new Shares to be issued at the issue price of HK$0.37 per Share to be allotted and issued to AVIC HK as part of the consideration for the sale and purchase of the entire issued share capital of the Target Company and the shareholder's loan note(s) owing by the Target Company to AVIC HK as at Acquisition Completion;
"Directors"	the directors of the Company;
"Effective Date"	the date on which all the conditions precedent under the Sale Framework Agreement have been satisfied (please refer to "Conditions precedent" under the section "Continuing Connected Transaction — the Sale Framework Agreement — Details of the Sale Framework Agreement" in the letter from the Board for details);
"Enlarged Group"	the enlarged Group immediately after the Acquisition Completion;
"EU"	the European Union;
"EUR"	the euro, which is the official currency of the Eurozone;
"Executive"	the Executive Director of the Corporate Finance Division of the Securities and Futures Commission of Hong Kong or any delegate for the time being of the Executive Director;
"FAA"	the Federal Aviation Administration of the US;
"FY2014"	the financial year ended 31 December 2014;
"FY2015"	the financial year ended 31 December 2015;
"FY2016"	the financial year ended 31 December 2016;

"Germany"	the Federal Republic of Germany;
"Group"	the Company and its subsidiaries;
"HK$"	Hong Kong dollars, the lawful currency of Hong Kong;
"Hong Kong"	Hong Kong Special Administrative Region of the PRC;
"HP"	Horsepower;
"Independent Board Committees"	the Code IBC and the LR IBC;
"Independent Shareholders"	the Code Independent Shareholders and the LR Independent Shareholders;
"JLL"	Jones Lang LaSalle Corporate Appraisal & Advisory Limited, being the independent valuer and consultant, in connection with its valuation as at 31 October 2017 of the property interests held by the Group;
"Last Trading Day"	19 September 2017, being the last trading day of the Shares immediately before the publication of the announcement of the Company dated 19 September 2017;
"Latest Practicable Date"	22 December 2017, being the latest practicable date for ascertaining certain information contained in this circular;
"Listing Rules"	the Rules Governing the Listing of Securities on the Stock Exchange;
"LR IBC"	the independent board committee comprising all the independent non-executive Directors, namely Mr. Chu Yu Lin, David, Mr. Li Ka Fai, David and Mr. Zhang Ping, which has been established to advise the LR Independent Shareholders on the Acquisition and the Sale Framework Agreement;
"LR Independent Shareholders"	the Shareholders other than Aviation Industry and its associates;
"MRO"	maintenance, repair and overhaul;
"OEM"	original equipment manufacturer;
"Offering"	the offer to the Qualifying Shareholders to purchase the Offer Shares on and subject to the terms and conditions set out in the Prospectus and the application form(s) to be despatched;

"Offer Share(s)"	initially not more than 2,484,166,998 Shares (assuming that there will be no change in the issued share capital of the Company from the Latest Practicable Date to and including the Record Date) offered pursuant to the Offering subject to adjustment as set out in the section headed "The Clawback Offer by AVIC HK" in the letter from the Board in this circular;
"Overseas Shareholder(s)"	registered holder(s) of Shares whose addresses on the register of members of the Company are outside Hong Kong as at the close of business on the Record Date;
"PMA"	parts manufacturer approval;
"Poly Group"	China Poly Group Corporation (中國保利集團公司), a state-owned enterprise incorporated in the PRC;
"PRC"	the People's Republic of China;
"Prospectus"	the prospectus to be issued by the Company and AVIC HK in relation to the Offering;
"Qualifying Shareholder(s)"	Code Independent Shareholder(s) whose name(s) appear on the register of members of the Company as at the close of business on the Record Date, other than certain Overseas Shareholders and other person(s) whom the directors of the Company and AVIC HK, after making relevant enquiries, consider it necessary or expedient to exclude from the Offering on account either of the legal restrictions under the laws of the relevant place or the requirements of the relevant regulatory body or stock exchange in that place;
"Record Date"	Tuesday, 30 January 2018, or such later date as the parties may announce, the record date for ascertaining the Assured Entitlements;
"RMB"	Renminbi, the lawful currency of PRC;
"Sale Framework Agreement"	an agreement entered into between the Company and Aviation Industry on 24 October 2017, in relation to sale of engines and engine parts to Aviation Industry and/or its associates for use in new aircraft manufacture and the sale of parts into the aftermarket for maintenance, repair and overhaul;
"SASAC"	the PRC State-owned Assets Supervision and Administration Commission;
"SFO"	Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong);

"SGM"	the special general meeting of the Company to be convened and held for the purposes of passing all necessary resolutions for the implementation of the Acquisition and Sale Framework Agreement and the transactions contemplated thereunder and the Whitewash Waiver;
"Shares"	ordinary share(s) of HK$0.10 each in the share capital of the Company;
"Shareholder(s)"	registered holder(s) of the Share(s);
"Stock Exchange"	The Stock Exchange of Hong Kong Limited;
"Somerley"	Somerley Capital Limited, a corporation licensed to carry out type 1 (dealing in securities) and type 6 (advising on corporate finance) regulated activities under the SFO and the independent financial adviser to the Independent Board Committees and the Independent Shareholders in respect of the Acquisition, the Sale Framework Agreement and the Whitewash Waiver;
"Takeovers Code"	the Hong Kong Code on Takeovers and Mergers;
"Target Company"	Motto Investment Limited, a company incorporated in BVI with limited liability and a direct wholly-owned subsidiary of AVIC International as at the Latest Practicable Date;
"Target Group"	the Target Company, and its subsidiaries;
"TMG"	Technify Motors GmbH, a company incorporated in Germany with limited liability and an indirect wholly-owned subsidiary of the Target Company as at the Latest Practicable Date;
"TMI"	Technify Motor (USA) Inc., a company incorporated in Delaware, USA with limited liability and an indirect wholly-owned subsidiary of the Target Company as at the Latest Practicable Date;
"Track Record Period"	the three years ended 31 December 2014, 2015 and 2016, and the six months ended 30 June 2017;
"UAS"	unmanned aviation systems;
"UAV"	unmanned aerial vehicles;
"UK"	the United Kingdom of Great Britain and Northern Ireland;
"US$" or "USD"	United States dollar, the lawful currency of the USA;
"US" or "USA"	the United States of America;

"Whitewash Relevant Period"	the period commencing on the date falling six months preceding 19 September 2017, being the date of the announcement of the Company relating to the Acquisition and Whitewash Waiver, up to and including the Lastest Practicable Date;
"Whitewash Waiver"	the waiver under Note 1 on Dispensations from Rule 26 of the Takeovers Code of the obligation on the part of the AVIC HK to make a general offer to the Shareholders for all issued shares and other securities (as defined in Note 4 to Rule 22 of the Takeovers Code) of the Company not already owned or agreed to be acquired by the Concert Group as a result of the allotment and issuance of the Consideration Shares to AVIC HK which will increase the Concert Group's collective holding of the voting rights of the Company by more than 2%; and
"%"	per cent.

AVIC International Holding (HK) Limited
中國航空工業國際控股(香港)有限公司

(Incorporated in Bermuda with limited liability)

(Stock Code: 232)

Executive Directors:
Mr. Liu Hongde (Chairman)
Mr. Pan Linwu (Deputy Chairman)
Mr. Lai Weixuan
Ms. Zhou Chunhua
Mr. Xu Hongge (Chief Executive Officer)

Non-executive Director:
Mr. Chow Wai Kam

Independent Non-executive Directors:
Mr. Chu Yu Lin, David
Mr. Li Ka Fai, David
Mr. Zhang Ping

Registered office:
Canon's Court
22 Victoria Street
Hamilton HM 12
Bermuda

Head office and principal place of business in Hong Kong:
Unit B, 15th Floor
United Centre
95 Queensway
Hong Kong

29 December 2017

To the Shareholders

Dear Sir or Madam,

VERY SUBSTANTIAL ACQUISITION AND CONNECTED TRANSACTION
APPLICATION FOR WHITEWASH WAIVER
CONTINUING CONNECTED TRANSACTION
CLAWBACK OFFER BY AVIC INTERNATIONAL (HK) GROUP LIMITED
RE-ELECTION OF DIRECTOR
NOTICE OF SPECIAL GENERAL MEETING

I. INTRODUCTION

Reference is made to the announcements of the Company dated 19 September 2017 and 27 October 2017 whereby the Board announced that the Company (as purchaser) entered into the Acquisition Agreement and the Amendment Deed, respectively, with AVIC HK (as seller) and AVIC International (as seller guarantor), pursuant to which AVIC HK has agreed to sell and the Company has agreed to acquire (i) the entire issued share capital of the Target Company and (ii) the shareholder's loan note(s) owing by the Target Company to AVIC HK at Acquisition Completion, at an aggregate consideration of HK$2,400,000,000, out of which HK$1,000,000,000 will be satisfied by cash and HK$1,400,000,000 will be satisfied by way of allotment and issue of the Consideration Shares.

As at the Latest Practicable Date, the Concert Group is interested in 1,895,715,000 Shares in aggregate, representing approximately 34.35% of the issued share capital of the Company. Following the allotment and issue of the Consideration Shares, the shareholding of the Concert Group will increase to approximately 61.05% of the issued share capital of the Company as enlarged by the allotment and issue of the Consideration Shares. As the Acquisition will increase the Concert Group's collective holding of voting rights of the Company by more than 2%, in the absence of the Whitewash Waiver, AVIC HK would be under an obligation to make a mandatory general offer for all the Shares not already owned or agreed to be acquired by the Concert Group pursuant to Rule 26 of the Takeovers Code.

An application to the Executive for the Whitewash Waiver has been made by AVIC HK pursuant to Note 1 on dispensations from Rule 26 of the Takeovers Code. The Whitewash Waiver, if granted by the Executive, will be subject to, among other things, the approval of the Independent Shareholders in respect of the Acquisition and the Whitewash Waiver at the SGM where voting on the relevant resolution shall be taken by poll.

Conditional upon and subject to Acquisition Completion, in order to provide Qualifying Shareholders the opportunity to further participate in and share the growth of the Company and at least to maintain their shareholdings without being diluted by the Acquisition, AVIC HK will offer initially not more than 2,484,166,998 Offer Shares, which constitute approximately 65.65% of the Consideration Shares, to the Qualifying Shareholders on a pro rata basis of 0.6855 Offer Share for every one Share held as at the close of business on the Record Date at HK$0.37 per Offer Share, which is equal to the issue price of the Consideration Shares pursuant to the Acquisition Agreement. Assuming there will be no change in the issued share capital of the Company and the Shares held by AVIC HK and its associates between the Latest Practicable Date and completion of the Offering, save for the allotment and issue of the Consideration Shares and the transfer of the Offer Shares by AVIC HK, 2,484,166,998 Offer Shares represent approximately 26.70% of the issued share capital of the Company as enlarged by the issue of the Consideration Shares on the Record Date.

Reference is also made to the announcement of the Company dated 24 October 2017 whereby the Board announced that the Company entered into the Sale Framework Agreement with Aviation Industry, pursuant to which subsequent to Acquisition Completion, the Group will sell engines and engine parts to Aviation Industry and/or its associates (excluding the Group and the Target Group) for use in new aircraft manufacture and the sale of parts into the aftermarket for maintenance, repair and overhaul.

The purpose of this circular is to provide the Shareholders with: (i) further details of the Acquisition and the Whitewash Waiver; (ii) the recommendation of the Code IBC in relation to the Acquisition and the Whitewash Waiver; (iii) the recommendation of the LR IBC in relation to the

Acquisition and the Sale Framework Agreement; (iv) a letter of advice from the Independent Financial Adviser to the Independent Board Committees and the Independent Shareholders in relation to the Acquisition, the Whitewash Waiver and the Sale Framework Agreement; (v) further information about the Target Group; (vi) financial information of the Group; (vii) accountants' report of the Target Company; (viii) management discussion and analysis on the Group and the Target Group; (ix) unaudited pro forma financial information of the Enlarged Group; (x) particulars of the Director for re-election; and (xi) a notice of the SGM.

II. THE ACQUISITION

On 19 September 2017, the Company (as purchaser) entered into the Acquisition Agreement with AVIC HK (as seller) and AVIC International (as seller guarantor), pursuant to which AVIC HK has agreed to sell and the Company agreed to acquire (i) the entire issued share capital of the Target Company and (ii) the shareholder's loan note(s) owing by the Target Company to AVIC HK at Acquisition Completion, at an aggregate consideration of HK$2,400,000,000. On 27 October 2017, the parties entered into the Amendment Deed to amend the payment terms regarding the deferred consideration under the Acquisition Agreement. Principal terms of the Acquisition Agreement are summarised below.

(A) THE ACQUISITION AGREEMENT

Date: 19 September 2017

Parties:

(a) Seller AVIC HK

(b) Purchaser the Company

(c) Seller Guarantor AVIC International

Subject matter

Under the Acquisition Agreement, AVIC HK has agreed to sell and the Company agreed to acquire (i) the entire issued share capital of the Target Company and (ii) the shareholder's loan note(s) owing by the Target Company to AVIC HK at Acquisition Completion.

Prior to Acquisition Completion, the Seller Guarantor has undertaken, at its own cost, to transfer the entire issued share capital of the Target Company to the Seller as part of the pre-sale reorganisation for the Acquisition.

Consideration

The consideration is HK$2,400,000,000, which is to be satisfied by the Company in the following manner:

(a) HK$1,400,000,000 will be satisfied by way of allotment and issue of the Consideration Shares to AVIC HK at Acquisition Completion;

(b) HK$200,000,000 will be satisfied by cash at Acquisition Completion; and

(c) HK$800,000,000 will be satisfied by cash upon the earlier occurrence of the following events:

(i) the Company having received the proceeds from the disposal of its real estate business, resulting in the Company having net cash balance of more than HK$800,000,000; and

(ii) the Company having net cash balance of more than HK$800,000,000.

The Company shall use its reasonable endeavours to procure that either of the above events is consummated within six months after the Acquisition Completion Date (the "**Six-month Period**"), including conducting financing activities where appropriate. If none of the above events has been consummated within the Six-month Period, the Company shall pay the deferred consideration of HK$800,000,000 to AVIC HK as soon as practicable upon the occurrence of any of the above events after the expiry of the Six-month Period and such payment shall not be construed as a default.

The consideration was determined between the Company and AVIC HK based on arm's length negotiations after taking into account, among other things, (i) the recent financial position and performance of the Target Group, whose earnings before interest, tax, depreciation and amortisation (calculated as the sum of profit before tax, finance costs, depreciation and amortisation of intangible assets) ("**EBITDA**") for FY2014, FY2015, FY2016 and 1H2017 amounted to approximately US$13.9 million, US$24.9 million, US$31.0 million and US$15.7 million, respectively; (ii) valuation of listed companies in the USA and companies being acquired in precedent transactions whose businesses are similar to that of the Target Group, which represents EBITDA multiples ranging between 5 times and 35 times when the consideration was negotiated, whereas the consideration of the Acquisition implies an EBITDA multiple of around 10 times based on the Target Group's EBITDA for FY2016 of approximately US$31.0 million; and (iii) the business prospect of the Target Group as elaborated in the "Reasons for and benefits of the Acquisition" below, which demonstrates the leading position of the Target Group in the worldwide general aviation aircraft piston engines market and the promising growth opportunity in PRC which the Target Group may be able to capture in the future.

Conditions to Acquisition Completion

Acquisition Completion shall be conditional on the following conditions having been fulfilled or waived in accordance with the terms of the Acquisition Agreement:

(a) each of the following being approved by the Independent Shareholders at the SGM, with voting being taken by way of poll: the Acquisition, the allotment and issue by the Company of the Consideration Shares and the Whitewash Waiver;

(b) the grant of the Whitewash Waiver by the Executive;

(c) the listing of, and permission to deal in, the Consideration Shares having been granted by the Stock Exchange and not having been revoked prior to Acquisition Completion;

(d) all applicable waiting periods (and any extensions thereof) under the United States Hart-Scott-Rodino Antitrust Improvement Act of 1976, as amended, having expired or otherwise having been terminated by the applicable Government Entities;

(e) AVIC HK having procured that certain bank loans owed by TMI and TMG are purchased by AVIC HK from the respective banks and that AVIC HK subsequently sells such loans to the Target Company in return for the issuance by the Target Company of interest free, unsecured and repayable on demand loan note(s);

(f) TMI having repaid its loan to CATIC International Finance Limited, a wholly-owned subsidiary of AVIC HK using funds resulting from an additional indirect equity investment by AVIC International into TMI;

(g) the Acquisition is not restricted pursuant to the German Foreign Trade Act in conjunction with the German Foreign Trade Ordinance;

(h) all required consents, approvals or filings of any governmental entity required to consummate the Acquisition having been obtained or completed to the Company's satisfaction;

(i) Aviation Industry and the shareholders of AVIC International having approved the Acquisition; and

(j) each of the warranties made by AVIC HK made in Acquisition Agreement being true and correct in all material respects (if such warranties are not qualified as to materiality) and being true and correct (if such warranties are qualified as to materiality) on and as of the Acquisition Completion Date.

The condition in paragraph (j) above may be waived by notice in writing from the Company. None of the other conditions to Acquisition Completion may be waived by either party. If any of the above conditions has not been fulfilled or waived on or before 31 March 2018 (or such later date as the parties may agree in writing), the Acquisition Agreement shall automatically terminate. As at the Latest Practicable Date, other than set out above in the conditions to Acquisition Completion, there are no mandatory consents, approvals or filings of any governmental entity required to consummate the Acquisition which have been identified or are contemplated. As at the Latest Practicable Date, save for the conditions in paragraphs (d) and (g), none of the above conditions has been fulfilled or waived.

The Consideration Shares

The Consideration Shares represent approximately 68.55% of the issued share capital of the Company as at the Latest Practicable Date and approximately 40.67% of the issued share capital of the Company as enlarged by the Consideration Shares.

The issue price of the Consideration Shares of HK$0.37 represents:

(a) a discount of approximately 18.68% to the closing price of HK$0.455 per Share as quoted on the Stock Exchange on the Latest Practicable Date.

(b) a premium of approximately 1.37% over the closing price of HK$0.365 per Share as quoted on the Stock Exchange on the Last Trading Day;

(c) a premium of approximately 2.78% over the average closing price of HK$0.36 per Share for the last 5 trading days up to and including the Last Trading Day;

(d) the average closing price of HK$0.37 per Share for the last 10 trading days up to and including the Last Trading Day;

(e) the average closing price of HK$0.37 per Share for the last 30 trading days up to and including the Last Trading Day;

(f) a premium of approximately 2.78% over the audited net assets value per Share of approximately HK$0.36, calculated based on the Company's audited equity attributable to owners of the parent of approximately HK$1,973 million as at 31 December 2016; and

(g) a premium of approximately 2.78% over the unaudited net asset value per Share of approximately HK$0.36, calculated based on the Company's unaudited equity attributable to owners of the parent of approximately HK$1,968 million as at 30 June 2017.

The Consideration Shares will at all time rank *pari passu* among themselves and with the Shares in issue as at the date of issue of the Consideration Shares. The Consideration Shares will be issued pursuant to a specific mandate to be sought at the SGM. Application will be made by the Company to the Listing Committee for the listing of, and permission to deal in, the Consideration Shares.

The issue price of the Consideration Shares was arrived on arm's length negotiations between the Company and AVIC HK, with reference to: (i) the average closing price per Share for the last 30 consecutive trading days immediately prior to the Last Trading Day; (ii) the audited net asset value per Share of the Group; and (iii) the proposed acquisitions announced by other listed companies on the Stock Exchange in the twelve-month prior to and including the date of the Acquisition Agreement which constituted a notifiable and connected transaction and involved issue of consideration shares under specific mandate.

In light of the above, the Directors (excluding the non-executive Director and the independent non-executive Directors whose opinion is set out in the letter from the Code IBC and the letter from the LR IBC) consider the issue price of the Consideration Shares is fair and reasonable.

Lock-up Undertaking

AVIC HK undertakes to the Company, among others, that without the Company's prior written consent, it will not directly or indirectly dispose of, nor directly or indirectly enter into any agreement to dispose of, any of the Consideration Shares (other than those Shares taken up by Qualifying Shareholders under the Offering) within six months from the Acquisition Completion Date. AVIC HK may, after expiration of such lock-up period, dispose of, or enter into any agreement to dispose of, the Consideration Shares.

Acquisition Completion

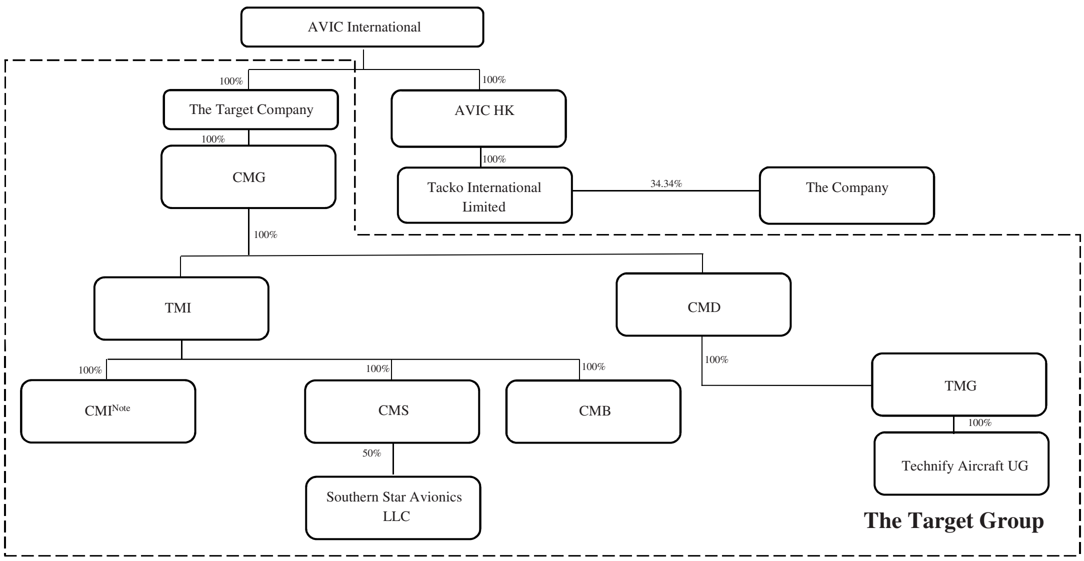
Acquisition Completion shall take place on the tenth Business Day after all the conditions to Acquisition Completion have been fulfilled or waived (or such other date as the parties may agree in writing).

Following Acquisition Completion, the Target Company will become a wholly-owned subsidiary of the Company and the results, assets and liabilities of the Target Group will be consolidated into the financial statements of the Group.

(B) SHAREHOLDING OF THE GROUP AND THE TARGET GROUP BEFORE AND AFTER ACQUISITION COMPLETION

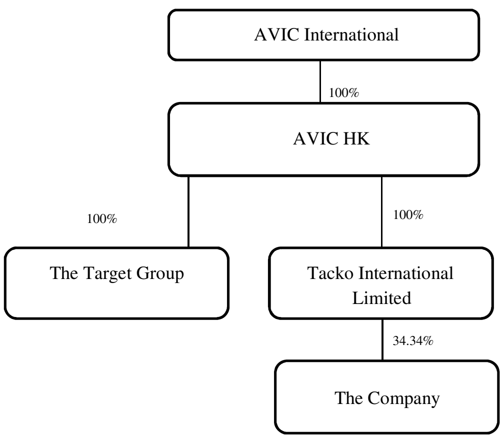
Based upon the shares in issue for each of the companies identified below, as at the Latest Practicable Date and assuming no changes to such issued shares prior to Acquisition Completion, the shareholding structure of the relevant companies before and after Acquisition Completion will be as follows:

Set out below is the shareholding structure of the Group and the Target Group as at the Latest Practicable Date.

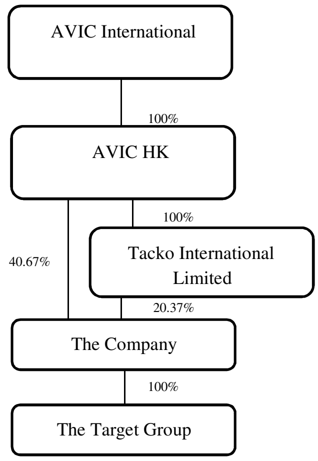


Note: CMI also owns 1,000 preferred shares of Mangrove Cell 1 PC, a protected cell of Mangrove Insurance Solutions, PCC, a protected cell captive insurance company.

Prior to Acquisition Completion, AVIC International will transfer the entire issued share capital of the Target Company to AVIC HK. Set out below the shareholding structure of the Group and the Target Group after the transfer of the Target Company to AVIC HK and immediately before Acquisition Completion.



Set out below the shareholding structure of the Group after Acquisition Completion.



(C) INFORMATION ON THE TARGET GROUP

For details of the Target Group, please refer to "Appendix I — Information about the Target Group" to this circular.

(D) REASONS FOR AND BENEFITS OF THE ACQUISITION

The Company is an investment holding company which has been engaged in property development and trading business since 2014. The Company was previously engaged in knitting and textile business until it was disposed in June 2016 and has been exploring new businesses or investment opportunities in the aero-technology related business and other fields to enhance its business development and financial position.

The Company has had a track record in aviation business since 2002: -

- On 28 May 2002, the Company entered into an income assignment agreement with AVIC International, pursuant to which AVIC International agreed to assign to the Company 80% of the net income it is entitled to from a joint venture between AVIC International and other third parties, named Project EC120, which is engaged in development, manufacture and distribution of helicopters. Under such income assignment agreement, the Company agreed to provide technical assistance and management consultancy services to AVIC International. Project EC120 continued to contribute profit to the Company until 2011 when it no longer produced sufficient net income for distribution. The Company continued to report Project EC120 as a financial asset in its financial statements and had recorded aero-technology related business as an individual segment in its annual report until FY2014.

- On 28 May 2002, the Company entered into an agreement to invest in CATIC Siwei Co., Ltd ("**CATIC Siwei**"), which engages in the provision of aerophotographic services, data collection, geospatial business applications and services, by way of a capital injection. As at the Latest Practicable Date, the Company, indirectly through nominee shareholding arrangements, held a 69.4% equity interest in CATIC Siwei.

As set out in the Company's announcement dated 7 September 2016, the Company was considering a series of business and asset reorganisation proposals which included the acquisition of certain assets and the disposal of the Group's real estate development business in the PRC. The proposed reorganisation was being contemplated by the Company as part of a wider restructuring campaign being implemented by SASAC. As part of the restructuring campaign, SASAC had requested Aviation Industry to dispose of all its real estate business.

In the course of contemplating the above-mentioned reorganisation, the Company has only considered the Target Group as a potential acquisition target due to the Company's interests in aviation business and the Target Group's demonstrated financial performance during the Track Record Period (details of which can be referred to accountant's report of the Target Company set out in Appendix III to this circular).

In connection with the Acquisition, the Company has engaged Euromonitor International Limited ("**Euromonitor**") to conduct an independent assessment of the aircraft piston engine manufacturing industry in the USA. According to the commissioned research report prepared by Euromonitor, the Target Group is one of the leading manufacturers of and services providers to general aviation aircraft piston engines worldwide. The Target Group has been in the piston aircraft engine manufacturing industry since the beginning of the growth of the dominating USA market for general aviation piston aircraft delivering its first certified aircraft engine in 1929 and its engine products have been used in the top 3 (in terms of fleet size) aircraft manufacturers of fixed wing piston powered aircraft, Beechcraft, Cessna, and Cirrus Aircraft since 1930. The Target Group stands apart from other major competitors in the field in its ability to produce engines ranging across market sectors dominated by its major competitors and in its capacities to produce both gasoline and diesel fuelled variations. The Target Group's history of innovation in diesel engine technology uniquely positions it to capture the market growth opportunities of general aviation both inside the USA and in the developing world. Certain clients use the diesel engines of the Target Group in their UAS aircrafts, while the market for UAS aircraft and technologies represents the most dynamic market for growth in aviation presently. With its main operations in the USA and Germany, the Target Group has established a manufacturing presence in both North America and Europe, the two regions of the world that presently account for more than 70% of the world market for piston engine powered aircraft.

The Target Group set up CMB in 2014 for product sales, service and distribution in PRC and plans further development to provide technology development and engineering support for the growing number of new OEM aircraft developers being established in PRC.

To further develop the general aviation industry in the PRC, the General Office of the State Council issued on 17 May 2016 the *Guidelines to Promote the Development of the General Aviation Industry (《國務院辦公廳關於促進通用航空業發展的指導意見》國辦發[2016]38號) ("**2016 Guideline**"),* proposing detailed measures for (i) fostering the general aviation market; (ii) accelerating the construction of airports for general aviation; (iii) promoting upgrades in the industry; (iv) widening the availability of low-altitude airspace; and (v) enhancing safety monitoring, with an aim of expanding the industry to have more than 500 airports, 5,000 aircrafts, and two million annual flight hours.

On top of the above policy, the *Civil Aviation Development 13th Five-Year Plan (中國民用航空發展第十三個五年規劃)* sets forth further proposals on the improvement of airport network and airport systems, and the expansion of the depth of aviatic infrastructure in the PRC by accelerating the development of passenger and cargo air transportation hubs, regional and international airports.

Given the governmental support mentioned above and the growing demand for aviation services in the PRC, the general aviation industry is likely to have a golden opportunity for development in future.

The Company believes that the Acquisition will provide an opportunity for the Group to capture the prospect of aviation industry, which will enable the Group to enhance the stability of revenue and cash flows and reduce the Group's reliance on property development in PRC which is undergoing a downward risk and subject to tightened government regulatory requirements.

Despite the fact that the US aircraft piston engine sales experienced a slight decline in 2016, the Directors recognise the Target Group's dominating position in the market (approximately 39.5% of the market share as estimated by Euromonitor. For details please refer to section headed "Appendix I — Information about the Target Group — 2. Industry Overview" to this circular), its overall ability in the research, design, manufacturing and sales of both gasoline and diesel fuelled engines which cover a broad range of horse power and have presence in not only the US and Europe but also emerging markets such as PRC (For details please refer to section headed "Appendix I — Information about the Target Group — 5. Business" to this circular) and its ability to achieve growth in revenue from approximately US$163.7 million for the FY2015 to US$204.3 million for the FY2016.

The Company is continuing to explore opportunities to dispose of the Group's real estate assets, including the Company's real estates in (i) Shahekou District of Dalian, PRC with total saleable area upon completion of 350,488 square metres and (ii) Chongqing with a total site area of approximately 375,252 square metres. As at the Latest Practicable Date, the Company has not yet entered into definitive terms for the proposed disposal.

Having considered the above, the Directors (excluding the non-executive Director and the independent non-executive Directors whose opinion is set out in the letter from the Code IBC and the letter from the LR IBC) believe that the Acquisition is in line with the development strategy of the Group and will facilitate the sustainable growth of the Group in the long run, and the terms of the Acquisition Agreement are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

(E) FINANCIAL IMPACT ON THE GROUP

Following Acquisition Completion, the Target Company will become a wholly-owned subsidiary of the Company and its accounts will be consolidated into the accounts of the Group. In light of the Target Group's past financial performance and market position, and the prospects of the piston engine industry, it is expected that the Target Group will contribute net operating cash inflows to the Enlarged Group.

Possible effect on earnings

For the FY2016, the Group's loss for the year attributable to owners of the parent was approximately HK$685.8 million. As presented in the unaudited pro forma consolidated statement of profit or loss of the Enlarged Group as set out in Appendix IV to this circular, had the Acquisition been completed on 1 January 2016, the Enlarged Group's loss for the year attributable to owners of the parent would have been approximately HK$318.3 million due to the profit of approximately HK$41.6 million contributed by the Target Company and pro-forma adjustments of approximately HK$325.9 million, details of which can be referred to Appendix IV to this circular.

Possible effect on net assets value

As of 30 June 2017, the Group's total assets and net assets value was approximately HK$5,909.0 million and HK$2,532.1 million respectively. As illustrated in the unaudited pro forma consolidated statement of financial position of the Enlarged Group set out in Appendix IV to this circular, had the Acquisition been completed on 30 June 2017, total assets of the Group as at 30 June 2017 would have been approximately HK$9,295.3 million and net assets value of the Group would have been approximately HK$4,372.8 million.

(F) FINANCIAL AND TRADING PROSPECTS OF THE ENLARGED GROUP

Upon Acquisition Completion, the Enlarged Group will be engaged in the manufacturing of and providing of services for general aviation aircraft piston engines, which enables the Enlarged Group to set up a potential growth business with a long-term return, enhance the stability of revenue and cash flows and reduce the Group's reliance on property development in PRC. This will enable the Enlarged Group to obtain equity and debt financing more easily, which will in turn enhance the Enlarged Group's profitability and facilitate further financing to develop its business so as to create value for its Shareholders. Upon Acquisition Completion, the Company intends to maintain the Target Group as a leading international aviation piston engine supplier by (i) retaining its current management team (see section headed "Appendix I — Information about the Target Group — 6. Directors and Senior Management" to this circular for their biographies); (ii) consolidating its market position in the US market; (iii) establishing its presence in the PRC and creating a strong brand name among Chinese OEMs and end users; (iv) focusing on technology development and introducing new products regularly; and (v) optimising its efficiency on sales, production and sourcing.

The Company and the Board are considering and continuing to explore opportunities to dispose of the Group's real estate business. As at the Latest Practicable Date, the Company has not yet entered into definitive terms for the proposed disposal. The Company intends to dispose of its real estate businesses by way of a public tender in the PRC and has conveyed such intention to certain potential purchasers, which are real estate development companies. But as at the Latest Practicable Date, no negotiation on the commercial terms of such proposed disposal has yet been commenced by the Company with any potential purchasers. The non-aviation trading business of the Group did not record any revenue in FY2016 and IH2017, and the Company intends to cease its operation in such business upon Acquisition Completion.

As disclosed in the Company's interim report for 1H2017, given that PRC is encouraging the development of its aviation industry, particularly the reform of low-altitude airspace management, the aero-technology related business is likely to have a golden opportunity for development in future. Upon Acquisition Completion, the Company will be well-positioned to seize the potential business opportunities available in the industry and benefit from the industrial development in future years.

As a result of the foregoing, and taking into account the unaudited pro forma financial information of the Enlarged Group contained in Appendix IV to this circular, the Directors are of the view that the Acquisition will improve the overall financial performance of the Company.

Save as disclosed above, AVIC HK has no intention to introduce any major changes in the business, including any redeployment of the fixed assets of the Group, and continued employment of the employees of the Company and of its subsidiaries.

Save as disclosed above, as at the Latest Practicable Date, the Company has no intention, negotiation, agreement, arrangement and understanding about acquiring any new business or injecting any new business into the Group.

(G) INFORMATION OF THE GROUP, AVIC INDUSTRY, AVIC INTERNATIONAL AND AVIC HK

The Company is a company incorporated in Bermuda with limited liability, the shares of which are listed on the main board of the Stock Exchange (stock code: 232). The Group's principal business activities include: (a) property development and investment business; and (b) trading business. During the year ended 31 December 2016, the Group disposed of a 51%-owned subsidiary to an independent third party and ceased its knitting and textile business because it had been loss-making in recent years.

Aviation Industry is a state-owned enterprise (全民所有制企業) established in the PRC and is wholly-owned by SASAC. Aviation Industry's core businesses consist of defense, transport aircraft, helicopter, avionics and systems, general aviation, aviation research and development, flight testing, trade and logistics, assets management, finance services, engineering and construction, automobile etc.

AVIC International is controlled by Aviation Industry. As the comprehensive platform under Aviation Industry, AVIC International's core businesses consist of international aviation, electronic high technology, international business, modern services, trade and bulk commodities, real estate and property services. As at the Latest Practicable Date, AVIC International is owned as to 62.52% by Aviation Industry, 14.31% by National Council for Social Security Fund (全國社會保障基金理事會), 14.31% by Beijing Plateau Hanhua Equity Investment Fund (limited partnership) (北京普拓瀚華股權投資基金合夥企業(有限合夥)) and 8.86% by AVIC CCB Aviation Industry Equity Investment

(Tianjin) Co., Ltd. (中航建銀航空產業股權投資(天津)有限公司). On 6 September 2016, Aviation Industry and Poly Group reached a preliminary intention for cooperation in respect of the acquisition of Aviation Industry's real estate development business and assets by Poly Group. As at the Latest Practicable Date and to the best knowledge of the Company, Poly Group was not a Shareholder.

AVIC HK is an investment holding company incorporated in Hong Kong with limited liability and a direct wholly-owned subsidiary of AVIC International as at the Latest Practicable Date.

(H) LISTING RULES IMPLICATIONS

As (i) Mr. Liu Hongde, Mr. Lai Weixuan and Ms. Zhou Chunhua are directors of AVIC International, (ii) Mr. Xu Hongge is a director of a subsidiary of AVIC International and (iii) Mr. Pan Linwu is a director of the Target Company, each of Mr. Liu Hongde, Mr. Lai Weixuan, Ms. Zhou Chunhua, Mr. Xu Hongge and Mr. Pan Linwu abstained from voting on the resolutions at the meeting of the Board for approving the Acquisition Agreement.

As the highest applicable percentage ratios calculated pursuant to Chapter 14 of the Listing Rules in respect of the Acquisition exceeds 100% and AVIC HK (as a wholly-owned subsidiary of AVIC International, the controlling Shareholder) is a connected person of the Company, the Acquisition constitutes a very substantial acquisition and connected transaction of the Company. Accordingly, the Acquisition is subject to the reporting, announcement and Independent Shareholders' approval requirements of the Listing Rules.

(I) TAKEOVERS CODE IMPLICATIONS AND APPLICATION FOR WHITEWASH WAIVER

As at the Latest Practicable Date, the issued share capital of the Company comprises 5,519,591,000 Shares and the Company does not have any options, warrants or convertible securities in issue. As at the Latest Practicable Date, the Concert Group owns/has control or direction over 1,895,715,000 Shares, which represented approximately 34.35% of the issued share capital of the Company. Other than the entering into of the Acquisition Agreement, none of the members of the Concert Group have acquired or disposed of or entered into any agreement or arrangement to acquire or dispose of any voting rights in the Company within the six months prior to 19 September 2017, being the date of the first announcement made by the Company in relation to the Acquisition.

Upon Acquisition Completion, 3,783,783,783 Shares, representing approximately 40.67% of the issued share capital of the Company as enlarged by the issue of the Consideration Shares, will be issued to AVIC HK. As the Acquisition will increase the Concert Group's collective holding of voting rights of the Company by more than 2%, in the absence of the Whitewash Waiver, AVIC HK would be under an obligation to make a mandatory general offer for all the Shares not already owned or agreed to be acquired by the Concert Group pursuant to the Takeovers Code as a result of the issue of Consideration Shares.

An application to the Executive for the Whitewash Waiver has been made by AVIC HK pursuant to Note 1 on dispensations from Rule 26 of the Takeovers Code. The Executive may or may not grant the Whitewash Waiver. If the Whitewash Waiver is not granted, the Acquisition Agreement will lapse and the Acquisition will not proceed. The Whitewash Waiver, if granted, would be subject to, among other things, the approval of the Independent Shareholders at the SGM by way of poll.

If the Whitewash Waiver is approved by the Independent Shareholders, upon the issue of the Consideration Shares to AVIC HK (and assuming there is no other change to the issued share capital of the Company), the interest of the Concert Group in the Company will exceed 50%. The Concert Group may further increase their shareholdings in the Company without incurring any further obligations under Rule 26 of the Takeovers Code to make a general offer.

(G) LISTING COMMITTEE'S DECISION

The Listing Committee has determined that the Acquisition is an extreme very substantial acquisition and the reverse takeover rules would not apply. The Company is required to prepare a transaction circular under an enhanced disclosure comparable to prospectus standard and Anglo Chinese Corporate Finance, Limited has been appointed as the financial adviser of the Company to conduct due diligence on the Acquisition.

III. CONTINUING CONNECTED TRANSACTION

(A) THE SALE FRAMEWORK AGREEMNT

Background

On 24 October 2017, the Company entered into the Sale Framework Agreement with Aviation Industry, pursuant to which subsequent to Acquisition Completion, the Group will sell engines and engine parts to Aviation Industry and/or its associates (excluding the Group and the Target Group) for use in new aircraft manufacture and the sale of parts into the aftermarket for maintenance, repair and overhaul.

Details of the Sale Framework Agreement

Date:	24 October 2017
Parties:	Aviation Industry and the Company
Subject:	Subsequent to Acquisition Completion, the Group will sell engines and engine parts to Aviation Industry and/or its associates (excluding the Group and the Target Group) for use in new aircraft manufacture and the sale of parts into the aftermarket for maintenance, repair and overhaul
Term:	From the Effective Date up to 31 December 2019
Pricing:	To be determined on a fair and reasonable basis based on the published price list and discounts provided based on factors including, but not limited to, volume levels
Payment:	Specific payment terms (including time and method of payment) are to be agreed between the parties by entering into specific agreement in each sale transaction

Conditions precedent:

(a) the due execution of the Sale Framework Agreement by the Company and Aviation Industry; and

(b) the Sale Framework Agreement and the transactions contemplated thereunder having been approved by the Board and having obtained all necessary authorisations and approvals (including, if necessary, approval from Independent Shareholders by way of poll at a general meeting) from the Stock Exchange and other relevant laws, regulations and rules (including the Listing Rules)

(B) HISTORICAL FIGURES, ANNUAL CAPS AND BASIS OF DETERMINATION

The Target Group has been selling engines and engine parts for use in new aircraft manufacture and the sale of parts into the aftermarket for maintenance, repair and overhaul to Aviation Industry and/or its associates (excluding the Group and the Target Group). Historical transaction amounts for such sales to Aviation Industry and/or its associates during the Track Record Period were as follows:

	For the year ended 31 December			**For the six months ended 30 June**
	2014	**2015**	**2016**	**2017**
	USD million	*USD million*	*USD million*	*USD million*
Actual historical transaction amount	21.2	19.1	20.0	8.4

Pursuant to the Sale Framework Agreement, it is proposed that the annual cap amounts for the sale of engine and engine parts to Aviation Industry and its associates (excluding the Group and the Target Group) for each of the three financial years ending 31 December 2017, 2018 and 2019 does not exceed the following:

	For the year ending 31 December		
	2017	**2018**	**2019**
	USD million	*USD million*	*USD million*
Annual cap	20.0(Note 1)	22.0	24.0

Note 1: The proposed annual cap is for the full year ending 31 December 2017.

The above annual caps were determined mainly by reference to: (i) the actual historical transaction amount for each of the three financial years ended 31 December 2016; and (ii) an adequate buffer for a potential increase in demand by Aviation Industry and/or its associates (excluding the Group and the Target Group).

(C) Pricing of products and control mechanism of the Company

The price lists of OEM and aftermarket products of the Target Group are set annually. The price lists are determined based on established benchmarks, such as producer price index, customer price index, labour costs and material costs, and are adjusted with reference to the price lists of prior year. Price lists of products are published either on the Target Group's website or available on request. In determining the discounts (if any) to be given to its customers, the Target Group will take into account factors, including but not limited to, the volume levels and scale of operation of customers.

The Company has formulated internal control measures and procedures in order to ensure the pricing mechanism and the terms of the transactions under the Sale Framework Agreement are fair and reasonable and no less favourable to the Company than the terms available to or from independent third parties, and in the interest of the Company and its Shareholders as a whole. A control mechanism to segregate duties to notify and review connected transactions has been set up within the Group. After the Acquisition Completion, the Target Group will need to report connected transactions monthly to the company secretary and financial department of the Company, and for each new transaction with Aviation Industry and/or its associates, the Target Group will be required to report and compare the terms, including but not limited to price and/or gross profit margin, of the transactions with those for products with similar features offered by the Target Group to independent third parties and obtain approval from the chief executive officer of the Company.

Further, the Company will comply with all relevant requirements under the Listing Rules which include the annual review and/or confirmation by the independent non-executive Directors and auditors of the Company on the actual execution of the transactions contemplated under the Sale Framework Agreement.

(D) REASON FOR AND BENEFITS OF THE SALE FRAMEWORK AGREEMENT

There is a historical connection and long-term cooperation relationship between the Target Group and Aviation Industry and/or its associates. The Target Group has historically been selling engines and engine parts to Aviation Industry and/or its associates, such as Cirrus Design Corporation, for use in new aircraft manufacture and for the sale of parts into the aftermarket for maintenance, repair and overhaul and will continue to do so on an ongoing basis. Such transactions are and will be conducted in the ordinary and usual course of business of the Target Company upon Acquisition Completion, and will continue to be agreed on an arm's length basis with terms that are fair and reasonable to the Company. Cirrus Design Corporation, which is indirectly owned as to 70% by Aviation Industry, is the world's largest producer of piston-powered aircraft by shipments located in the United States. Also, with the growth in the PRC general aviation industry in recent years and the intentions of the PRC government in encouraging the development of such industry, the Company, upon Acquisition Completion, will be able to seize the potential business opportunities available in such industry and benefit from the industrial development in future years. The Company considers that it is in its best interest to continue the business relationship between the Target Group and Aviation Industry and/or its associates upon Acquisition Completion, provided that such parties will purchase from the Target Group at prices comparable to market prices and are considered to be fair and reasonable to the Group. The Company therefore entered into the Sale Framework Agreement with Aviation Industry to govern such sales that are expected to continue upon Acquisition Completion.

The Directors (excluding the independent non-executive Directors whose opinion is set out in the letter from the LR IBC) consider that the Sale Framework Agreement has been entered into on normal commercial terms and in the ordinary and usual course of business of the Group, and the Sale Framework Agreement and its proposed annual caps are fair and reasonable and in the interests of the Group and the Shareholders as a whole.

(E) IMPLICATIONS UNDER THE LISTING RULES

Aviation Industry and its associates are connected persons of the Company under Chapter 14A of the Listing Rules. As disclosed in the Acquisition Announcement, upon Acquisition Completion, the Target Company will become a wholly-owned subsidiary of the Company, therefore ongoing transactions between the Target Group and Aviation Industry and/or its associates that are expected to continue after Acquisition Completion will constitute continuing connected transactions of the Company under the Listing Rules.

As the highest applicable percentage ratio for the transactions pursuant to the Sale Framework Agreement is more than 5%, the Sale Framework Agreement constitutes a non-exempt continuing connected transaction for the Company under Chapter 14A of the Listing Rules and is therefore subject to reporting, announcement and independent shareholders' approval requirements.

As (i) Mr. Liu Hongde, Mr. Lai Weixuan and Ms. Zhou Chunhua are directors of AVIC International, (ii) Mr. Xu Hongge is a director of a subsidiary of AVIC International and (iii) Mr. Pan Linwu is a director of the Target Company, each of Mr. Liu Hongde, Mr. Lai Weixuan, Ms. Zhou Chunhua, Mr. Xu Hongge and Mr. Pan Linwu abstained from voting on the resolutions at the meeting of the Board for approving the Sale Framework Agreement.

IV. THE CLAWBACK OFFER BY AVIC HK

Conditional upon and subject to the Acquisition Completion, in order to provide Qualifying Shareholders the opportunity to further participate in and share the growth of the Company and at least to maintain their shareholdings without being diluted by the Acquisition, AVIC HK will offer initially not more than 2,484,166,998 Offer Shares, which constitute approximately 65.65% of the Consideration Shares, approximately 45.01% of the issued share capital of the Company as at the Latest Practicable Date and approximately 26.70% of the issued share capital of the Company as enlarged by the allotment and issue of the Consideration Shares, to the Qualifying Shareholders on a pro rata basis of 0.6855 Offer Share for every one Share held as at the close of business on the Record Date at HK$0.37 per Offer Share, which is equal to the issue price of the Consideration Shares pursuant to the Acquisition Agreement, the details of which are as set out below.

As the Offering is conditional upon Acquisition Completion, the Offering may or may not proceed. Shareholders should exercise caution when dealing in the Shares of the Company.

Principal Terms of the Offering:

Number of Offer Shares:	Initially not more than 2,484,166,998 Shares and will be adjusted upwards for any increase in the number of Shares held by the Qualifying Shareholders up to, and including the Record Date based on the Offering ratio as set out in the paragraph headed "Assured Entitlement" below.
Offer Price:	HK$0.37 per Offer Share (being determined with reference to the average closing price of the Shares for the 30 trading days up to and including the Last Trading Day) as quoted on the Stock Exchange, which is equal to the issue price of the Consideration Shares pursuant to the Acquisition Agreement, excluding applicable fees, levies and buyer's ad valorem stamp duty at a rate of 0.1% payable by the Qualifying Shareholders.
Assured Entitlement:	Shareholders will be entitled to apply on the basis of 0.6855 Offer Share for every one existing Share held as at the close of business on the Record Date. A Qualifying Shareholder will be entitled to apply for a number of Offer Shares which is equal to or less than or in excess of his or her Assured Entitlement (subject to a minimum of 100 Offer Shares). The Assured Entitlement of each Qualifying Shareholder will be rounded down to the nearest whole number of Offer Shares, such that no fractional Share will be offered. No odd lot matching services will be provided by AVIC HK in respect of the Offering.
Transferability:	The Assured Entitlements of the Qualifying Shareholders to the Offer Shares are not transferable or capable of renunciation and there will be no trading in nil-paid entitlements on the Stock Exchange. Any Offer Share not purchased or taken up by the Qualifying Shareholders will be available for excess application by other Qualifying Shareholders.
Status of the Offer Shares:	The Offer Shares to be sold under the Offering shall be fully-paid and rank *pari passu* in all respects with the existing Shares, free from all liens, charges, encumbrances, pre-emptive rights and any other third party rights of any nature and together with all rights attaching to them, including the right to receive in full all dividends and other distributions, if any, declared, made or paid on or after the date of the issuance of the Consideration Shares.

Excess Application:	Qualifying Shareholders are entitled to apply for Offer Shares offered but not taken up. Application is made by completing the excess application form which will accompany the Prospectus. The directors of AVIC HK will allocate the excess Offer Shares at their discretion on a fair and reasonable basis and as far as practicable on a pro rata basis by reference to the number of excess Offer Shares applied for under each application. No preference will be given to topping up odd lots to whole board lots.
Qualifying Shareholders:	All Code Independent Shareholders whose names appear on the register of members of the Company as at the close of business on the Record Date, other than the Overseas Shareholders whom the directors of the Company and AVIC HK, after making relevant enquiries, consider it necessary or expedient to exclude from the Offering on account either of the legal restrictions under the laws of the relevant place or the requirements of the relevant regulatory body or stock exchange in that place.
Condition:	The Offering is conditional upon Acquisition Completion. If Acquisition Completion does not take place on or before 31 March 2018 or such later date as may be announced by the Company, the Offering will lapse and any applications made by the Qualifying Shareholders for the Offer Shares pursuant to the Offering will be rejected.

Offering Arrangement

Given the Offering involves the offer of the Shares to the Qualifying Shareholders on a pro rata basis to enable the Qualifying Shareholders to further participate in and share the growth of the Company, the Prospectus will be issued by the Company and AVIC HK jointly. The Company will provide administrative assistance that would be necessary and expedient for implementing the Offering, e.g. the closure of the register of members in order to determine the Assured Entitlements of the Qualifying Shareholders, and the despatch of the Prospectus and the application forms through the Company's branch share registrars and transfer office. The costs and expenses arising from the implementation of the Offering will be borne by AVIC HK. AVIC HK will be primarily responsible for the preparation of the Prospectus and other documentations in relation to the Offering and the Company will provide reasonable assistance to AVIC HK to ensure the accuracy and sufficiency of information contained in the Prospectus and other documentations in relation to the Offering.

Expected Timetable

An indicative timetable of the Offering is set out as follows:

Date of the SGM and the announcement of the SGM poll results	Tuesday, 23 January 2018
Last day for trading in Shares with the Assured Entitlements	Wednesday, 24 January 2018
First day for trading in Shares without the Assured Entitlements	Thursday, 25 January 2018
Latest time to lodge completed transfer forms and the relevant share certificates in order to qualify for the Assured Entitlements	4:30 p.m., Friday, 26 January 2018
Book closure period in relation to the Offering	From Monday, 29 January 2018 to Tuesday, 30 January 2018 (both dates inclusive)
Record Date	Tuesday, 30 January 2018
Acquisition Completion/issue of Consideration Shares	Wednesday, 31 January 2018
Register of members of the Company reopens	Wednesday, 31 January 2018
Despatch of the Prospectus and forms of acceptance	Monday, 5 February 2018
Offer period	From Tuesday, 6 February 2018 to Wednesday, 21 February 2018 (both dates inclusive)
Latest time for lodging applications and payments for the Offer Shares	4:00 p.m., Wednesday, 21 February 2018
Announcement of the results of the Offering	Wednesday, 7 March 2018
Despatch share certificates of the Offer Shares	Thursday, 15 March 2018
Dealings in the Offer Shares commence	9:00 a.m., Friday, 16 March 2018

Note: This assumes the Independent Shareholders have approved the Acquisitions at the SGM and the Stock Exchange has granted the approval for the listing of, and permission to deal in, the Consideration Shares.

All times in this circular refer to Hong Kong time. Dates stated for events mentioned in the timetable above are indicative only and may be extended or varied. Any changes to the expected timetable for the Offering will be announced as appropriate.

Closure of register of members in relation to the Offering

The register of members of the Company will be closed from Monday, 29 January 2018 to Tuesday, 30 January 2018, both dates inclusive, for the purposes of establishing the Assured Entitlements of the Qualifying Shareholders on the Record Date. During this period, no transfer of Shares will be registered. In order to qualify for the Assured Entitlements, all transfers of Shares, accompanied by the relevant share certificates must be lodged with the Company's branch share registrars and transfer office in Hong Kong, Computershare Hong Kong Investor Services Limited at Rooms 1712-1716, 17/F, Hopewell Centre, 183 Queen's Road East, Hong Kong, for registration not later than 4:30 p.m. on Friday, 26 January 2018.

V. EFFECT OF THE ACQUISITION AND OFFERING ON THE SHAREHOLDING STRUCTURE OF THE COMPANY

The issue of the Consideration Shares will not result in a change of control of the Company. For illustration purpose only, assuming that (i) there will be no change in the issued share capital of the Company and the Shares held by AVIC HK and its associates between the Latest Practicable Date and completion of the Offering, save for the allotment and issue of the Consideration Shares and the transfer of the Offer Shares by AVIC HK; and (ii) the initial 2,484,166,998 Offer Shares are fully accepted by the Qualifying Shareholders, the table below sets out the shareholding structure of the Company as at the Latest Practicable Date, immediately upon Acquisition Completion, and immediately upon completion of the Offering:

	As at the Latest Practicable Date		Immediately upon Acquisition Completion		Immediately upon completion of the Offering	
	No. of Shares	**Approximate % of the issued share capital of the Company**	**No. of Shares**	**Approximate % of the issued share capital of the Company**	**No. of Shares**	**Approximate % of the issued share capital of the Company**
The Concert Group	1,895,715,000	34.35%	5,679,498,783	61.05%	3,195,331,785	34.35%
- Tacko International Limited	1,895,559,000	34.34%	1,895,559,000	20.37%	1,895,559,000	20.37%
- AVIC HK	0	0.00%	3,783,783,783	40.67%	1,299,616,785	13.97%
- Mr. Li Shangfu (a director of AVIC International)	156,000	0.00%	156,000	0.00%	156,000	0.00%
CK Hutchison Holdings Limited	450,000,000	8.15%	450,000,000	4.84%	758,475,000	8.15%
Other public Shareholders	3,173,876,000	57.50%	3,173,876,000	34.11%	5,349,567,998	57.50%
Total	**5,519,591,000**	**100.00%**	**9,303,374,783**	**100.00%**	**9,303,374,783**	**100.00%**

On the aforesaid assumption, 2,484,166,998 Offer Shares represent approximately 26.70% of the issued share capital of the Company as enlarged by the issue of the Consideration Shares on the Record Date. If the public float of the Company falls below the minimum requirement of 25% upon completion of the Offering, the Company will use its best endeavour to restore sufficient public float by conducting placing of new Shares to independent third party investors.

VI. RE-ELECTION OF DIRECTOR

In accordance with the Company's Bye-law 102(B), any Director appointed by the Board to fill a casual vacancy shall hold office only until the next following general meeting of the Company and shall then be eligible for re-election at that meeting. On 26 May 2017, Mr. Zhang Ping was appointed as an independent non-executive Director to fill a vacancy and he shall hold office until the SGM and be subject to re-election at such meeting. The particulars of Mr. Zhang Ping are set out in Appendix VI to this circular.

VII. SGM

A notice of SGM to be held at Monaco Room, Basement 1, Regal Hongkong Hotel, 88 Yee Wo Street, Causeway Bay, Hong Kong, on Tuesday, 23 January 2018 at 3:00 p.m. is set out on pages SGM-1 to SGM-3 of this circular for the purpose of considering and, if thought fit, approving the Acquisition Agreement and the transactions contemplated thereunder, the Whitewash Waiver, the Sale Framework Agreement and the re-election of Director.

A proxy form for use at the SGM is enclosed. Whether or not you intend to attend the SGM, you are requested to complete the accompanying proxy form in accordance with the instructions printed thereon and return the same to the branch share registrar and transfer office of the Company in Hong Kong, Computershare Hong Kong Investor Services Limited at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong as soon as possible but in any event not less than 48 hours before the time appointed for the holding of the SGM or any adjournment thereof. Completion and return of the proxy form shall not preclude you from attending and voting in person at the SGM or any adjournment thereof if you so desire and, in such event, the instrument appointing a proxy shall be deemed to be revoked.

As at the Latest Practicable Date, the Concert Group is interested in 1,895,715,000 Shares, representing approximately 34.35% of the total number of Shares in issue. The Concert Group is required to abstain from voting on the proposed resolutions to approve the Acquisition Agreement and the transactions contemplated thereunder and the Whitewash Waiver at the SGM. As at the Latest Practicable Date, Aviation Industry and its associates are interested in 1,895,559,000 Shares, representing approximately 34.34% of the total number of Shares in issue. In view of the interests of Aviation Industry in the Sale Framework Agreement, Aviation Industry and its associates will be required to abstain from voting in relation to the Sale Framework Agreement and the transactions contemplated thereunder at the SGM. Save for the aforesaid and to the best knowledge of the Company, as at the Latest Practicable Date, no other Shareholder has a material interest or was involved in the Acquisition Agreement and the transactions contemplated thereunder, the

Whitewash Waiver, the Sale Framework Agreement and the transactions contemplated thereunder and the re-election of Director, and therefore no other Shareholder is required to abstain from voting on the proposed resolutions to approve the Acquisition Agreement and the transactions contemplated thereunder, the Whitewash Waiver, the Sale Framework Agreement and the re-election of Director.

Pursuant to Rules 13.39(4) and 13.39(5) of the Listing Rules, the resolutions proposed to be approved at the SGM will be taken by poll and an announcement will be made by the Company on the results of the SGM.

VIII. RECOMMENDATION

Your attention is drawn to (i) the letter from the Code IBC dated 29 December 2017 on pages 32 to 33 of this circular and the letter from the LR IBC dated 29 December 2017 on pages 34 to 35 of this circular, which set out the recommendation from the Code IBC to Code Independent Shareholders on the Acquisition and the Whitewash Waiver and the recommendation from LR IBC to LR Independent Shareholders on the Acquisition and the Sale Framework Agreement; and (ii) the letter from Somerley which contains its advice to the Independent Board Committees and the Independent Shareholders in respect of the Acquisition, Whitewash Waiver and the Sale Framework Agreement.

The Directors (including the members of the Independent Board Committees) consider that the Acquisition Agreement and the transactions contemplated thereunder, the Whitewash Waiver and the Sale Framework Agreement and the transactions contemplated thereunder are fair and reasonable, on normal commercial terms and in the interests of the Company and the Shareholders as a whole, and the re-election of Director is in the interests of the Company and the Shareholders as a whole. Accordingly, the Directors recommend that the Independent Shareholders should vote in favour of all the proposed resolutions set out in the notice of the SGM.

IX. ADDITIONAL INFORMATION

Your attention is also drawn to the information set out in the appendices to this circular.

Yours faithfully,
For and on behalf of the Board
AVIC International Holding (HK) Limited
Liu Hongde
Chairman

The following is the text of a letter from the Code IBC to the Code Independent Shareholders in connection with the Acquisition and Whitewash Waiver for inclusion in this circular.

AVIC International Holding (HK) Limited
中國航空工業國際控股(香港)有限公司
(Incorporated in Bermuda with limited liability)
(Stock Code: 232)

29 December 2017

To the Code Independent Shareholders

Dear Sir or Madam,

VERY SUBSTANTIAL ACQUISITION AND CONNECTED TRANSACTION APPLICATION FOR WHITEWASH WAIVER

We refer to the circular dated 29 December 2017 of the Company of which this letter forms part (the "**Circular**"). Capitalised terms defined in the Circular shall have the same meaning herein unless the context otherwise requires.

We have been authorised by the Board to form the Code IBC to consider and advise the Code Independent Shareholders in respect of the Acquisition and Whitewash Waiver, details of which are set out in the section headed "Letter from the Board" contained in the Circular.

We wish to draw your attention to the letter from the Board set out on pages 8 to 31 of the Circular and the letter of advice from Somerley, the Independent Financial Adviser appointed to advise the Independent Board Committees and the Independent Shareholders on the terms of the Acquisition Agreement and the Whitewash Waiver, set out on pages 36 to 83 of the Circular.

Having considered, among other matters, the factors and reasons considered by, and the opinion of Somerley as stated in its letter of advice, the terms and conditions of the Acquisition Agreement and the Whitewash Waiver, the business and financial effects of the Acquisition on the Company, the quality and size of the business of the Target Group and the effect of the Acquisition on the Group, we consider that the terms and conditions of the Acquisition Agreement and Whitewash Waiver are fair and reasonable and on normal commercial terms, and in the interests of the Company and the Shareholders as a whole.

Accordingly, we recommend the Code Independent Shareholders to vote in favour of the resolution(s) to be proposed at the SGM in respect of the Acquisition Agreement and the transactions contemplated thereunder and the Whitewash Waiver.

Yours faithfully,

The Code IBC

AVIC International Holding (HK) Limited

Mr. Chow Wai Kam
Non-executive Director

Mr. Chu Yu Lin, David **Mr. Li Ka Fai, David** **Mr. Zhang Ping**
Independent non-executive Directors

The following is the text of a letter from the LR IBC to the LR Independent Shareholders in connection with the Acquisition and the Sale Framework Agreement for inclusion in this circular.

AVIC International Holding (HK) Limited
中國航空工業國際控股(香港)有限公司
(Incorporated in Bermuda with limited liability)
(Stock Code: 232)

29 December 2017

To the LR Independent Shareholders

Dear Sir or Madam,

VERY SUBSTANTIAL ACQUISITION AND CONNECTED TRANSACTION APPLICATION FOR WHITEWASH WAIVER

CONTINUING CONNECTED TRANSACTION

We refer to the circular dated 29 December 2017 of the Company of which this letter forms part (the "**Circular**"). Capitalised terms defined in the Circular shall have the same meaning herein unless the context otherwise requires.

We have been authorised by the Board to form the LR IBC to consider and advise the LR Independent Shareholders in respect of the Acquisition and the Sale Framework Agreement, details of which are set out in the section headed "Letter from the Board" contained in the Circular.

We wish to draw your attention to the letter from the Board set out on pages 8 to 31 of the Circular and the letter of advice from Somerley, the Independent Financial Adviser appointed to advise the Independent Board Committees and the Independent Shareholders on the terms of the Acquisition Agreement, the Whitewash Waiver and the Sale Framework Agreement, set out on pages 36 to 83 of the Circular.

Having considered, among other matters, the factors and reasons considered by, and the opinion of Somerley as stated in its letter of advice, the terms and conditions of the Acquisition Agreement and the Sale Framework Agreement, the business and financial effects of the Acquisition on the Company, the quality and size of the business of the Target Group and the effect of the Acquisition on the Group, we consider that (i) though the entering into the Acquisition Agreement is not in the ordinary and usual course of business of the Group, the terms and conditions of the Acquisition Agreement are fair and reasonable and on normal commercial terms, and in the interests of the Company and the Shareholders as a whole; and (ii) the entering into the Sale Framework Agreement and the transactions contemplated thereunder is in the ordinary and usual course of business of the Group, the terms and conditions of the Sale Framework are fair and reasonable and on normal commercial terms, and in the interests of the Company and the Shareholders as a whole.

Accordingly, we recommend the LR Independent Shareholders to vote in favour of the resolution(s) to be proposed at the SGM in respect of the Acquisition Agreement and the transactions contemplated thereunder and the Sale Framework Agreement and the transactions contemplated thereunder.

Yours faithfully,

The LR IBC

AVIC International Holding (HK) Limited

Mr. Chu Yu Lin, David **Mr. Li Ka Fai, David** **Mr. Zhang Ping**
Independent non-executive Directors

The following is the letter of advice from Somerley Capital Limited to the Independent Board Committees and the Independent Shareholders, which has been prepared for the purpose of inclusion in this circular.

SOMERLEY CAPITAL LIMITED
20th Floor
China Building
29 Queen's Road Central
Hong Kong

29 December 2017

To: the Independent Board Committees and
the Independent Shareholders

Dear Sirs,

(1) VERY SUBSTANTIAL ACQUISITION AND CONNECTED TRANSACTION; (2) APPLICATION FOR WHITEWASH WAIVER; AND (3) CONTINUING CONNECTED TRANSACTIONS

INTRODUCTION

We refer to our appointment to advise the Independent Board Committees and the Independent Shareholders in relation to the Acquisition, the Whitewash Waiver and the Sale Framework Agreement (the "**Continuing Connected Transactions**"). Details of them are set out in the circular of the Company dated 29 December 2017 (the "**Circular**"), of which this letter forms part. Unless otherwise defined, capitalised terms used in this letter shall have the same meanings as those defined in the Circular.

On 19 September 2017 (after trading hours), the Company (as purchaser) entered into the Acquisition Agreement with AVIC HK (as seller) and AVIC International (as seller guarantor), pursuant to which AVIC HK has agreed to sell and the Company agreed to acquire (i) the entire issued share capital of the Target Company; and (ii) the shareholder's loan note(s) owing by the Target Company to AVIC HK at Acquisition Completion, at an aggregate consideration of HK$2,400,000,000 (the "**Consideration**"), out of which HK$1,000,000,000 will be satisfied by cash and HK$1,400,000,000 will be satisfied by way of allotment and issue of the Consideration Shares to AVIC HK. On 27 October 2017, AVIC International, AVIC HK and the Company entered into the Amendment Deed to amend the payment terms regarding the final payment of HK$800,000,000 of the Consideration.

As the highest applicable percentage ratio calculated pursuant to Chapter 14 of the Listing Rules in respect of the Acquisition exceeds 100% and AVIC HK (as a wholly-owned subsidiary of AVIC International, which is owned as to 62.52% by Aviation Industry, the controlling shareholder of the Company) is a connected person of the Company, the Acquisition constitutes a very substantial acquisition and connected transaction of the Company. Accordingly, the Acquisition is subject to the reporting, announcement and Independent Shareholders' approval requirements under Chapter 14A of the Listing Rules.

As at the Latest Practicable Date, the Concert Group is interested in 1,895,715,000 Shares in aggregate, representing approximately 34.35% of issued share capital of the Company. Following the allotment and issue of the Consideration Shares, the shareholding of the Concert Group will increase to approximately 61.05% of issued share capital of the Company as enlarged by the allotment and issue of the Consideration Shares. As the Acquisition will increase the Concert Group's collective holding of voting rights of the Company by more than 2%, AVIC HK would be, in the absence of the Whitewash Waiver, under an obligation to make a mandatory general offer for all the Shares not already owned or agreed to be acquired by the Concert Group pursuant to Rule 26 of the Takeovers Code. In this regard, an application to the Executive for the Whitewash Waiver has been made by AVIC HK pursuant to Note 1 on dispensations from Rule 26 of the Takeovers Code. The Whitewash Waiver, if granted by the Executive, will be subject to, among other things, the approval of the Independent Shareholders at the SGM by way of poll.

The Concert Group and the Shareholders who are involved or interested in the Acquisition and the Whitewash Waiver shall be required to abstain from voting in respect of the resolution to approve the Acquisition and the Whitewash Waiver at the SGM.

On 24 October 2017, the Company entered into the Sale Framework Agreement with Aviation Industry, pursuant to which, subsequent to Acquisition Completion, the Group will continue to sell engines and engine parts to Aviation Industry and/or its associates (excluding the Group and the Target Group) for use in new aircraft manufacturing and will sell parts in the aftermarket for maintenance, repair and overhaul. Upon Acquisition Completion, the Target Company will become a wholly-owned subsidiary of the Company and Aviation Industry is the controlling shareholder of the Company and hence a connected person of the Company. Accordingly, the transactions pursuant to the Sale Framework Agreement will constitute continuing connected transactions of the Company under the Listing Rules upon Acquisition Completion. As the highest applicable percentage ratio for the transactions pursuant to the Sale Framework Agreement under Rule 14.07 of the Listing Rules is more than 5%, the transactions contemplated under the Sale Framework Agreement constitute non-exempt continuing connected transactions for the Company under Chapter 14A of the Listing Rules and is therefore subject to reporting, announcement and independent shareholders' approval requirements.

As (i) Mr. Liu Hongde, Mr. Lai Weixuan and Ms. Zhou Chunhua are directors of AVIC International; (ii) Mr. Xu Hongge is a director of a subsidiary of AVIC International; and (iii) Mr. Pan Linwu is a director of the Target Company, each of Mr. Liu Hongde, Mr. Lai Weixuan, Ms. Zhou Chunhua, Mr. Xu Hongge and Mr. Pan Linwu abstained from voting on the resolutions at the meeting of the Board for approving the Sale Framework Agreement. Aviation Industry and its associates will also be required to abstain from voting in relation to the resolution to approve the Sale Framework Agreement and the transactions contemplated thereunder at the SGM.

The LR IBC of the Company comprising all the independent non-executive Directors, namely Mr. Chu Yu Lin, David, Mr. Li Ka Fai, David and Mr. Zhang Ping, has been established by the Company to advise the Independent Shareholders on the terms of the Acquisition, the terms and annual caps in respect of the Sale Framework Agreement. The Code IBC comprising all the independent non-executive Directors, namely Mr. Chu Yu Lin, David, Mr. Li Ka Fai, David and Mr. Zhang Ping, and the sole non-executive Director, namely Mr. Chow Wai Kam, has been established by the Company to advise the Independent Shareholders on the terms of the Acquisition and the Whitewash Waiver. The Independent Board Committees have approved our appointment as the Independent Financial Adviser to advise the Independent Board Committees and the Independent Shareholders in these regards.

We are not associated or connected with the Company, its directors, its controlling shareholder or any party acting, or presumed to be acting, in concert with any of them and accordingly, we are considered eligible to give independent advice to (i) the LR IBC and the Independent Shareholders on the terms of the Acquisition, the terms and annual caps in respect of the Sale Framework Agreement; and (ii) the Code IBC and the Independent Shareholders on the Acquisition and the Whitewash Waiver.

As at the Latest Practicable Date, Somerley Capital Limited does not have any relationships or interests with the Company that could reasonably be regarded as relevant to the independence of Somerley Capital Limited. In the last two years, there has been no engagement between the Company and Somerley Capital Limited. Apart from normal professional fees paid or payable to us in connection with this appointment as the Independent Financial Adviser, no arrangement exists whereby we will receive any fees or benefits from the Company, its directors, its controlling shareholder or any of their respective substantial shareholders or any party acting, or presumed to be acting, in concert with any of them. Accordingly, we do not consider any conflict of interest arises for Somerley Capital Limited in acting as the Independent Financial Adviser of the Acquisition, the Whitewash Waiver and the Sale Framework Agreement.

In formulating our advice, we have reviewed, among other things, the Acquisition Agreement, the Sale Framework Agreement, the annual reports of the Company for the years ended 31 December 2014, 31 December 2015 and 31 December 2016 (the "**2014 Annual Report**", "**2015 Annual Report**" and "**2016 Annual Report**", together the "**Annual Reports**"), the interim report of the Company for the six months ended 30 June 2017 (the "**Interim Report**") and the information as set out in the Circular. We have relied on the information and facts supplied, and the opinions expressed, by the Directors and management of the Group and have assumed that they are true, accurate and complete in all material aspects as at the Latest Practicable Date. We have also sought and received confirmation from the Directors and directors of AVIC International, that all material relevant information has been supplied to us and that no material facts have been omitted or withheld from the information supplied and opinions expressed to us. We have no reason to doubt the truth or accuracy of the information provided to us, or to believe that any material information has been omitted or withheld. We have, however, not conducted any independent investigation into the business and affairs of the Group, the Target Group or any of their respective associates or any party acting, or presumed to be acting, in concert with any of them, nor have we carried out any independent verification of the information supplied. We have also assumed that all representations contained or referred to in the Circular were true at the time they were made and at the Latest Practicable Date and will continue to be true up to the time of the SGM, and that the Independent Shareholders will be informed as soon as reasonably practicable if we become aware of any material change to such information provided and representations made.

PRINCIPAL FACTORS AND REASONS CONSIDERED

In arriving at our opinion and recommendation, we have taken into account the following principal factors and reasons:

1. Industry of the Target Group

As set out in the section headed "Information about the Target Group — 2. Industry overview" in Appendix I to the Circular, today the USA is the global leader in terms of general aviation aircraft fleet size and pilot population as well as general aviation aircraft shipments and revenues, positions it has long held. Also, the USA continues to produce approximately 70% of the world's certified aircraft and accounts for around half of all revenues in general aviation aircraft manufacturing. Faced with a mature and saturated market in North America and Western Europe, the general aviation industry faces unique challenges in accessing presently untapped markets. As economic growth and disposable incomes rise in the newly developed countries, a lack of infrastructure and burdensome regulatory procedures create challenges for market expansion in economies that have recently slowed down. In 2016, growth in Latin America, Asia Pacific, the Middle East and Africa remained soft. However, there are promising signs on the horizon as exemplified by changes taking place in China, the largest potential market.

In the piston engine aircraft segment, the USA manufacturers dominate the industry, a position they have held since the late 1920s. While piston aircraft sales declined around 4% worldwide in 2016, the USA did regain its position in terms of market share which inched up slightly. The revenue from sales of piston engines, MRO and spares in the USA declined by approximately 5% in 2016 as compared to 2015. Fluctuations are noted in revenue between 2013 and 2016. The industry is very concentrated with the top two players controlling approximately 88% of revenue shares in 2016. Faced with decades long relationships between OEM aircraft manufacturers, the leading three companies have focused on technical improvements in engines within their core competency and improving after service channels and developing strategic alliances around the world to tap into markets in the developing world.

Factors that drive demand for general aviation, in the traditionally strong yet mature markets of North America and Europe, by default, drive demand in the general aviation piston engine manufacturing segment as well. As discretionary incomes rise and unemployment dips, the possibility of participating in general aviation activities and purchasing general aviation aircraft increases, particularly in those segments of the population with annual household incomes greater than US$150,000. Improving conditions for business travel and continued challenges of "flying commercial" in these markets also support the demand for general aircraft piston engines.

Out to 2037, GDP growth in the developing world is expected to outpace that of the developed world, driven largely by the economies of India and China. Markets exist in China, India, Brazil and Argentina and to a lesser extent the more advanced economies of sub-Saharan Africa for the future of general aviation across all engine segments. In particular, China presents significant growth opportunities for general aviation in terms of sheer size — an increasingly affluent population and geography — as the country transitions from a largely agrarian society to a rapidly expanding manufacturing and service based economy. Significant opportunity exists for the emergence of new OEM manufacturers of piston engine aircraft to emerge in China. GDP growth in China is expected to average 4.9% over the forecast period 2016-2037. With their extensive manufacturing experience, the USA manufacturers are well positioned to provide this market with not only engines, but also subsystems and parts. For further details of the industry of the Target Group, please refer to the section headed "Information about the Target Group — 2. Industry overview" in Appendix I to the Circular.

2. Background of the Target Group

(i) ***Information of the Target Group***

The Target Company, a wholly-owned subsidiary of AVIC International, is the holding company of Continental Motors Group Limited, the holding company of Technify Motor (USA) Inc. and Continental Motors Deutschland Limited. The Target Group is principally engaged in the research, design, manufacturing and sales of aircraft piston engines fuelled by gasoline or diesel and engine spare parts and the provision of aftermarket service and support for general aviation aircraft through factory owned service centres.

As disclosed in the "Letter from the Board" contained in the Circular, in connection with the Acquisition, the Company has engaged Euromonitor International Limited ("**Euromonitor**") to conduct an independent assessment of the aircraft piston engine manufacturing industry in the USA. According to the commissioned research report prepared by Euromonitor, the Target Group is one of the leading manufacturers of and services providers to general aviation aircraft piston engines worldwide. The Target Group has been in the piston aircraft engine manufacturing industry since the beginning of the growth of the dominating USA market for general aviation piston aircraft delivering its first certified aircraft engine in 1929 and its engine products have been used in the top 3 (in terms of fleet size) aircraft manufacturers of fixed wing piston powered aircraft, Beechcraft, Cessna, and Cirrus Aircraft since 1930.

The Target Group stands apart from other major competitors in the field in its ability to produce engines ranging across market sectors dominated by its major competitors and in its capacities to produce both gasoline and diesel fuelled variations. The Target Group's history of innovation in diesel engine technology uniquely positions it to capture the market growth opportunities of general aviation both inside the USA and in the developing world. Certain clients use the diesel engines of the Target Group in their UAS aircrafts, while the market for UAS aircraft and technologies represents the most dynamic market for growth in aviation presently. With its main operations in the USA and Germany, the Target Group has established a manufacturing presence in both North America and Europe, the two regions of the world that presently account for more than 70% of the world market for piston engine powered aircraft. The Target Group set up CMB in 2014 for product sales, service and distribution in China and plans further development to provide technology development and engineering support for the growing number of new OEM aircraft developers being established in China.

As set out in the section headed "Information about the Target Group — 5. Business" in Appendix I to the Circular, the engine products of the Target Group can be categorised into three categories, namely (i) continental gasoline engine products; (ii) continental titan series gasoline engine products; and (iii) continental diesel engine products. The gasoline engine product is the traditional business line of the Target Group that can be traced back to 1904. The Target Group has five gasoline product lines. The continental titan series gasoline engines are currently used in the experimental aircraft market segments. The Target Group's diesel-powered engines focus on high use aircraft (e.g. pilot training and passenger transport) since it has several advantages in that market segment, including: (i) its engines are easier and more efficient to operate and maintain on a longer-term basis, compared to other piston-powered engines; and (ii) diesel is more fuel and cost efficient compared to leaded avgas (the leading alternative to diesel). The Target Group has three diesel product lines.

In addition, the Target Group manufactures a full line of aftermarket parts for the repair, maintenance and overhaul of both Continental and Lycoming branded engine products, such as cylinders, crankshafts, crankcases, ignition systems, gear boxes and more. Sales of aftermarket spare parts accounted for approximately 30% to 42% of total revenue of the Target Group during the Track Record Period.

The Target Group also offers a wide range of aviation services including but not limited to (i) overhaul or repair of Continental, Lycoming and P&W PT6 aviation engines; (ii) major power plant and airframe maintenance; (iii) factory engine sales and engine installations; (iv) avionics sales, repair and installation; (v) aircraft interior upgrades and refurbishment; (vi) supplemental type certificate installations; and (vii) fixed-base operator services. Overhaul service typically means a complete disassembly, inspection, repair, reassembly, test, and approval for return to service within the fits and limits specified by the manufacturer's overhaul data. An overhaul engine will normally be resold in the aftermarket at a lower price than new engines. The Target Group also provides installation and modification services of avionics and interior for small aircrafts and maintenance, plus repair and overhaul services for certain types of turbine engines.

(ii) ***Financial performance of the Target Group***

The accountant's report on the Target Group is set out in Appendix III to the Circular. Set out below is a summary of the consolidated statements of profit or loss of the Target Group for each of the three years ended 31 December 2014, 2015 and 2016 and for the six months ended 30 June 2016 and 2017.

	For the six months ended 30 June		Year ended 31 December		
	2017	**2016**	**2016**	**2015**	**2014**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
	(audited)	*(unaudited)*	*(audited)*	*(audited)*	*(audited)*
Revenue	99,432	101,191	204,315	163,689	161,444
Cost of sales	(67,955)	(67,980)	(138,883)	(111,907)	(112,110)
Gross profit	**31,477**	**33,211**	**65,432**	**51,782**	**49,334**
Selling expenses	(4,583)	(5,571)	(11,043)	(10,233)	(9,609)
General and administrative expenses	(16,718)	(18,407)	(33,956)	(27,152)	(36,069)
Other operating income/(expenses), net	87	162	(119)	35	92
Finance costs	(5,386)	(5,285)	(10,793)	(8,785)	(8,769)
Share of profit of a joint venture	35	17	14	1	2
Profit/(loss) before tax	**4,912**	**4,127**	**9,535**	**5,648**	**(5,019)**
Income tax credit/(expense)	(1,308)	(1,363)	(4,163)	5,945	(2,610)
Profit/(loss) for the period/year	**3,604**	**2,764**	**5,372**	**11,593**	**(7,629)**

(i) Revenue

The Target Group's revenue increased by approximately 1.39%, from approximately US$161.4 million in 2014 to approximately US$163.7 million in 2015, mainly attributable to the impact of acquisitions that gave the Target Group access to adjacent markets, which was offset by the reduced value in purchases from its top five customers from approximately US$57.4 million in 2014 to approximately US$51.9 million in 2015. It then further increased by approximately 24.82% to approximately US$204.3 million in 2016, mainly attributable to (i) the Target Group increasing inventory available in the marketplace; (ii) the acquisitions completed in 2015 that provided access to adjacent markets and further created new growth opportunities; and (iii) the increased sales of UAV (drone) applications using diesel engines. For the six months ended 30 June 2017, total revenue of the Target Group was approximately US$99.4 million, representing a slight decrease of approximately 1.74% comparing to the corresponding period in 2016, mainly caused by a decrease in repair and maintenance service income which was partially offset by an increase in the sale of engines.

(ii) Cost of sales

The Target Group's cost of sales decreased slightly by approximately 0.18% from approximately US$112.1 million in 2014 to approximately US$111.9 million in 2015. The decrease was primarily attributable to cost saving initiatives implemented in factory operations. It then increased by approximately 24.11% to approximately US$138.9 million in 2016, which was in line with the increase in revenue of approximately 24.82% for the same period. The Target Group's cost of sales decreased by approximately US$25,000 to approximately US$68.0 million for the six months ended 30 June 2017 as compared to the corresponding period in 2016, mainly due to the decrease in revenue of approximately 1.74% for the same period.

(iii) Gross profit and gross profit margin

As a result of the above, the Target Group's gross profit increased slightly by approximately 4.96% from approximately US$49.3 million in 2014 to approximately US$51.8 million in 2015, with a slight improvement in gross profit margin from approximately 30.56% in 2014 to approximately 31.63% in 2015. It then further increased by approximately 26.36% to approximately US$65.4 million in 2016, accompanied with a slight increase of gross profit margin to approximately 32.03% in 2016, mainly attributable to UAV sales which contributed to an increase in gross profit. The Target Group's gross profit decreased by approximately 5.22% to approximately US$31.5 million for the six months ended 30 June 2017 as compared with the corresponding period in 2016. Gross profit margin decreased from approximately 32.82% to approximately 31.66% for the same period. The decrease in gross profit was resulted from the drop in revenue and the decline of margin due to change of volume and mix.

(iv) Selling expenses

The Target Group's selling expenses increased by approximately US$0.6 million from approximately US$9.6 million in 2014 to approximately US$10.2 million in 2015, primarily attributable to the impact of additional sales costs acquired with the acquisitions made in 2015. It was followed by an increase of approximately 7.92% to approximately US$11.0 million in 2016, mainly as a result of costs associated with increased marketing activities to increase the Target Group's visibility in the global market and the increase in warranty expenses due to the significant increase in revenue for the period. The Target Group's selling expenses decreased by approximately 17.73% to approximately US$4.6 million for the six months ended 30 June 2017. Such decrease was a result of a drop in warranty expenses.

(v) General and administrative expenses

The Target Group's general and administrative expenses decreased by approximately 24.72% from approximately US$36.1 million in 2014 to approximately US$27.2 million in 2015, followed by an increase of approximately 25.06% to approximately US$34.0 million in 2016, mainly because of a reduction in the product liability and other related expenses. The Target Group's general and administrative expenses decreased by approximately 9.18% from approximately US$18.4 million for the six months ended 30 June 2016 to approximately US$16.7 million for the six months ended 30 June 2017, mainly due to reduction in consulting services costs and general insurance costs.

A significant portion of such expenses in the Target Group's business is aviation product liability. In order to manage expenses and risks relating to aviation product liability, the Target Group maintains a product liability insurance program, which consists of a Self-Insured Retention and a layer of coverage by the insurers subject to policy limits. The Target Group maintained a provision to reflect the risk of payments based on the expected outflow of resources to cover the product claims and liabilities and any related costs. For each of the three years ended 31 December 2016 and the six months ended 30 June 2017, the Target Group recorded net product liability provision/(reversal of such provision) and other related expenses of approximately US$10.2 million, (US$3.8 million), US$4.0 million and US$0.7 million respectively. These amounts included a net reversal of product liability provision of approximately US$2.3 million, US$14.9 million, US$5.1 million and US$3.5 million for each of the three years ended 31 December 2016 and the six months ended 30 June 2017, respectively, mainly as a result of the close, resolution or settlement of certain cases brought forward from previous years.

(vi) Finance costs

The finance costs were stable in 2014 and 2015, amounted to approximately US$8.8 million in each of both years. In 2016, there was an increase of approximately US$2.0 million in finance costs due to increased interest payments and increased loan guarantee costs. For the six months ended 30 June 2017, the finance costs remained fairly stable at approximately US$5.4 million as compared to that for the corresponding period in 2016.

(vii) Income tax credit/(expense)

The Target Group recorded income tax expense of approximately US$2.6 million in 2014 but enjoyed income tax credit of approximately US$5.9 million in 2015. The income tax credit in 2015 resulted from the income tax expense of approximately US$0.4 million and deferred tax credit of approximately US$6.3 million, which was mainly contributed by the recognition of deferred tax assets in 2015. The Target Group recorded income tax expense of approximately US$4.2 million in 2016.

The Target Group recorded income tax expense of approximately US$1.3 million for the six months ended 30 June 2017, a slight decrease of approximately US$0.1 million as compared to that for the corresponding period in 2016.

(viii) Profit/(loss) for the period/year

As a result of the above, the profit for the year increased by approximately US$19.2 million from a loss of approximately US$7.6 million in 2014 to a profit of approximately US$11.6 million in 2015. It then reduced by approximately US$6.2 million to approximately US$5.4 million in 2016, which was mainly due to the tax credit in 2015 as mentioned above.

For the six months ended 30 June 2017, the Target Group recorded a profit of approximately US$3.6 million, an increase of approximately 30.39% from approximately US$2.8 million for the six months ended 30 June 2016. Its profit margin also improved from approximately 2.7% to approximately 3.6% for the same period.

(iii) ***Financial position of the Target Group***

Set out below is a summary of the consolidated statements of financial position of the Target Group as at 31 December 2014, 2015, 2016 and 30 June 2017.

	As at 30 June 2017	**As at 31 December 2016**	**As at 31 December 2015**	**As at 31 December 2014**
	US$'000	*US$'000*	*US$'000*	*US$'000*
	(audited)	*(audited)*	*(audited)*	*(audited)*
NON-CURRENT ASSETS				
Property, plant and equipment	31,789	34,165	38,730	34,343
Goodwill	109,453	109,153	109,373	106,714
Other intangible assets	119,036	115,185	111,626	105,831
Investment in a joint venture	85	50	36	35
Deferred tax assets	—	—	468	—
Prepayment	125	142	177	216
Total non-current assets	260,488	258,695	260,410	247,139
CURRENT ASSETS				
Inventories	59,638	52,001	46,419	39,054
Trade receivables, prepayments and other receivables	19,616	20,456	29,771	17,151
Due from fellow subsidiaries	2,344	3,734	3,254	5,968
Restricted bank balance	—	—	—	8,083
Cash and cash equivalents	8,460	14,105	9,419	13,191
Total current assets	90,058	90,296	88,863	83,447
CURRENT LIABILITIES				
Trade payables, other payables and accruals	19,795	22,718	25,123	21,013
Interest-bearing loans and borrowings	21,600	21,600	5,959	346
Provisions and other liabilities	4,109	4,164	2,972	6,558
Deferred revenue	143	466	122	184
Tax payable	78	4	277	152
Due to group companies	50,514	39,411	24,332	5,167
Total current liabilities	96,239	88,363	58,785	33,420

	As at 30 June 2017 US$'000 (audited)	As at 31 December 2016 US$'000 (audited)	As at 31 December 2015 US$'000 (audited)	As at 31 December 2014 US$'000 (audited)
NON-CURRENT LIABILITIES				
Interest-bearing loans and borrowings	216,128	222,824	256,367	257,568
Provisions and other liabilities	13,112	15,849	23,004	36,940
Deferred revenue and defined benefit obligations	4,879	5,087	4,222	3,771
Deferred tax liabilities	4,927	3,714	—	5,961
Due to group companies	2,194	2,318	2,153	868
Total non-current liabilities	**241,240**	**249,792**	**285,746**	**305,108**
NET ASSETS/(LIABILITIES)	**13,067**	**10,836**	**4,742**	**(7,942)**
EQUITY/(DEFICIENCY IN ASSETS)				
Share capital	20,000	20,000	20,000	20,000
Reserves	(6,933)	(9,164)	(15,258)	(27,942)
TOTAL EQUITY/(DEFICIENCY IN ASSETS)	**13,067**	**10,836**	**4,742**	**(7,942)**

(i) Property, plant and equipment

As at 31 December 2014, 2015, 2016 and 30 June 2017, property, plant and equipment amounted to approximately US$34.3 million, US$38.7 million, US$34.2 million and US$31.8 million, respectively, representing approximately 10% of the Target Group's total assets as at the respective dates. The balance increased from approximately US$34.3 million as at 31 December 2014 to approximately US$38.7 million as at 31 December 2015, mainly because of its business combinations in 2015. The Target Group's property, plant and equipment then decreased by approximately US$4.5 million to approximately US$34.2 million as at 31 December 2016, primarily due to the depreciation expenses amounted to approximately US$6.0 million. Such balance decreased to approximately US$31.8 million as at 30 June 2017, mainly caused by the depreciation expenses of approximately US$3.1 million incurred for the six months ended 30 June 2017.

(ii) Other intangible assets

Other intangible assets mainly represent product technology, licence and completed programs, trademarks and development programs in progress. As at 31 December 2014, 2015 and 2016 and 30 June 2017, intangible assets amounted to approximately US$105.8 million, US$111.6 million, US$115.2 million and US$119.0 million, respectively, representing approximately 32.01%, 31.96%, 33.01% and 33.96% of the Target Group's total assets, respectively. Other intangible assets increased from approximately US$105.8 million as at 31 December 2014 to approximately US$111.6 million as at 31 December 2015, mainly because of its business combinations in 2015. The Target Group's intangible assets then further increased by approximately US$3.6 million to approximately US$115.2 million as at 31 December 2016, primarily due to the capitalised development costs of approximately US$8.3 million. The Target Group's intangible assets increased by approximately 3.34% to approximately US$119.0 million as at 30 June 2017, mainly resulted from the addition of development costs of approximately US$4.8 million.

(iii) Goodwill

As at 31 December 2014, 2015, 2016 and 30 June 2017, goodwill amounted to approximately US$106.7 million, US$109.4 million, US$109.2 million and US$109.5 million, respectively, representing approximately 32.28%, 31.31%, 31.28% and 31.22% of the Target Group's total assets, respectively. The balance as at 31 December 2014 was mainly related to the acquisition of Southern Avionics and Communications, Inc. Goodwill increased from approximately US$106.7 million as at 31 December 2014 to approximately US$109.4 million as at 31 December 2015 as a result of its two acquisitions completed during 2015. It then decreased slightly to approximately US$109.2 million as at 31 December 2016 because of impairment and exchange realignment, but later on rebounded to approximately US$109.5 million, as at 30 June 2017, also due to the exchange realignment.

(iv) Inventories

As at 31 December 2014, 2015, 2016 and 30 June 2017, inventories amounted to approximately US$39.1 million, US$46.4 million, US$52.0 million and US$59.6 million, respectively, representing approximately 11.81%, 13.29%, 14.90% and 17.01% of the Target Group's total assets, respectively. The Target Group's inventories increased from approximately US$39.1 million as at 31 December 2014 to approximately US$46.4 million as at 31 December 2015 and further increased by approximately US$5.6 million to approximately US$52.0 million as at 31 December 2016, primarily due to the acquisitions completed in 2015. As at 30 June 2017, the Target Group's inventories increased to approximately US$59.6 million from approximately US$52.0 million as at 31 December 2016, mainly attributable to the Target Group retaining additional inventories as additional safety buffers to reduce inventory lead time.

(v) Trade receivables, prepayments and other receivables

As at 31 December 2014, 2015, 2016 and 30 June 2017, trade receivables, prepayments and other receivables amounted to approximately US$17.2 million, US$29.8 million, US$20.5 million and US$19.6 million, respectively, representing approximately 5.19%, 8.52%, 5.86% and 5.60% of the Target Group's total assets, respectively. The Target Group's trade receivables, prepayments and other receivables increased substantially from approximately US$17.2 million as at 31 December 2014 to approximately US$29.8 million as at 31 December 2015, primarily due to slower collections of receivables from customers. The Target Group's trade receivables, prepayments and other receivables then decreased by approximately 31.21%, to approximately US$20.5 million as at 31 December 2016, primarily due to an emphasis by management and finance on maintaining strong collections to terms. The Target Group's trade receivables, prepayments and other receivables decreased slightly by approximately 4.11% to approximately US$19.6 million as at 30 June 2017.

(vi) Trade payables, other payables and accruals

As at 31 December 2014, 2015, 2016 and 30 June 2017, the trade payables, other payables and accruals were approximately US$21.0 million, US$25.1 million, US$22.7 million and US$19.8 million, respectively. The increase in balance as at 31 December 2015 was mainly due to an increase in loan interest payments and trade payables from the acquisitions it completed. It subsequently decreased by approximately US$2.4 million to approximately US$22.7 million as at 31 December 2016, which was mainly attributable to reduced trade payables, and further decreased by approximately US$2.9 million to approximately US$19.8 million as at 30 June 2017, mainly because of less purchases resulting from inventory control.

(vii) Interest-bearing loans and borrowings

Interest-bearing loans and borrowings amounted to approximately US$257.9 million, US$262.3 million, US$244.4 million and US$237.7 million as at 31 December 2014, 2015, 2016 and 30 June 2017 respectively. The balance mainly represents loans borrowed from the Export-Import Bank of China and Bank of China Limited. The decrease in loan balance as at 31 December 2016 and 30 June 2017 was mainly attributable to the repayment of certain loans during 2016 and 2017.

(viii) Provisions and other liabilities

As at 31 December 2014, 2015, 2016 and 30 June 2017, the Target Group's provisions and other liabilities were approximately US$43.5 million, US$26.0 million, US$20.0 million and US$17.2 million respectively, representing mainly product liability provisions related to probable costs made for the product liability claims from legal proceedings. The decrease in balance was mainly due to the close, resolution or settlement of certain cases brought forward from previous year. As a result, the Target Group reassessed the provision amounts for outstanding product liability claims at the end of each period during the Track Record Period.

3. Background of the Group and rationale for the Acquisition

(i) ***Background of the Group***

The Company is an investment holding company and the Group has been engaged in property development and investment business and trading business since 2014 and was previously engaged in knitting and textile business, until it was disposed of in 2016. During the year ended 31 December 2016, the Group disposed Zhejiang Dongyang Jinniu, a 51%-owned subsidiary engaging in the production and distribution of knitting and textile products, knitted fabrics and clothing since it had been loss-making in recent years. The Group also has a track record in aviation business since 2002.

In respect of the property development and investment business, the Group is engaged in the property development of residential and commercial projects. As stated in the 2016 Annual Report, during the year, two projects were in progress. One was located at the Southern side of Zhongshan

Road of the Shahekou District of the Dalian City ("**Dalian Project**"), and another was situated in a newly developed residential area with communal facilities in the Liangjiangxin District of Chongqing ("**Chongqing Project**"). The Dalian Project is a large-scale development project comprising offices, retail shops and residential buildings, it is currently in the development and construction phase and pre-sale of residential/office space commenced in June 2013. The Chongqing Project comprises twelve parcels of land located in Liangjiangxin District of Chongqing and is currently in the early development phase. Revenue from the property development and investment business contributed all the Group's revenue for the year ended 31 December 2016 and 99.6% of the Group's revenue for the year ended 31 December 2015.

For aviation business, as at the Latest Practicable Date, the Company held a 69.4% equity interest in CATIC Siwei Co., Ltd ("**CATIC Siwei**"), indirectly through nominee shareholding arrangements. CATIC Siwei engages in the provision of aerophotographic services, data collection, geospatial business applications and services. The Company invested in CATIC Siwei on 28 May 2002.

(ii) ***Financial performance of the Group***

The financial information of the Group is set out in Appendix II to the Circular. Set out below is a summary of the consolidated statements of profit or loss of the Group for each of the three years ended 31 December 2014, 2015 and 2016 and the six months ended 30 June 2016 and 2017, which are extracted from the Annual Reports and the Interim Report.

	Six months ended 30 June		**Year ended 31 December**		
	2017	**2016**	**2016**	**2015**	**2014**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
	(unaudited)	*(unaudited)*	*(audited)*	*(audited and restated)*	*(audited)*
					(Note)
Continuing operations					
Revenue	29,740	64,587	102,786	2,154,988	70,856
Gross profit	8,760	28,559	28,517	180,534	5,823
Profit/(loss) from continuing operations	(67,007)	(348,668)	(736,293)	97,516	5,947
Discontinued operation					
Profit/(loss) from discontinued operation	—	(5,091)	27,362	(14,056)	—
Profit/(loss) for the year/period	**(67,007)**	**(353,759)**	**(708,931)**	**83,460**	**5,947**

Note: As disclosed in the 2014 Annual Report and 2015 Annual Report, the financial results from knitting and textile business had not been classified as discontinued operation for the year ended 31 December 2014.

During the year ended 31 December 2014, the Group was principally engaged in knitting and textile business and trading of raw materials and auxiliary materials. During each of the two years ended 31 December 2015 and 2016 and the six months ended 30 June 2017, the Group was principally engaged in the property development and investment business. Continuing operations for financial years ended 31 December 2015 and 2016 represented results from the property development and investment business and discontinued operations represented results from the knitting and textile business.

Continuing operations

a) Revenue

For the six months ended 30 June 2017, revenue of the Group decreased by approximately 54% to approximately HK$29.7 million as compared to the corresponding period in 2016. As stated in the Interim Report, the PRC government continued to impose restrictions on purchases and sales of properties in the PRC. It also introduced price restriction and more stringent credit policies on purchase of properties during the period. The policies and regulations introduced by the PRC government led to a decrease in trading volume of properties of Dalian Project. The Group did not generate any revenue from its trading business during the six months ended 30 June 2017.

For the year ended 31 December 2016, the Group's revenue decreased to approximately HK$103 million by approximately HK$2 billion, or approximately 95% from approximately HK$2.15 billion in 2015. As stated in the 2016 Annual Report, the substantial decrease in revenue was mainly due to policy control on capital flows of financial institutions, causing tightened capital liquidity. As stated in the 2016 Annual Report, in several cities, a series of macro-economic control measures introduced in succession and restrictions on property purchases and mortgage loans were re-launched. As a result, the trading volume of properties in Dalian showed a downward trend, leading to a significant decrease in the Group's revenue in 2016. The Group did not generate any revenue from its trading business during 2016.

For the year ended 31 December 2015, the Group's revenue increased to approximately HK$2.15 billion by approximately HK$2.1 billion, from approximately HK$71 million in 2014. The substantial increase in revenue was mainly due to the property development and investment business acquired by the Group on 30 December 2014, the Group started to sell and lease out properties during the year ended 31 December 2015.

b) *Profit/(loss) from continuing operations*

For the six months ended 30 June 2017, the Group's loss was approximately HK$67 million, representing a decrease of approximately 81% from the same period in 2016, mainly due to (i) a decline in gross profit given a drop in revenue during the period; (ii) the significant decrease in fair value loss on derivative financial instruments and equity investment at fair value through profit or loss by approximately HK$173 million; (iii) a decrease in the share of loss of the joint venture, CATIC Siwei, by approximately HK$33 million; (iv) a drop in impairment of an available-for-sale investment by approximately HK$46 million; and (v) gain on disposal of convertible loans of approximately HK$87 million.

The Group recorded a loss of approximately HK$736 million from continuing operations for the year ended 31 December 2016 as compared to a profit of approximately HK$98 million for the year ended 31 December 2015, which was mainly attributable to (i) a decrease in gross profit by approximately HK$152 million as a result of the significant drop in revenue in 2016; (ii) an increased share of loss of CATIC Siwei by approximately HK$188 million; (iii) the fair value loss on derivative financial instruments of approximately HK$109 million; (iv) fair value loss recognised on listed equity investment of approximately HK$198 million; and (v) the decrease in net gain on deemed disposal of associates by approximately HK$430 million, partially offset by the decrease in impairment of an available-for-sale investment by approximately HK$177 million.

For the year ended 31 December 2015, profit from continuing operations amounted to approximately HK$98 million, mainly attributable to the change in the principal business of the Group during the year from knitting and textile business to property development and investment business from 2014 to 2015.

Discontinued operation

During the year ended 31 December 2016, the Group disposed Zhejiang Dongyang Jinniu, which was engaged in the production and distribution of knitting and textile products, knitted fabrics and clothing, and ceased the knitting and textile business as it had been loss-making in recent years. Such business was classified as discontinued operation and the Group recorded a profit of approximately HK$27 million from discontinued operation for the year ended 31 December 2016 as compared to a loss of approximately HK$14 million for the year ended 31 December 2015, mainly attributable to the gain on disposal of approximately HK$32 million.

(iii) ***Financial position of the Group***

Set out below is a summary of financial positions of the Group as at 31 December 2014, 31 December 2015, 31 December 2016 and 30 June 2017, which is extracted from the Annual Reports and the Interim Report.

	As at 30 June 2017 *HK$'000* *(unaudited)*	**As at 31 December 2016** *HK$'000* *(audited)*	**As at 31 December 2015** *HK$'000* *(audited)*	**As at 31 December 2014** *HK$'000* *(audited)*
NON-CURRENT ASSETS				
Property, plant and equipment	23,425	24,975	31,595	41,297
Investment properties	325,391	315,866	373,425	—
Prepaid land lease payments	—	—	2,814	2,958
Intangible assets	—	—	380	570
Investment in a joint venture	50,137	58,602	290,621	317,899
Investment in associates	12,265	13,378	24,146	237,963
Available-for-sale investments	192,897	278,745	400,421	121,771
Derivative financial instruments	68	11,338	119,896	125,373
Trade receivable	—	20,178	21,628	—
Due from a fellow subsidiary	—	—	3,178	—
Loan to a related company	—	—	11,976	18,750
Prepayments	—	—	278	3,765
Deferred tax assets	10,327	10,025	9,685	—
Total non-current assets	614,510	733,107	1,290,043	870,346
CURRENT ASSETS				
Properties under development and completed properties held for sale	4,326,947	4,105,317	4,070,648	4,950,000
Inventories	—	—	4,564	2,855
Trade and bills receivables	88,307	69,442	155,450	19,379
Due from fellow subsidiaries	2,646	10,960	46,016	—
Due from a non-controlling shareholder of a subsidiary	—	—	323	—
Due from an intermediate holding company	—	5,282	—	—
Loans to associates	9,783	9,497	—	—
Loans to related companies	17,265	16,760	17,230	19,750
Prepayments, deposits and other receivables	45,575	42,978	61,714	1,204,613
Available-for-sale investments	48,636	—	—	51,071
Equity investment at fair value through profit or loss	61,714	87,619	285,713	166,797
Derivative financial instruments	184	—	—	25,497
Prepaid taxes	23,078	16,186	12,156	120,981
Time deposit with original maturity of more than three months when acquired	—	—	—	155,588
Pledged time deposits	—	—	359	375
Cash and cash equivalents	670,377	605,925	473,330	1,093,361
Total current assets	5,294,512	4,969,966	5,127,503	7,810,267

	As at 30 June 2017 HK$'000 (unaudited)	As at 31 December 2016 HK$'000 (audited)	As at 31 December 2015 HK$'000 (audited)	As at 31 December 2014 HK$'000 (audited)
CURRENT LIABILITIES				
Due to non-controlling shareholders of subsidiaries	117,783	88,444	64,301	49,734
Due to an intermediate holding company	7,535	—	14,164	—
Due to fellow subsidiaries	2,969	1,643	4	123,400
Loans from fellow subsidiaries	621,547	586,592	205,988	2,103,087
Trade and bills payables	35,178	41,213	92,358	8,495
Other payables and accruals	22,217	17,223	32,744	56,083
Customer deposits	1,367,722	920,238	248,310	1,757,152
Interest-bearing bank borrowings	—	—	37,964	39,625
Tax payable	36,954	37,449	68,139	38,912
Total current liabilities	2,211,905	1,692,802	763,972	4,176,488
Net current assets	3,082,607	3,277,164	4,363,531	3,633,779
NON-CURRENT LIABILITIES				
Loans from an intermediate holding company	489,756	475,419	509,581	—
Loans from a fellow subsidiary	540,976	648,045	1,658,683	258,750
Interest-bearing bank borrowings	—	230,134	—	665,061
Deferred tax liabilities	134,328	129,920	153,652	218,553
Total non-current liabilities	1,165,060	1,483,518	2,321,916	1,142,364
Net assets	2,532,057	2,526,753	3,331,658	3,361,761
Equity				
Issued capital	551,959	551,959	551,959	551,959
Reserves	1,416,273	1,421,313	2,185,575	2,231,412
Equity attributable to owners of the parent	1,968,232	1,973,272	2,737,534	2,783,371
Non-controlling interests	563,825	553,481	594,124	578,390
TOTAL EQUITY	2,532,057	2,526,753	3,331,658	3,361,761
Net asset value ("NAV") per Share (HK$)	0.36	0.36	0.50	0.50

As shown in the table above, the non-current assets of the Group mainly consisted of investment properties, available-for-sale investments and investment in a joint venture as at 30 June 2017. Investment properties consist of commercial properties in the PRC. As at 31 December 2015, investment properties amounted to approximately HK$373 million, as a result of reclassification from properties under development related to a property in Liaoning Province in the PRC after the Group entered into operating lease arrangements in relation to the property. As at 30 June 2017, investment properties amounted to approximately HK$325 million.

As at 30 June 2017, the Group's current assets mainly consisted of properties under development and completed properties held for sale of approximately HK$4.3 billion, representing properties in Dalian, which are partly completed, and in Chongqing, which were under progress as at 30 June 2017. Cash and cash equivalents increased from approximately HK$473 million as at 31 December 2015 to approximately HK$606 million as at 31 December 2016, which was mainly attributable to the increase in customer deposits as at 31 December 2016. Cash and cash equivalents amounted to approximately HK$670 million as at 30 June 2017.

As at 30 June 2017, the Group's liabilities mainly consisted of (i) loans from fellow subsidiaries of approximately HK$1.2 billion and loan from an intermediate holding company of approximately HK$490 million, which were both unsecured and bear interest at 6% per annum; and (ii) customer deposits, representing the proceeds of the pre-sale of properties, amounted to approximately HK$1.4 billion.

As at 30 June 2017, the NAV per Share was approximately HK$0.36 per Share, calculated by dividing the NAV of the Group attributable to owners of the parent of approximately HK$1,968 million by the number of Shares in issue of 5,519,591,000 as at 30 June 2017.

(iv) ***Rationale for the Acquisition***

As stated in the Company's announcement dated 7 September 2016, the Company was considering a series of business and asset reorganisation proposals which included the acquisition of certain assets and the disposal of the Group's real estate development business in the PRC. As stated in the "Letter from the Board" contained in the Circular, the proposed reorganisation was being contemplated by the Company as part of a wider restructuring campaign being implemented by the PRC State-owned Assets Supervision and Administration Commission (SASAC). As part of the restructuring campaign, SASAC had requested Aviation Industry to dispose of all its real estate business.

On the other hand, the Acquisition is also likely to be favourable to the future development of the Group considering the factors set out below.

— *PRC real estate market and the existing business of the Group*

The Group has been engaging in the property development and investment business after the acquisition of such business on 30 December 2014. The Group was profit-making during the year ended 31 December 2015 with the sales and leasing of properties during the year. However, in 2016, due to policy control introduced on 30 September 2016 on capital flows of financial institutions, the trading volume of the Group's properties decreased significantly, leading to a loss for the year.

The PRC real estate market continued to remain strong in 2016 after the downturn in 2014. According to statistics released by the National Bureau of Statistics of the PRC[1], investment in the real estate development in the PRC recorded an increase of approximately 6.9% in 2016 from 2015. Sales and sales area of commodity housing increased by approximately 34.8% and 22.5% respectively in 2016 as compared to 2015. However, the growth in sales and sales area of commodity housing slowed down to approximately 21.5% and 16.1% respectively in the first half of 2017 as compared to the same period in 2016.

Furthermore, the situation varied in different regions of the PRC. According to the statistics released by Dalian Municipal Bureau of Statistics[2], investment in the real estate development in Dalian decreased by approximately 40.4% in 2016 as compared to 2015. Based on the latest statistics available, sales and sales area of commodity housing in Dalian recorded an increase of approximately 13.4% and 5.7% respectively during the first eight months in 2016 as compared to the same period in 2015. It demonstrates that the real estate market in Dalian was lagging behind the national growth as mentioned above. According to statistics released by the Chongqing Municipal Bureau of Statistics[3], investment in the real estate development in Chongqing recorded a decrease of approximately 0.7% in 2016 as compared to 2015. Both sales and sales area of commodity housing recorded an annual growth of approximately 16.3% in 2016. The above statistics indicate that the development of real estate market varied in different regions of the PRC.

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1 National Bureau of Statistics of the PRC: http://www.stats.gov.cn/tjsj/zxfb/201701/t20170120_1455967.html, http://www.stats.gov.cn/tjsj/zxfb/201707/t20170717_1513528.html

2 Dalian Municipal Bureau of Statistics: http://www.stats.dl.gov.cn/

3 Chongqing Municipal Bureau of Statistics: http://www.cqtj.gov.cn/xwdt/201701/t20170120_439333.htm

In recent years, the PRC government has been introducing policies and regulations to (i) stimulate the development of the real estate market; and (ii) stabilise the then overheating real estate market. In light of the negative growth in both sales and sales area of commodity housing in 2014 as compared to 2013 based on statistics released by the National Bureau of Statistics of the PRC, the PRC government has issued notices in early 2015 to lower the minimum level of down payment and related business tax relief to encourage the development of the market. The PRC real estate market experienced a recovery later in 2015. In order to prevent the market from overheating, Beijing government took the lead in introducing housing policies to control the market growth by imposing a range of restrictions in late September 2016. Governments of a number of cities in the PRC, including Chongqing, followed shortly after that on introducing similar policies. These measures mainly include the tightening of down payment requirements and purchase restrictions on properties. More measures were put in place in March 2017 by the Beijing government, mainly in relation to raising the down payment for second home purchasers and suspending housing loans with a maturity of 25 years or more.

In view of the above, development of the real estate market in the PRC is likely to be influenced by policies and regulations introduced by the PRC government, which creates uncertainties on future development of the PRC real estate market and hence the existing business of the Group.

— *Development of the PRC general aviation industry*

Upon Acquisition Completion, the Group will be engaging in the aircraft piston engine manufacturing for general aviation piston aircraft. Apart from the established market in the USA with details set out in the "1. Industry of the Target Group" of this letter, the Group also allows itself to explore opportunities available in the PRC in relation to general aviation industry given its recent development.

In recent years, there has been rapid development in the general aviation industry in the PRC. The State Council of the PRC issued the Opinions on Promoting the Development of Civil Aviation (《國務院關於促進民航業發展的若干意見》國發〔2012〕24號) in July 2012, stating that the PRC government will put efforts in developing the general aviation industry. Based on report released by the Civil Aviation Administration of China ("**CAAC**")[4], the flight hours of the general aviation industry in the PRC amounted to approximately 517,000 in 2012 and increased to approximately 764,700 in 2016, representing a compound annual growth rate ("**CAGR**") of approximately 10.3%. The general aviation aircraft fleet size grew from 1,320 in 2012 to 2,096 in 2016, representing a CAGR of approximately 12.3%. The number of enterprises in the PRC general aviation industry increased from 146 in 2012 to 320 in 2016 at a CAGR of approximately 21.7%.

4 Civil Aviation Administration of China: http://www.caac.gov.cn/XXGK/XXGK/TJSJ/201705/t20170508_44009.html

Despite such growth in recent years, the general aviation industry in the PRC is still under development according to the Guidance on Promoting the Development of General Aviation Industry (the "**PRC General Aviation Guidance**") issued by the State Council of the PRC in May 2016 (《國務院辦公廳關於促進通用航空業發展的指導意見》國辦發〔2016〕38號). The PRC government has announced its initiative in further promoting the general aviation industry in future years. According to the PRC General Aviation Guidance, it is set to build a general aviation industry that has more than 500 general aviation airports, 5,000 aircrafts and a group of competitive enterprises in the PRC by the end of 2020. Ultimately, the PRC government intends to put more efforts in providing diversified general aviation services and stimulating aviation innovation and to improve manufacturing capabilities in key aviation technologies. Further, as stated in the PRC General Aviation Guidance, aviation consumption is encouraged to be integrated with the Internet, tourism and other creative industries. Also, the PRC government intends to strengthen international cooperation in aviation manufacturing, operations management and pilot training.

Moreover, it is also noted in the 13th Five-year Plan for China's Civil Aviation Development (中國民用航空發展第十三個五年規劃), released jointly by CAAC, National Development and Reform Commission of the PRC and the Ministry of Transport of the PRC in December 2016, that the PRC government is supporting the implementation of the PRC General Aviation Guidance, stating that there are plans on building more infrastructure, putting in place a standard system and continuously improving the operating environment and expanding service areas.

In light of the above, with the growth in the PRC general aviation industry in recent years and the intentions of the PRC government encouraging the development of the industry, the Group, upon Acquisition Completion, will be well-positioned to seize the potential business opportunities available in the industry and benefit from the industrial development in future years.

— *Financial impact of the Acquisition on the Group*

The Target Group has been making profits during the years ended 31 December 2015 and 2016, and during the six months ended 30 June 2017. Based on the unaudited pro forma financial information of the Enlarged Group in Appendix IV to the Circular, upon Acquisition Completion, the loss attributable to owners of the parent and the gearing ratio of the Enlarged Group would decrease. Also, equity attributable to owners of the parent would be enhanced. It demonstrates that there is potential improvement in the performance and the financial position of the Group upon Acquisition Completion. For further details on the financial effects of the Acquisition, please refer to the section headed "6. Financial effects of the Acquisition" of this letter.

— *Potential synergies with AVIC Group*

AVIC Group focuses their operations on aviation and provide complete services to customers in many sectors, from research and development to operation, manufacturing and financing. AVIC Group's business units cover defence, transport aircrafts, helicopters, avionics and systems, general aviation, aviation research and development, flight testing, trade and logistics, assets management, finance services, engineering and construction, and automobiles etc. Upon Acquisition Completion, the business of the Group will be in line with the overall development of AVIC Group and potentially create operational synergies for the Enlarged Group going forward.

As stated in the "Letter from the Board" contained in the Circular, the Directors are of the view that the Acquisition will provide an opportunity for the Group to capture the prospect of aviation industry, which will enable the Group to enhance the stability of revenue and cash flows and reduce the Group's reliance on property development in the PRC, which is undergoing a downward risk and subject to tightened government regulatory requirements.

Having considered the above, in particular, (i) the performance of the existing business of the Group and the uncertainties on the PRC real estate market; (ii) the recent development of the PRC general aviation industry and the PRC government's intention to boost the industry; (iii) the financial impact of the Acquisition on the Group; and (iv) potential synergies with AVIC Group, we concur with the Directors' view that the Acquisition will facilitate the sustainable growth of the Group in the long run and is in the interests of the Company and the Shareholders as a whole.

4. Principal terms of the Acquisition

Date: 19 September 2017

Parties: AVIC HK (the seller)
The Company (the purchaser)
AVIC International (the seller guarantor)

(i) *Subject matter*

Under the Acquisition Agreement, AVIC HK has agreed to sell and the Company agreed to acquire (i) the entire issued share capital of the Target Company; and (ii) the shareholder's loan note(s) owing by the Target Company to AVIC HK at Acquisition Completion.

Prior to Acquisition Completion, the seller guarantor has undertaken, at its own cost, to transfer the entire issued share capital of the Target Company to the seller as part of the pre-sale reorganisation for the Acquisition.

(ii) *Conditions precedent of the Acquisition*

Acquisition Completion is subject to the fulfilment or waiver (as applicable) of the conditions (the "**Conditions Precedent**") as set out in the section headed "Conditions to Acquisition Completion" in the "Letter from the Board" contained in the Circular, including but not limited to:

a) each of the following being approved by the Independent Shareholders at the SGM, with voting being taken by way of poll, the Acquisition, the allotment and issue by the Company of the Consideration Shares and the Whitewash Waiver; and

b) the grant of the Whitewash Waiver by the Executive.

(iii) *Consideration*

The Consideration is HK$2,400,000,000. On 27 October 2017, AVIC International, AVIC HK and the Company entered into the Amendment Deed to amend the payment terms regarding the deferred consideration under the Acquisition Agreement. According to the Acquisition Agreement and the Amendment Deed, the Consideration is to be satisfied by the Company in the following manner:

a) HK$1,400,000,000 will be satisfied by way of allotment and issue of the Consideration Shares to AVIC HK at Acquisition Completion;

b) HK$200,000,000 will be satisfied by cash at Acquisition Completion; and

c) HK$800,000,000 will be satisfied by cash upon the earlier occurrence of the following events:

   (i) the Company having received the proceeds from the disposal of its real estate business, resulting in the Company having net cash balance of more than HK$800,000,000; and

   (ii) the Company having net cash balance of more than HK$800,000,000.

The Company shall use its reasonable endeavours to procure that either of the above events is consummated within six months after the Acquisition Completion Date (the "**Six-month Period**"), including conducting financing activities where appropriate. If none of the above events has been consummated within the Six-month Period, the Company shall pay the deferred consideration to AVIC HK as soon as practicable upon the occurrence of any of the above events after the expiry of the Six-month Period and such payment shall not be construed as a default.

The arrangement pursuant to the Amendment Deed regarding the last instalment of the Consideration amounting to HK$800 million offers the Company a greater financial flexibility for its operations in the short term. It is considered that the Acquisition, with its payment terms, is in the interest of the Company and the Shareholders as a whole.

As set out in the "Letter from the Board" contained in the Circular, the Consideration was determined based on arm's length negotiations between the Company and AVIC HK, taking into account various factors, among other things:

a) the recent financial position and performance of the Target Group;

b) valuation of listed companies in the USA and companies being acquired in precedent transactions whose businesses are similar to that of the Target Group; and

c) the business prospect of the Target Group, which demonstrates the leading position of the Target Group in the worldwide general aviation aircraft piston engines market and the promising growth opportunity in the PRC which the Target Group may be able to capture in the future.

Assessment on the Consideration

For the purposes of assessing the reasonableness and fairness of the Consideration, we have (i) identified a list of transactions (the "**Comparable Transactions**"); and (ii) reviewed a number of comparable companies which are principally engaged in the manufacturing of aircraft engines or engine parts (the "**Comparable Companies**"). We have considered the trading multiples of enterprise value ("**EV**") to earnings before interest, tax, depreciation and amortisation ("**EBITDA**"), EV to earnings before interest and tax ("**EBIT**"), and price to earnings ("**P/E**") ratio of the Comparable Transactions, the Comparable Companies and the Acquisition. EV is defined as the market capitalisation plus the sum of interest bearing debts, preferred equity and minority interests minus cash and cash equivalents of a company. It is the value of a company's business and operations as a whole. EV to EBITDA ("**EV/EBITDA**") and EV to EBIT ("**EV/EBIT**") is a commonly used metric for comparing the value of a company, which can avoid distortion of taxation and/or capital structure. A lower EV/EBITDA, EV/EBIT or P/E ratio indicates a company might be undervalued and would appear more attractive to potential acquirers. Unlike asset-based companies such as property groups and banks, the Target Group is in the manufacturing sector and has been profit-making for each of the two years ended 31 December 2015 and 2016 and the six months ended 30 June 2017, therefore, we are of the view that adopting enterprise value multiples, including EV/EBITDA and EV/EBIT, and P/E ratio can provide a more meaningful comparison than price to book value ("**P/B**") ratio when valuing a profitable business.

As set out in the section headed "Conditions to Acquisition Completion" in the "Letter from the Board" contained in the Circular, settlement arrangement for outstanding loans owed to or guaranteed by related parties of the Target Group is as follows:

a) each loan receivable of The Export-Import Bank of China and Bank of China Limited from TMI and TMG respectively shall be purchased from the respective banks by AVIC HK, which will then be the new lender. AVIC HK will subsequently sell the two loans to the Target Company for the Shareholder's Note(s). Upon Acquisition Completion, such Shareholder's Note(s) will then become shareholder's loans from the Company to the Target Company at the same terms as the Shareholder's Notes' original issue; and

b) the Target Group will repay its loan from CATIC International Finance Limited using funds resulting from additional equity investment by AVIC International in TMI prior to Acquisition Completion.

As a result, there will be no outstanding loan or guarantee arrangement between AVIC International or AVIC HK and the Company after Acquisition Completion.

In light of the above loan settlement arrangement, profit generated by the Target Group for the 12-month period ended 30 June 2017 is adjusted by (i) the amount of finance costs in relation to the outstanding loans owed to or guaranteed by related parties of the Target Group for financing various acquisitions of the Target Group prior to the Track Record Period, which will no longer be incurred in the future; and (ii) the relevant income tax adjustments in respect of the finance costs mentioned in (i). Based on (a) the Consideration of HK$2,400,000,000; and (b) the adjusted financial figures of the Target Group for the 12-month period ended 30 June 2017, the EV/EBITDA, EV/EBIT and P/E ratio of the Acquisition are set out in the table below.

	For the 12-month period ended 30 June 2017 *US$'000* *(Approximately)*	**Remarks**
A. Adjusted financial figures of the Target Group		
Profit after tax *(note 1)*	6,212	A
Profit adjustments:		
(i) finance costs in relation to the outstanding loans owed to or guaranteed by related parties of the Target Group for financing various acquisitions of the Target Group prior to the Track Record Period *(note 2)*	10,241	B
(ii) estimated income tax adjustment in respect of the finance costs in (i) *(note 3)*	(3,667)	C
Adjusted profit after tax	**12,786**	D=A+(B+C)

	For the 12-month period ended 30 June 2017 *US$'000* *(Approximately)*	Remarks
B. EBITDA and EBIT of the Target Group		
Profit before tax	10,320	E
EBITDA adjustments:		
(i) depreciation and amortisation *(note 1)*	10,743	F
(ii) finance costs *(note 1)*	10,894	G
EBITDA	**31,957**	H=E+(F+G)
EBIT	**21,214**	I=E+G
Consideration *(note 4)*	307,692	J
EV/EBITDA	**9.6**	K=J/H
EV/EBIT	**14.5**	L=J/I
P/E (based on adjusted profit after tax)	**24.1**	M=J/D

Notes:

1. Profit after tax, depreciation and amortisation and finance costs for the 12-month period ended 30 June 2017 is calculated based on the audited financial statements of the Target Group for the year ended 31 December 2016 and six months ended 30 June 2016 and 2017 as set out in Appendix III to the Circular.

2. The finance costs are related to the outstanding loans owed to or guaranteed by related parties of the Target Group as at 30 June 2017 for financing various acquisitions of the Target Group prior to the Track Record Period. As discussed above, certain bank loans shall become shareholder's loans from the Company to the Target Company which are interest-free and unsecured upon Acquisition Completion and the Target Company will repay its loan from CATIC International Finance Limited using funds resulting from additional equity investment by AVIC International. As such, these finance costs would no longer be incurred by the Target Group upon Acquisition Completion and are adjusted for the calculation of the P/E ratio of the Acquisition.

3. The estimated income tax adjustment was calculated based on the income tax rate of 39.58%.

4. The exchange rate of US$1:HK$7.8 is used in the above calculation of the amount of the Consideration.

(i) EV/EBITDA, EV/EBIT and P/E ratio analysis on the Comparable Transactions

For the purposes of assessing the reasonableness and fairness of the Consideration, we have identified the Comparable Transactions.

Data of the Comparable Transactions is extracted from Mergermarket. Mergermarket is an independent merger and acquisition intelligence services provider. It mainly provides global advisory and corporate communities with intelligence and analysis. Mergermarket is part of the Mergermarket Group with a global network of 300 mergers and acquisitions journalists in 67 locations, having the largest team worldwide according to its website. According to the Mergermarket's website, their journalists monitor more than 3,000 global media sources daily, summarising the most relevant stories to supplement the information provided by their correspondents. Mergermarket maintains a database of historical deals, covers European deals greater than Euro 5 million since 1998, all American deals greater than US$5 million since 2001 and all Asia-Pacific deals greater than US$5 million since 2003. Summary information and selected financial information for the historical deals can be retrieved from its database. In view of the above, the data source from Mergermarket is reliable and widely used internationally.

The Comparable Transactions are selected based on the following criteria: (i) transactions announced in Mergermarket under the sector of "Industrial products and services" and sub-sector "Aerospace"; (ii) the target companies being engaged in manufacturing of aircraft parts, engines and engines parts and/or equipment manufacturing (excluding (a) manufacturing of materials; (b) lifting and pulling devices; (c) radar, air traffic control system; and (d) cabin interior products used in the aerospace industry); (iii) transactions announced in Mergermarket during the period from 1 January 2014 to the Latest Practicable Date; and (iv) excluding transactions where parameters not disclosed in Mergermarket. We consider the Comparable Transactions an exhaustive list of relevant comparable transactions based on the said criteria above.

Based on such criteria, we have identified ten Comparable Transactions, which provide an analysis for the purpose of assessing the Consideration. The results of EV/EBITDA, EV/EBIT and P/E ratio of the Comparable Transactions are set out in the table below.

	Date of announcement	Target company	Stock exchange and principle place of business	Principal business of the target company	Bidder	Deal value	EV/ EBITDA	EV/ EBIT	P/E
						(HK$ million)			
				(Note 1)		*(Note 1)*	*(Note 1)*	*(Note 1)*	*(Note 1)*
1	18/9/2017	Orbital ATK, Inc.	New York Stock Exchange ("**NYSE**"); USA	Develops and manufactures space systems, satellites, launch vehicles and satellite-based networks *(Note 3)*	Northrop Grumman Corporation	71,660	14.5	19.4	26.8
2	04/09/2017	Rockwell Collins, Inc.	NYSE; USA	Manufactures aviation electronics and communication equipment for commercial and military aircrafts	United Technologies Corporation	234,032	23.9	30.0	25.5

	Date of announcement	Target company	Stock exchange and principle place of business	Principal business of the target company	Bidder	Deal value	EV/ EBITDA	EV/ EBIT	P/E
						(HK$ million)			
				(Note 1)		*(Note 1)*	*(Note 1)*	*(Note 1)*	*(Note 1)*
3	19/01/2017	Zodiac Aerospace SA	Euronext Paris; France	Develops aerospace equipment and systems for commercial, regional and business aircraft, as well as helicopters and space applications	Safran SA	69,128	17.1	30.8	65.8
4	31/05/2016	Kreisler Manufacturing Corporation	OTC Pink; USA	Manufactures and sells precision metal components and assemblies for use in military and commercial aircraft engines and industrial gas turbines	United Flexible, Inc.	227	14.5	19.0	36.0
5	20/10/2016	Avio (81% stake)	BrsaItaliana; Italy	Designs, develops and produces solid-propellant space propulsion motors and tactical propulsion systems	Leonardo-Finmeccanica SpA; Space2	1,977	9.9	26.4	45.3
6	29/05/2015	Shifang Mingri Aerospace Industrial Co., Ltd.	Non-listed; China	Provides aircraft parts products	Xinjiang Machinery Research Institute Co., Ltd.	5,697	19.8	27.8	40.2
7	15/05/2015	Euravia Engineering & Supply Co. Ltd.	Non-listed; UK	Provides repair and overhaul solutions for a wide range of aircraft and helicopter gas turbine engines	Magellan Aerospace Corporation	274	6.2	6.6	11.4
8	01/06/2015	Zodiac Aerospace SA (3.65% stake)	Euronext Paris; France	Develops aerospace equipment and systems for commercial, regional and business aircraft, as well as helicopters and space applications	Fonds Strategique de Participations	3,009	16.7	19.4	26.0
9	30/01/2014	Showa Aircraft Industry Co Ltd (29.98% stake)	Tokyo; Japan	Manufactures aircraft parts and special purpose vehicles	Mitsui Engineering & Shipbuilding Co.,ltd.	1,805	18.6	48.6	90.7
10	03/03/2014	Aernnova Aerospace, S.A.U. (30% stake)	Non-listed; Spain	Provides market engineering services, composite and metallic parts and repair and product support services	Springwater Capital LLC	1,610	6.0	9.9	18.5
	Comparable Transactions:								
	Lowest						**6.0**	**6.6**	**11.4**
	Highest						**23.9**	**48.6**	**90.7**
	Average						**14.7**	**23.8**	**38.6**
	Median						**15.6**	**22.9**	**31.4**

Date of announcement	Target company	Stock exchange and principle place of business	Principal business of the target company	Bidder	Deal value	EV/ EBITDA	EV/ EBIT	P/E
					(HK$ million)			
			(Note 1)		*(Note 1)*	*(Note 1)*	*(Note 1)*	*(Note 1)*
Comparable Transactions (excluding the outliers) *(Note 2)*								
Lowest						**6.0**	**6.6**	**11.4**
Highest						**23.9**	**30.0**	**45.3**
Average						**13.9**	**19.8**	**28.7**
Median						**14.5**	**19.4**	**26.4**
The Acquisition						**9.6**	**14.5**	**24.1**

Notes:

1. The exchange rate of US$1: HK$7.81 as at the Latest Practicable Date is extracted from Bloomberg and used in the above calculation. Principal business of the target companies, deal value, EV/EBITDA, EV/EBIT and P/E ratio of the Comparable Transactions were extracted from the respective details of the Comparable Transactions in the Mergermarket.

2. The Comparable Transaction involving Zodiac Aerospace SA and Showa Aircraft Industry Co Ltd have P/E ratios over 60 times. Given the majority of the P/Es of the Comparable Transactions fall in the range from approximately 11 to 50, we consider more meaningful to exclude those with such high P/E ratios from our assessment.

3. As disclosed in Mergermarket, Orbital ATK, Inc. falls into the following sub-sectors, namely “Aerospace”, “Defence aircraft and parts manufacture” and “Missiles and missile guidance systems”. In addition to the principal business as disclosed in Mergermarket, Orbital ATK, Inc. also produces highly-engineered, lightweight and reliable structures for commercial and military aircraft programs as disclosed in its website.

Among the Comparable Transactions, the Acquisition, in terms of EV/EBITDA, EV/EBIT, P/E ratio, is lower than the average of those of the Comparable Transactions.

(ii) EV/EBITDA, EV/EBIT and P/E ratio analysis on the Comparable Companies

To enhance our analysis on the Consideration, we reviewed a number of Comparable Companies. The Comparable Companies have been selected based on the following criteria: (i) listed on the stock exchange in the United States, Western Europe, the PRC or developed Asia-Pacific countries, with country of domicile in the same countries; (ii) under the industry of “Aircraft & Parts Manufacturing” as classified by the Bloomberg Industry Classification System; (iii) principally engaged in aircraft parts, engine and engine parts manufacturing; and (iv) over 50% of total revenue was generated by manufacturing of aircraft system components, engines and engines parts during the most recent financial year. In order to have a fair and representative sample size in assessing the fairness and reasonableness of the Consideration, we have taken into account the principal business of the Target Group, i.e. manufacturing of piston engines, and also extended the business scope to manufacturing of aircraft parts, engines and engines parts and/or equipment manufacturing. Also, we have considered a threshold on revenue proportion of the relevant businesses generated by the Comparable Companies in order to select close comparables for analysis. Given that majority of operations of the Target Group involve North America and Europe, companies listed in countries in North America and Europe are selected, listed companies in the PRC and developed Asia-Pacific countries are also included to illustrate market sentiment towards the companies engaging in similar business.

Based on such criteria, we have identified 13 Comparable Companies, which provide a relevant benchmark for the purpose of assessing the Consideration. For each of the Comparable Companies, the ratios are calculated based on (i) the financial information extracted from the respective annual report, interim report or quarterly report; and (ii) the respective market capitalisation as at the Latest Practicable Date. We consider the Comparable Companies an exhaustive list of relevant comparable companies based on the said criteria above.

The results of the EV/EBITDA, EV/EBIT and P/E ratio of the Comparable Companies and the Acquisition are set out in the table below.

	Company name	**Stock code**	**Stock exchange**	**Principal business**	**Market capitalisation as at the Latest Practicable Date**	**EV/ EBITDA**	**EV/ EBIT**	**P/E**
					(Note 1)	*(Note 2)*	*(Note 2)*	*(Note 3)*
					HK$ billion			
1	Sifco Industries, Inc.	SIF:US	NYSE American	Produces, repairs, plates, machines, and markets jet engine and other aerospace components.	0.30	N/A	N/A	N/A
2	MTU Aero Engines AG	MTX:GR	Xetra	Develops and manufactures engines and offers commercial engine services and support.	73.0	13.0	18.1	21.3
3	Esterline Technologies Corporation	ESL:US	NYSE	Produces technology interface systems for commercial and military aircraft, jet engine sensors and electrical power distribution equipment, high temperature resistant materials, combustible ordinance and electronic warfare countermeasure products.	17.8	9.2	14.2	19.4
4	HEICO Corp	HEI:US HEI.A:US	NYSE	Designs, manufactures, and sells aerospace products and services through its subsidiaries.	56.3	21.6	26.2	38.8

	Company name	Stock code	Stock exchange	Principal business	Market capitalisation as at the Latest Practicable Date *(Note 1)* *HK$ billion*	EV/ EBITDA *(Note 2)*	EV/ EBIT *(Note 2)*	P/E *(Note 3)*
5	United Technologies Corporation	UTX:US	NYSE	Produces aircraft engines, elevators and escalators, heating and air conditioning equipment, helicopters, aerospace systems, fuel cell systems, and fire safety equipment.	794.5	11.7	14.7	19.7
6	Senior PLC	SNR:LN	London	Manufactures specialist engineering products for the automotive, industrial and aerospace sectors, including flexible tubing, fluid transfer devices, de-icing systems, assembly components for jet engines, and parts for automotive air conditioning systems.	11.3	11.1	22.0	27.9
7	Astronics Corporation	ATRO:US ATROB:US	ATRO US: NASDAQ; ATROB: OTC Pink	Supplies advanced technologies and products to the global aerospace, defense and semiconductor industries, including advanced, high-performance electrical power generation and distribution systems, lighting and safety systems, avionics products, aircraft structures, engineering design and systems certification, and automatic test systems.	9.4	17.2	25.3	34.2
8	Chaheng Precision Co Ltd	4546:TT	TPEx Emerging	Manufacturers and distributes precision equipment and aero-engine products.	0.78	9.3	15.3	13.9
9	TransDigm Group	TDG:US	NYSE	Manufactures ignition systems and components, gear pumps, mechanical and electromechanical actuators and controls, NiCad batteries and chargers, power conditioning devices, hold-open rods and locking devices, engineered connectors and latches, cockpit security devices, and AC and DC motors.	110.8	16.2	18.0	32.4

	Company name	Stock code	Stock exchange	Principal business	Market capitalisation as at the Latest Practicable Date *(Note 1)* *HK$ billion*	EV/ EBITDA *(Note 2)*	EV/ EBIT *(Note 2)*	P/E *(Note 3)*
10	Safran SA	SAF:FP	Euronext Paris	Designs, develops, manufactures and sells engines for aircraft, helicopters and satellites, either alone or in partnership with other companies.	341.9	6.6	8.0	10.7
11	AECC Aviation Power Co Ltd	600893.CH	Shanghai	Produces aircraft power devices, aerospace turbines, aerospace engines, and other products, also provides equipment testing, equipment maintenance, and other services.	75.0	37.6	41.8	65.4
12	Xi'an ChenXi Aviation Technology	300581.CH	Shenzhen	Designs, produces, and sells aviation GPS systems, engine controls, and other related electronic parts.	3.3	41.2	43.0	54.2
13	AECC Aero-Engine Control Co Ltd	000738.CH	Shenzhen	Produces aerospace ship power control systems, walking machinery power control systems, aircraft parts, and other products.	21.4	51.7	59.3	75.5
	Comparable Companies *(Note 4)*				**Lowest**	**6.6**	**8.0**	**10.7**
					Highest	**51.7**	**59.3**	**75.5**
					Average	**20.5**	**25.5**	**34.4**
					Median	**14.6**	**20.0**	**30.2**
	Comparable Companies (excluding outliers) *(Note 5)*				**Lowest**	**9.2**	**14.2**	**13.9**
					Highest	**51.7**	**59.3**	**75.5**
					Average	**23.3**	**29.8**	**37.5**
					Median	**14.1**	**23.7**	**31.0**
	The Acquisition					**9.6**	**14.5**	**24.1**

Notes:

1. The market capitalisation of the Comparable Companies are extracted from Bloomberg and exchange rates of US$1:HK$7.81, EUR1:HK$9.26, GBP1:HK$10.46 and TWD1:HK$0.26 as at the Latest Practicable Date are used in the above calculation.

2. The EV is calculated as the market capitalisation as at the Latest Practicable Date plus net debt (short-term and long-term debt minus cash and cash equivalents), preferred equity and non-controlling interests of a company according to the

respective annual report, interim report or quarterly report. The EBITDA and EBIT are calculated based on the profit before tax, adjusted by the depreciation and amortisation expenses and finance costs extracted from the annual reports, interim reports or quarterly reports of the respective Comparable Companies.

3. The P/E is calculated based on the (i) market capitalisations of each of the Comparable Companies as at the Latest Practicable Date; and (ii) profits attributable to the equity holders of the Comparable Companies based on the annual reports, interim reports or quarterly reports of the respective Comparable Companies.

4. Sifco Industries, Inc. recorded loss attributable to its equity holders calculated based on its latest annual report and therefore has been excluded in calculating the range, average and median of multiples of the Comparable Companies.

5. MTU Aero Engines AG, HEICO Corp, United Technologies Corporation, TransDigm Group, Safran SA and AECC Aviation Power Co Ltd have market capitalisations of over HK$24 billion, i.e. approximately ten times of the amount of the Consideration. Given the Consideration is HK$2.4 billion, it is considered that these six companies are not comparable in light of the relatively large market capitalisations of over HK$24 billion and are excluded in our assessment.

As set out in the above table, EV/EBITDA, EV/EBIT and the P/E ratio of the Acquisition fall within the range of those of the Comparable Companies. The Acquisition, in terms of the EV multiples, is at the lower end among the Comparable Companies. It is lower than the median of the Comparable Companies in terms of P/E ratio. The EV/EBITDA and EV/EBIT of the Acquisition are lower than the average EV/EBITDA and EV/EBIT of the Comparable Companies and the P/E ratio of the Acquisition is lower than the average of the P/E ratios of the Comparable Companies.

Based on the above analysis, we are of the view that the Consideration is fair and reasonable so far as the Independent Shareholders are concerned.

5. Issue price of the Consideration Shares

The total number of the Consideration Shares will be 3,783,783,783 Shares and the issue price will be HK$0.37 (the "**Issue Price**") per Consideration Share, representing:

a. a premium of approximately 1.37% over the closing price of HK$0.365 per Share as quoted on the Stock Exchange on the Last Trading Day;

b. a premium of approximately 2.78% over the average closing price of HK$0.36 per Share for the last five trading days up to and including the Last Trading Day;

c. the average closing price of HK$0.37 per Share for the last ten trading days up to and including the Last Trading Day;

d. the average closing price of HK$0.37 per Share for the last thirty trading days up to and including the Last Trading Day;

e. a discount of approximately 18.68% to the closing price of HK$0.455 per Share on the Latest Practicable Date;

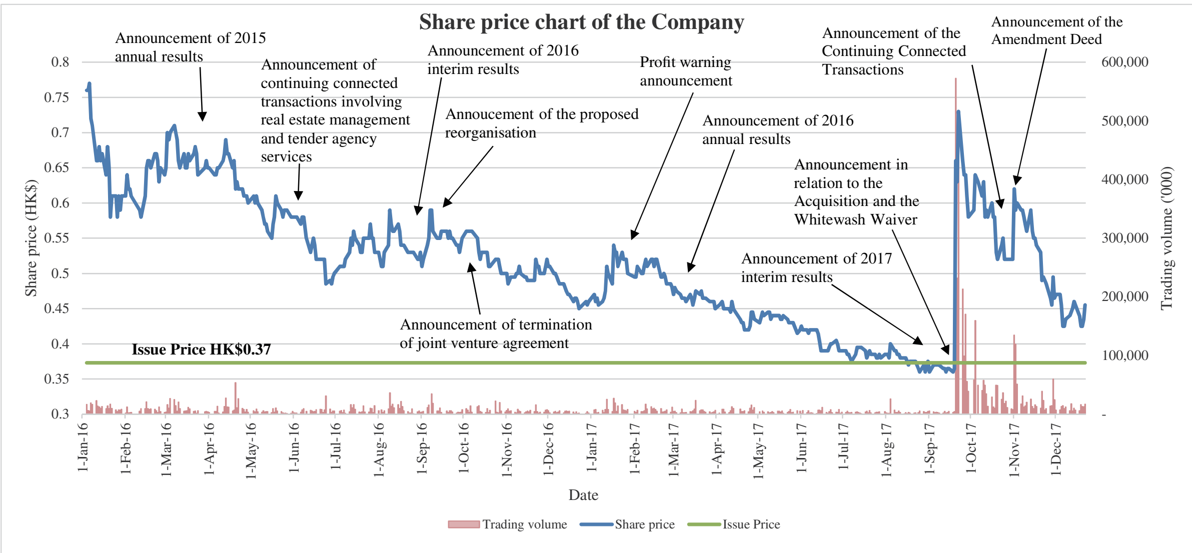
f. a premium of approximately 2.78% over the unaudited net assets value per Share of approximately HK$0.36, calculated based on the Company's unaudited equity attributable to owners of the parent of approximately HK$1,968 million as at 30 June 2017;

g. a premium of approximately 2.78% over the audited net assets value per Share of approximately HK$0.36, calculated based on the Company's audited equity attributable to owners of the parent of approximately HK$1,973 million as at 31 December 2016; and

h. a premium of approximately 12.12% to the adjusted unaudited net assets value per Share as at 30 June 2017, adjusted by its valuation as at 31 October 2017, of approximately HK$0.33, as set out in the sub-section headed "5. Issue price of the Consideration Shares — Adjusted NAV" in this letter.

Analysis of the Issue Price

The chart below illustrates the daily closing price per Share for the period from 1 January 2016 up to and including the Latest Practicable Date (the "**Review Period**").



Source: Bloomberg

During the Review Period, the closing Share price fluctuated between HK$0.36 per Share and HK$0.77 per Share, with an average Share price of approximately HK$0.52. It is noted that, in general, there was a downward trend of the Share price during the Review Period prior to the release of the announcement of the Acquisition (the "**Announcement**").

As shown in the chart above, the Shares closed between HK$0.58 and HK$0.77 during the period from 4 January 2016 to 10 March 2016, the day the profit warning announcement for the year ended 31 December 2015 was published. The Share price went down slightly to HK$0.65 per Share on the next day after the release of the profit warning announcement. The Company later issued the 2015 annual results announcement on 24 March 2016 with an improvement in performance, mainly due to the property development and investment business acquired by the Group in 2014. The Share price increased gradually subsequently for a short period of time and reached HK$0.69 on 13 April 2016.

The Share price was on a descending trend dropping from HK$0.69 on 13 April 2016 to HK$0.58 on 30 May 2016, and recorded a minimum of HK$0.55 per Share on 16 May 2016. The Company entered into framework agreements with connected parties on 31 May 2016 involving the provision for pre-handover real estate management services and tender agency services by the connected parties. The Share price maintained at HK0.58 after the release of announcement of such continuing connected transactions. The Share price dropped to a minimum of HK$0.485 on 24 June 2016.

On 17 August 2016, the Company released a profit warning announcement for 2016 interim results. The Company later published the 2016 interim results announcement on 26 August 2016, demonstrating a deteriorating financial performance of the Group for the six months ended 30 June 2016 as compared to the corresponding period in 2015. The Share price decreased by approximately 2% on the next trading day after the release of 2016 interim results.

The Share price increased by approximately 8% in early September 2016, from HK$0.51 on 1 September 2016 to HK$0.55 on 6 September 2016, and further increased to HK$0.59 on 7 September 2016 before the suspension of trading in the Shares on the same day, pending the release of an announcement in relation to a proposed reorganisation of real estate business and assets of Aviation Industry. The Company released the announcement on the proposed reorganisation later on 7 September 2016 and trading in the Shares was resumed on 8 September 2016, the Share price closed at HK$0.59 on that day.

On 30 September 2016, the Company announced the termination of joint venture agreement on establishing a joint venture company to engage in the research and development, design and manufacture of parts and components for commercial aircraft and provision of related technical services as conditions had not been satisfied. There was a slight increase in Share price of approximately 2% to HK$0.56 on the next trading day. The Share price experienced a general downward trend during the rest of the period in 2016 and closed at HK$0.46 on 30 December 2016.

The Company published a profit warning announcement for the 2016 annual results on 26 January 2017, stating that a substantial loss is expected for 2016 resulted from the unsatisfactory performance of the property development and investment business and certain investments held by the Group. The Share price decreased by approximately 4% from HK$0.52 to HK$0.5 on the next trading day. On 14 March 2017, the 2016 annual results announcement was released, showing a significant deterioration in the Company's performance as compared to 2015, resulting in a decrease of approximately 2% from HK$0.465 to HK$0.455 in the Share price on the next trading day.

On 10 August 2017, the Company issued a profit warning announcement for the 2017 interim results, it is expected that the loss would significantly decrease as compared to the same period in 2016. The Share price dropped by approximately 1% on the next trading day after the release of profit warning announcement. The Company published its 2017 interim results announcement on 25 August 2017 and the loss for the period has substantially decreased as compared to 2016. On the next trading day, the Share price increased by approximately 3% to HK$0.37 per Share.

After the publication of the Announcement on 19 September 2017, the closing price of the Shares increased sharply from HK$0.365 on 19 September 2017 (the Last Trading Day) to HK$0.66 on 20 September 2017 (the first trading day after the release of the Announcement), representing an increase of approximately 81%. In our view, the increase in the Share price was possibly attributable to the market anticipation of favourable effects of the Acquisition following the Announcement. The Share price reached a maximum of HK$0.73 on 22 September 2017.

On 24 October 2017, the Company released the announcement in relation to the Continuing Connected Transactions, the Share price remained unchanged on the next day after the release of the announcement. The announcement on the Amendment Deed was published on 27 October 2017, the Share price remained at HK$0.52 on the next trading day.

The Share price closed in a range between HK$0.425 and HK$0.62 per Share since then and closed at HK$0.455 per Share on the Latest Practicable Date.

During the Review Period, the monthly trading volume of the Shares ranged between approximately 66.2 million and 1,934.3 million, representing approximately 1.2% to 35.0% of the total issued share capital of the Company. The trading of Shares was not particularly active prior to the release of the Announcement. It is noted that the number of Shares traded daily increased significantly after the publication of the Announcement, as demonstrated by an average trading volume of approximately 3.3 million for the last five trading days up to and including the Last Trading Day and approximately 325.2 million for the five trading days subsequent to the release of the Announcement, which is believed as a result of the market response to the Acquisition.

Adjusted NAV

In evaluating the fairness and reasonableness of the Issue Price, we have taken into account the adjusted unaudited consolidated net assets (the "**Adjusted NAV**") of the Group set out in Appendix II to the Circular, based on the unaudited consolidated financial statements of the Group as at 30 June 2017 and the adjustments with reference to the valuation report as set out in Appendix V to the Circular.

	HK$ million
Unaudited consolidated NAV of the Group attributable to owners of the parent as at 30 June 2017	1,968
Adjustment:	
- Unaudited total comprehensive loss for July to October 2017 attributable to owners of the parent	(21)
- Revaluation deficit arising from the valuation of property interests attributable to owners of the parent as at 31 October 2017 *(Note 1)*	(109)
Adjusted NAV	1,838
Adjusted NAV per Share *(Note 2)*	**HK$0.33**
Issue Price	**HK$0.37**
Premium to the Adjusted NAV per Share	**12.12%**

Notes:

1. This represents revaluation deficit arising from the decrease of market value of the property interests held by the Group as valued by Jones Lang LaSalle Corporate Appraisal & Advisory Limited as at 31 October 2017 compared with their corresponding book value as at the same date, after taking into account the relevant tax impact and adjusting for relevant interests not attributable to owners of the parent.

2. Based on 5,519,591,000 Shares in issue as at the Latest Practicable Date.

As set out in the above table, the Issue Price of HK$0.37 per Share represents a premium of approximately 12.12% to the Adjusted NAV per Share of approximately HK$0.33.

Conclusion

Based on a number of qualitative and quantitative factors (as discussed below), we consider that the Issue Price is fair and reasonable to the Independent Shareholders:

(1) the Group has been experiencing operating losses for the year ended 31 December 2016 and the six months ended 30 June 2017 and there has been a declining operational performance on the Group's property development business as indicated by the continuous decrease in revenue since 2016 as set out in the section headed "3. Background of the Group and rationale for the Acquisition — (ii) Financial performance of the Group" of this letter, the comparison with recent share prices may be more appropriate in assessing the Issue Price given the recent performance of the Company;

(2) the Issue Price represents a premium of approximately 2.78% to the NAV per Share of approximately HK$0.36 as at 30 June 2017 and a premium of approximately 12.12% to the Adjusted NAV per Share of approximately HK$0.33;

(3) the Issue Price (a) is higher than the closing price on the Last Trading Day; (b) represents a premium of approximately 2.78% over the average of the closing prices for the last five trading days up to and including the Last Trading Day; and (c) equal to the average closing prices for the last ten and thirty trading days up to and including the Last Trading Day; and

(4) the benefits arising from the Acquisition, including but not limited to, (i) the performance of the existing business of the Group and the Acquisition allows the Group to achieve sustainable growth with the recent development of the PRC general aviation industry and the intentions of the PRC government in promoting the industry; and (ii) the financial effects of the Acquisition on the Group, should be evaluated as a package in assessing the fairness and reasonableness of the Issue Price.

6. Financial effects of the Acquisition

The unaudited pro forma financial information of the Enlarged Group as set out in Appendix IV to the Circular illustrates the effects of the Acquisition on the Group. The unaudited pro forma consolidated statement of profit or loss of the Enlarged Group provides an illustration of the impact of the Acquisition on the profit or loss of the Enlarged Group.

(i) Loss attributable to owners of the parent

Loss attributable to owners of the parent would decrease from approximately HK$686 million to approximately HK$318 million, mainly as a result of the gain on bargain purchase arising from the Acquisition of approximately HK$390 million. Given (i) the Target Group has been performing efficiently with positive earnings since 2015; and (ii) the benefits of the Acquisition, which is elaborated in the sub-section headed "3. Background of the Group and rationale for the Acquisition — (iv) Rationale for the Acquisition" above, we are of the view that the decrease in pro forma loss is in the interests of the Company and the Shareholders.

(ii) Equity attributable to owners of the parent

As of 30 June 2017, the Group's NAV attributable to owners of the parent was approximately HK$1,968 million. According to the unaudited pro forma financial information of the Enlarged Group set out in Appendix IV to the Circular, the unaudited pro forma net assets of the Enlarged Group attributable to owners of the parent would have increased to approximately HK$3,809 million. The NAV per Share would increase from approximately HK$0.36 per Share as at 30 June 2017 to approximately HK$0.41 per Share immediately after Acquisition Completion. The asset enhancement is considered to be in the interests of the Company and the Shareholders.

(iii) Gearing

As at 30 June 2017, the Group's gearing ratio, calculated on the basis of the interest-bearing debts as a percentage of equity attributable to owners of the parent plus interest-bearing debts, was approximately 46%. According to the unaudited pro forma financial information of the Enlarged Group set out in Appendix IV to the Circular, the gearing ratio of the Enlarged Group immediately after Acquisition Completion would decrease to approximately 31%, mainly as a result of the increase in equity attributable to owners of the parent with the allotment and issue of the Consideration Shares. We consider a decrease of gearing ratio to be in the interest of the Company.

(iv) Dilution

The Consideration Shares represent approximately 68.55% of the issued share capital of the Company as at the Latest Practicable Date and approximately 40.67% of the issued share capital of the Company as enlarged by the issue of the Consideration Shares.

	As at the Latest Practicable Date		Immediately after the allotment and issue of the Consideration Shares	
	Number of Shares	*%*	*Number of Shares*	*%*
The Concert Group	1,895,715,000	34.35	5,679,498,783	61.05
- Tacko International Limited	1,895,559,000	34.34	1,895,559,000	20.37
- AVIC HK	—	—	3,783,783,783	40.67
- Mr. Li Shangfu (a director of AVIC International)	156,000	0.00	156,000	0.00
CK Hutchison Holdings Limited	450,000,000	8.15	450,000,000	4.84
Other public Shareholders	3,173,876,000	57.50	3,173,876,000	34.11
Total	**5,519,591,000**	**100.00**	**9,303,374,783**	**100.00**

As shown in the table above, the shareholding of the existing Shareholders (other than the Concert Group) in the Company will decrease from approximately 65.65% as at the Latest Practicable Date to approximately 38.95% immediately after the allotment and issue of the Consideration Shares. AVIC HK will become the controlling Shareholder upon Acquisition Completion. Although the shareholding of the existing Shareholders (other than the Concert Group) will be diluted, having taken into account (i) the benefits to be brought about by the Acquisition; and (ii) the fairness and reasonableness of the Consideration and the Issue Price, we are of the view that the dilution effect on shareholding of the existing Shareholders acceptable.

(v) Clawback offer by AVIC HK

Conditional upon and subject to Acquisition Completion, AVIC HK will offer Qualifying Shareholders initially not more than 2,484,166,998 Offer Shares at HK$0.37 per Offer Share, which is equal to the issue price of the Consideration Shares pursuant to the Acquisition Agreement. Qualifying Shareholders are given the opportunity to participate in the Offering which allows them to maintain their shareholdings without being diluted by the Acquisition. For details of the clawback offer by AVIC HK, please refer to the section headed "IV. The clawback offer by AVIC HK" in the "Letter from the Board" contained in the Circular.

7. Important risk factors of the Acquisition

Shareholders' attention is also drawn to the section headed "1. Risk factors" in Appendix I to the Circular for the risks relating to, among others, the Acquisition, the business and industry of the Target Group when considering the Acquisition, including but not limited to:

- The business of the Target Group relies on its ability to attract and retain its senior management and other dedicated and qualified engineers and technicians.

- The Target Group's product development activities may not be successful, may be more costly than expected, or the Target Group may not be able to manufacture new developed products at a manner that meets its expected cost structure.

- Product liability claims, product recalls or other liabilities in relation to the products and services provided by the Target Group may result payments of substantial claims and other expenses that could exceed its insurance coverage.

- The Target Group is subject to the risks inherent in doing business in the USA and in other countries.

- The business operations of the Target Group may be adversely affected by strikes.

- The Target Group's success is dependent on the performance of the general aviation industry and macro-economic cycles.

- Changes on the regulation of aviation fuel may lead to higher fuel price and retirement of certain types of aircrafts.

8. Whitewash Waiver — Takeovers Code provisions

Upon Acquisition Completion, the Concert Group will be interested in approximately 61.05% of the issued share capital of the Company as enlarged by the allotment and issue of the Consideration Shares (assuming that there is no change in the issued share capital of the Company other than the issue of the Consideration Shares from the Latest Practicable Date and up to the date of Acquisition Completion). As the Acquisition will increase the Concert Group's collective holding of voting rights of the Company by more than 2%, under Rule 26.1 of the Takeovers Code, AVIC HK would be obliged to make a mandatory general offer to the Shareholders for all the issued Shares not already owned or agreed to be acquired by the Concert Group, unless the Whitewash Waiver is obtained from the Executive. In this regard, AVIC HK has made an application to the Executive for the Whitewash Waiver which, if granted, will be subject to, among other things, approval by the Independent Shareholders at the SGM by a way of poll.

Independent Shareholders should note that the Acquisition is conditional on, among other things, the granting of the Whitewash Waiver by the Executive and the approval of the Acquisition and the Whitewash Waiver by the Independent Shareholders at the SGM. Such condition precedent cannot be waived under the terms of the Acquisition Agreement. If the Whitewash Waiver is not granted by the Executive or the Whitewash Waiver is not approved by the Independent Shareholders, the Acquisition Agreement will lapse and the Acquisition will not proceed. The approval of the Whitewash Waiver by the Independent Shareholders will be therefore necessary for the Group to proceed to Acquisition Completion.

CONTINUING CONNECTED TRANSACTIONS — SALE FRAMEWORK AGREEMENT

On 24 October 2017, the Company entered into the Sale Framework Agreement with Aviation Industry, pursuant to which subsequent to Acquisition Completion, the Group will sell engines and engine parts to Aviation Industry and/or its associates (excluding the Group and the Target Group) for use in new aircraft manufacture and the sale of parts into the aftermarket for maintenance, repair and overhaul. Set out below is a summary of details of the Sale Framework Agreement.

Term:	From the Effective Date up to 31 December 2019
Pricing:	To be determined on a fair and reasonable basis based on the published price list and discounts provided based on factors including, but not limited to, volume levels
Payment:	Specific payment terms (including time and method of payment) are to be agreed between the parties by entering into specific agreement in each sale transaction

Assessment

As stated in the "Letter from the Board" contained in the Circular, the pricing is based on the published price list and discounts provided based on factors including but not limited to volume levels. The price lists of OEM and aftermarket products of the Target Group are set annually. The price lists are determined based on established benchmarks, such as producer price index, customer price index, labour costs and material costs, and are adjusted with reference to the price lists of prior year. We have discussed with the management of the Group and it is noted that the price list is available on the Target Group's website, or available upon request, and is applicable to all parties, which we consider fair and reasonable. In determining the discounts (if any) to be provided to customers, as discussed with the management of the Group, we understand that the Target Group will take into account factors, including but not limited to, the volume levels and scale of operation of customers.

As advised by the management of the Group, we understand that there are internal control measures in place to govern the conduct of the transactions under the Sale Framework Agreement. We are also advised that duty segregation to notify and review connected transactions has been set up in which the Target Group needs to report connected transactions monthly to the company secretary and financial department of the Company, and for each new transaction with Aviation Industry and/or its associates, the Target Group needs to report and compare the terms, including but not limited to, price and/or gross profit margin, of the transactions with those for products with similar features offered by the Target Group to independent third parties and get approval from the chief executive officer of the Company. We consider reasonable for the management of the Target Group to compare the terms offered by the Target Group to independent third parties on products with similar features to ensure that the pricing terms offered by the Group are no less favourable to the Group.

Reason for and benefits of the Sale Framework Agreement

As disclosed in the Circular, the Target Group has historically been selling engines and engine parts to Aviation Industry and/or its associates, such as Cirrus Design Corporation, for use in new aircraft manufacture and for the sale of parts into the aftermarket for maintenance, repair and overhaul and will continue to do so on an ongoing basis. Cirrus Design Corporation, an indirect non-wholly-owned subsidiary of Aviation Industry, is the world's largest producer of piston-powered aircraft by shipments located in the USA. Also, with the growth in the PRC general aviation industry in recent years and the intentions of the PRC government in encouraging the development of such industry, the Company, upon Acquisition Completion, will be able to seize the potential business opportunities available in such industry and benefit from the industrial development in future years. The Company considers it in its best interest to continue the business relationship between the Target Group and Aviation Industry and/or its associates upon Acquisition Completion, provided that such parties will purchase from the Target Group at prices comparable to market prices and are considered to be fair and reasonable to the Group. The Company therefore entered into the Sale Framework Agreement with Aviation Industry to govern such sales that are expected to continue upon Acquisition Completion.

Given that (i) the Group, upon Acquisition Completion, will be principally engaged in the manufacture of engines and engine components; and (ii) the Target Group, which forms part of the Group upon Acquisition Completion, has been conducting transactions with Aviation Industry and/or its associates over the years which are similar to those under the Sale Framework Agreement, and the Sale Framework Agreement represents a continuation of such business relationship, we concur with the Directors' view that the entering into the Sale Framework Agreement is in the interests of the Company and the Shareholders as a whole, and consider that the transactions under the Sale Framework Agreement are in the ordinary and usual course of business of the Group upon Acquisition Completion.

Historical figures, annual caps and basis of determination

The Target Group has been selling engines and engine parts for use in new aircraft manufacture and the sale of parts into the aftermarket for maintenance, repair and overhaul to Aviation Industry and/or its associates (excluding the Group and the Target Group). Set out below are the (i) historical transaction amounts for such sales to Aviation Industry and/or its associates during the Track Record Period; and (ii) the proposed annual caps for the sale of engine and engine parts to Aviation Industry and its associates (excluding the Group and the Target Group) for each of the three financial years ending 31 December 2017, 2018 and 2019.

	Actual transaction amounts				Proposed annual caps		
	For the year ended 31 December			For the six months ended 30 June	For the year ending 31 December		
	2014	2015	2016	2017	2017	2018	2019
(USD million)							
Sale of engines and engine parts to Aviation Industry and/or its associates (excluding the Group and the Target Group)	21.2	19.1	20.0	8.4	20.0 *(Note 1)*	22.0	24.0

Note 1: The proposed annual cap is for the full year ending 31 December 2017.

As disclosed in the Circular, the proposed annual caps were determined mainly by reference to (i) the actual historical transaction amounts for each of the three financial years ended 31 December 2016; and (ii) an adequate buffer for a potential increase in demand by Aviation Industry and/or its associates (excluding the Group and the Target Group).

The proposed annual cap for 2017 is approximately equal to the average of the actual transaction amounts for the three years ended 31 December 2016. An annual growth of approximately 10% in the proposed annual caps in 2018 and 2019 was adopted. Taking into account that the revenue of the Target Group maintained a CAGR of approximately 12% from 2014 to 2016, it is considered that theannual growth applied in estimating the proposed annual caps is reasonable, with an adequate buffer to incorporate the potential increase in demand by Aviation Industry and/or its associates. Overall, we consider that the proposed annual caps have been set by the Company with due care and are fair and reasonable.

Annual review of the Continuing Connected Transactions

Pursuant to Rules 14A.55 to 14A.59 of the Listing Rules, the Continuing Connected Transactions are subject to the following annual review requirements:

a) each year, the independent non-executive Directors must review the Continuing Connected Transactions and confirm in the annual report whether the Continuing Connected Transactions have been entered into:

   (i) in the ordinary and usual course of business of the Group;

   (ii) on normal commercial terms or better; and

   (iii) according to the agreements governing them on terms that are fair and reasonable and in the interests of the Shareholders as a whole;

b) each year, the auditors of the Company must provide a letter to the Board (with a copy provided to the Stock Exchange at least 10 business days before the bulk printing of the Company's annual report), confirming whether anything has come to their attention that causes them to believe that the Continuing Connected Transactions:

(i) have not been approved by the Board;

(ii) were not, in all material aspects, in accordance with the pricing policies of the Group if the transactions involve the provision of goods or services by the Group;

(iii) were not entered into, in all material aspects, in accordance with the Sale Framework Agreement; and

(iv) have exceeded the proposed annual caps;

c) the Company must allow, and ensure that the counterparties to the Continuing Connected Transactions allow, the Company's auditors sufficient access to their records for the purpose of reporting on the Continuing Connected Transactions as set out in paragraph (b). The Board must state in the annual report whether the Company's auditors have confirmed the matters set out in Listing Rule 14A.56; and

d) the Company shall promptly notify the Stock Exchange and publish an announcement if the independent non-executive Directors and/or the auditors of the Company cannot confirm the matters set out in paragraphs (a) and/or (b) respectively.

In light of the reporting requirements for the Continuing Connected Transactions, in particular, (a) the restriction of the values of the Continuing Connected Transactions by way of the proposed annual caps; and (b) the requirements under the Listing Rules for ongoing review by the independent non-executive directors and the auditors of the Company of the terms of the Continuing Connected Transactions and the proposed annual caps, we are of the view that there exist appropriate measures to govern the conduct of the Continuing Connected Transactions and to safeguard the interests of the Independent Shareholders.

DISCUSSION AND ANALYSIS

Independent Shareholders should consider the Acquisition based on the principal factors and reasons set out in detail above and summarised below:

1. Strategic move for the Group

The Target Group is principally engaged in the research, design, manufacturing and sales of aircraft piston engines fuelled by gasoline or diesel and engine spare parts and the provision of aftermarket service and support for general aviation aircraft through factory owned service centres. On top of the sizeable market in the USA, the development of the aviation industry in the PRC also provides opportunities for the Target Group given the growth of the industry in recent years and the intentions of the PRC government in promoting the industry. The Acquisition allows the Group to focus its business on the aviation industry and reduce its reliance on property development in the PRC. In view of the above, we consider the Acquisition a strategic move for the Group, potentially providing synergy with the overall development of AVIC Group.

2. Consideration

The Consideration of HK$2,400,000,000 is determined based on the recent financial position, performance and prospects of the Target Group, and valuation of listed companies in the USA and companies being acquired in precedent transactions whose businesses are similar to that of the Target Group. To assess the Consideration, we have identified Comparable Transactions and noted that the Acquisition is priced below the average of the Comparable Transactions in terms of EV multiples and P/E ratio. We have also identified Comparable Companies which are principally engaged in aircraft parts, engine and engine parts manufacturing and conducted EV multiples and P/E ratio analysis. The EV multiples and P/E ratio of the Acquisition are also lower than the average for the Comparable Companies.

3. Settlement of the Consideration

The Consideration will be satisifed as to HK$1,000,000,000 in cash and as to HK$1,400,000,000 by way of allotment and issue of the Consideration Shares to AVIC HK at the Issue Price of HK$0.37 per Share.

The Issue Price of HK$0.37 per Consideration Share represents premia of approximately 1.37% and 2.78% to the closing price on the Last Trading Day and the average closing price for the last five trading days up to and including the Last Trading Day respectively, and is equal to the average closing prices for the last ten and thirty trading days up to and including the Last Trading Day. The Issue Price also represents a premium of approximately 12.12% to the adjusted NAV per Share of the Group as at 30 June 2017, adjusted by its valuation as at 31 October 2017.

4. Financial effects of the Acquisition

Based on the unaudited pro forma financial information of the Enlarged Group as set out in Appendix IV to the Circular, the loss attributable to owners of the parent would decrease from approximately HK$686 million to approximately HK$318 million, mainly as a result of the gain on bargain purchase arising from the Acquisition of approximately HK$390 million. The equity attributable to owners of the parent would increase from approximately HK$1,968 million to approximately HK$3,809 million and NAV per Share immediately after Completion will increase from approximately HK$0.36 per Share to approximately HK$0.41 per Share. The gearing ratio (defined as interest-bearing debts as a percentage of equity attributable to owners of the parent plus interest-bearing debts) of the Group as at 30 June 2017 was approximately 46%. The gearing ratio of the Enlarged Group immediately upon Acquisition Completion would decrease to approximately 31%.

5. Decrease in Independent Shareholders' percentage shareholding

The shareholding of the existing Shareholders (other than the Concert Group) in the Company is expected to be diluted from approximately 65.65% as at the Latest Practicable Date to approximately 38.95% immediately after the allotment and issue of the Consideration Shares. The dilution is itself an unattractive feature, but in our view should be assessed in the context of the benefits of the Acquisition as a whole as discussed above. In this context, we consider the potential dilution is acceptable. Qualifying Shareholders should note that AVIC HK will offer initially not more than 2,484,166,998 Offer Shares at HK$0.37 per Offer Share, which is equal to the Issue Price in the Offering. The offering allows Qualifying Shareholders to maintain their shareholdings without being diluted by the Acquisition.

6. The Whitewash Waiver

In the event that the Acquisition and the Whitewash Waiver are not approved by the Independent Shareholders at the SGM, the Acquisition Agreement will lapse and the Acquisition will not proceed. In such circumstances, the Company and the Independent Shareholders will be unable to benefit from the Acquisition as discussed above.

Upon Acquisition Completion, the holding of the Concert Group will increase from approximately 34.35% to 61.05%, which will allow the Concert Group to buy further Shares in due course without triggering a general offer. In the context of the strategic acquisition of the Target Group and the benefits discussed above, we consider this justified.

7. Continuing Connected Transactions upon Acquisition Completion

The entering into the Sale Framework Agreement represents a continuation of the business relationship between the Target Group and Aviation Industry and/or its associates upon Acquisition Completion. The pricing of the transactions contemplated is based on the published price list and discounts provided based on factors including but not limited to volume levels. The conduct of the Continuing Connected Transactions is governed by internal control measures of the Group, including but not limited to, review by management of the Group and the independent non-executive directors and auditors of the Company. The proposed annual caps of the Continuing Connected Transactions were determined mainly with reference to historical transaction amounts plus a reasonable annual growth rate. We are of the view that the Sale Framework Agreement is on normal commercial terms and fair and reasonable so far as the Company and the Independent Shareholders are concerned.

OPINION AND RECOMMENDATION

Having taken into account the above principal factors, we consider that (i) the Acquisition (including issue of the Consideration Shares), while not in the ordinary and usual course of business of the Group because of the size of the Target Group, is fair and reasonable, on normal commercial terms and in the interests of the Company and the Shareholders as a whole; (ii) the granting of the Whitewash Waiver is fair and reasonable in the circumstances; and (iii) the terms of the transactions to be carried out pursuant to the Sale Framework Agreement (including the proposed annual caps) are fair and reasonable, on normal commercial terms, in the ordinary and usual course of business of the Enlarged Group and in the interests of the Company and the Shareholders as a whole. We therefore advise the Independent Board Committees to recommend, and we ourselves recommend, the Independent Shareholders to vote in favour of the relevant ordinary resolutions to be proposed at the SGM.

Yours faithfully,
for and on behalf of
SOMERLEY CAPITAL LIMITED

David Ching	**Donald Chung**
Director	*Director*

Mr. David Ching is a licensed person registered with the Securities and Futures Commission and a responsible officer of Somerley Capital Limited, which is licensed under the SFO to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities. He has over fifteen years of experience in the corporate finance industry.

Mr. Donald Chung is a licensed person registered with the Securities and Futures Commission and a responsible officer of Somerley Capital Limited, which is licensed under the SFO to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities. He has over ten years of experience in the corporate finance industry.

RISKS RELATING TO THE ACQUISITION

Acquisition Completion is subject to the fulfilment of conditions precedent as set out in the Acquisition Agreement, and may not take place as contemplated, or at all

The Acquisition Completion is subject to the fulfilment of conditions precedent to completion as set out in the Acquisition Agreement. Certain of these conditions precedent involve the actions and decisions of third parties including relevant regulatory authorities, which are not within the control of the contracting parties to the Acquisition Agreement. The Company cannot assure you that all or any of the conditions precedent as set out in the Acquisition Agreement will be fulfilled or the completion of the Acquisition will take place as contemplated, or at all.

RISKS RELATING TO THE BUSINESS OF THE TARGET GROUP

Relocation of production facilities may encounter delays caused by events that are unforeseeable by and beyond the control of the Target Group

The Target Group plans to build a new manufacturing and office centre in Mobile to enhance its operational and energy efficiency and personnel productivity. However, unforeseen events that are beyond their control (for instance, adverse weather, postponement of regulatory approvals, permits and licenses, labour disturbances and deferment of delivery of equipment), may delay the anticipated timetable, and the actual costs, of the construction.

The Target Group's business relies on its ability to attract and retain its senior management and other dedicated and qualified engineers and technicians

The Target Group depends on its senior management (for biographies of the Target Group's senior management, please refer to section headed "Appendix I — Information about the Target Group — 6. Directors and Senior Management — Senior Management of the Target Group") and qualified engineers for the smooth operation of its factories and execution of its business plans. In addition, the Target Group relies significantly on its engineers and technicians to manufacture its products and render its services to customers. The Target Group's staff is critical to maintaining the quality of its products and services and to upholding its reputation. The continuing services of its executive directors, senior management team, qualified engineers and technicians are crucial to its future success. If its executive directors or members of senior management as set out in "Directors and Senior Management" in this circular are unable or unwilling to continue their services with the Target Group, the Company may not be able to replace them with qualified candidates in a timely manner, or at all, which may result in material adverse changes to the established brand image, reputation, product quality or standards of the Target Group, and in turn, may disrupt its business, and materially and adversely affect its business, results of operations and financial condition. Furthermore, to maintain the quality of its products and services and further grow its business, the Target Group needs to continue to attract and retain qualified engineers and technicians who are able or willing to work with it and able to meet its high standards. The Target Group might have difficulties to locate qualified workers with the necessary experience and qualifications who meet its standards to join its production lines. There is no guarantee that the Target Group can retain or recruit such key personnel in the future.

The Target Group's product development activities may not be successful, may be more costly than expected, or the Target Group may not be able to manufacture new developed products in a manner that meets its expected cost structure

The Target Group has engaged in a significant level of product research and development activities. Its new products may not meet its customers' expectations, industry standards, or other factors which may affect its products or services or make them less desirable or obsolete. To maintain its position in the market, the Target Group will need to continue its investment in research and development. As a result, it may limit or divert resources from other departments or potential investments. If the capital injected in its product development activities is not able to meet its anticipated outcomes, its future sales and margins could be affected.

Product liability claims, product recalls or other liabilities in relation to the products and services provided by the Target Group may result in payments of substantial claims and other expenses that could exceed its insurance coverage

The sale of the products of the Target Group and the services provided by the Target Group expose it to a certain level of risks of product liability and claims arising from accidents of general aviation aircraft in which the products of the Target Group were installed. The Target Group has had in the past liability claims relating to its products, and it currently is subject to the same liability claims and also in the future for both its past and current products. The Target Group expects that some of these claims may have a material adverse impact on its business and cash flows. The services the Target Group offered to its customers are also subject to claims with respect to the services provided. Such liability claims can be expensive to defend and may cause reputational damage. The Target Group believes that it has appropriate insurance coverage policies that enable it to cover any related claims. However, the insurance coverage currently in place may not cover all liabilities or be available in the future at a cost acceptable to us. As a result, if the Target Group has a product liability claim, and where the liabilities are not covered or fully covered by its insurance or for which rectification or other recovery is not available, it could have a material adverse impact on the business, cash flows and operations of the Target Group. For the year ended 31 December 2014, 2015, 2016 and for the six months ended 30 June 2017, the Target Group's product liability and other related expenses amounted to US$10,244,000, US$(3,800,000), US$3,982,000 and US$696,000 respectively. As at the Latest Practicable Date, the Target Group's product liability provisions amounted to US$10,000,000.

Product liability provisions are the provisions estimated by the management of the Target Group when there are present or future expected product liability claims. Each year, the management of the Target Group would assess the Target Group's financial exposure to these claims or expected claims by taking account into (1) the coverage of the available insurance policies for the relevant financial year, (2) the nature and development of the relevant actions, (3) the merits and the likely outcomes of the cases and (4) past experiences. As explained on page III-57 of the circular, the management of the Target Group would consult the insurers and legal counsels in assessing these factors to provide an accurate provision for the relevant year. Product liability and other related expenses during the Track Record Period (see page I-69) provide a snapshot of the amount actually incurred by the Target Group on the compensation and expenses for the product liability claims for each financial year.

The suppliers of the Target Group may not be able to supply it with materials or parts which are of a quality or quantity that is sufficient to meet its production needs

The Target Group is dependent upon its suppliers to supply it with the parts and raw materials used in the manufacture of engines that it sells to its customers. The Target Group may from time to time experience an increase in costs for parts or raw materials that it sources from its suppliers, or it may suffer a shortage of parts or raw materials for several reasons, such as sudden high demand in the whole aviation industry resulting in shortages in parts and raw materials it uses, sudden loss of a significant supplier, work stoppages, or production difficulties that may affect its suppliers. In addition, global economic uncertainty may have impact on the financial stability of its suppliers and may affect their financing ability, which may affect their ability to deliver parts and materials to the Target Group. The Target Group's customers rely on it to deliver its products on time and have certain rights if its products cannot meet the agreed standards. If the Target Group cannot manage its suppliers and supply costs well, it could result in the delay of its customer contracts and may damage its reputation and its customer relationships. Moreover, sourcing and quality issues that its suppliers may face can adversely affect the quality and effectiveness to produce and deliver the Target Group's products and services and may result in liability or reputational harm. It could have a material adverse impact on its business, cash flows and operations.

Additional tax expense or additional tax exposures could affect its future profitability

The Target Group is subject to income taxes in the USA, Germany and the PRC. Its tax liabilities are dependent upon the distribution mix of operating income among these different jurisdictions. Its tax expense includes estimates of tax that may be incurred and reflects various assumptions that may impact the valuation of its deferred tax assets and liabilities. Its on-going operations could be adversely affected by changes in the effective tax rate, such as changes in tax incentives.

The Target Group is subject to the risks inherent in doing business in the USA and in other countries

In FY2016, approximately 80% of the total sales of the Target Group were made to customers in North America. Its business and operations may be subject to risks associated with doing business in the USA and internationally, including:

- Import and export controls;
- Changes in regulatory environments;
- Potential adverse tax consequences; and
- Fluctuations in foreign exchange rates.

The intellectual property rights of the Target Group may not be sufficient to protect its products or technologies

It is important for the Target Group to protect and obtain patents or rights to patents, protect trade secrets and prevent its competitors from infringing on its patents, trademarks and other intellectual property rights for its operations. The Target Group will only be able to protect its intellectual property from unauthorised use only when it is well covered by valid and enforceable patents, trademarks, or licenses. The intellectual property rights of the Target Group may not be sufficient to protect its products or technologies. Additionally, the laws for other foreign countries might not recognise intellectual property rights or protect them to the same extent as do the laws of the USA. The current or future technologies of the Target Group may, regardless of its intent, infringe upon the patents or violate other proprietary rights of third parties. In the case of such infringement or violation, the Target Group may face material litigation. If the Target Group is unable to protect its existing patent and any future patents it may register, it could have a material adverse impact on the business, cash flows and operations of the Target Group.

The business operations of the Target Group may be adversely affected by information systems interruptions or intrusion

The Target Group relies on its information systems throughout its operations to support its multiple business activities function. If these information systems do not operate properly or are subject to cyber security attacks, the Target Group could experience production downtimes, delays in operations, other major impacts on its operations or its capability to manufacture products and services to its customers. If the Target Group suffers from a corruption of data, security outbreak, loss of confidential or protected information or inappropriate use of its systems, this could have a material adverse impact on its business, financial condition, operations and cash flows. However, the Target Group will endeavour to mitigate these risks by improving its internal control, enhancing employee training, monitoring and employing appropriate measures to lower the risk of such threats.

Some of the Target Group's facilities located in the coastal regions of southeastern USA may be subject to damage and interruptions from adverse weather

Some of the Target Group's production facilities are located in the coastal regions of southeastern USA. These facilities are vulnerable to the risks associated with hurricanes and tropical storms. In addition to the damages to the facilities, the adverse weather may interrupt the Target Group's USA operation by affecting employees' accessibility to traffic for work, causing a loss of power, and/or restricting the delivery of supplies by the suppliers and finished products to the customers. Although CMI has obtained insurance for such damages and maintained a storm and disaster preparation procedure, the damages and interruptions resulting from adverse weather may still severely harm the Target Group's operation and reputation.

The business operations of the Target Group may be adversely affected by strikes

CMI is operating under a one-year contract with the United Autoworker's Local Union 1639 (the "**UALU**") that covers the wages, benefits and holidays of factory workers which will expire on 20 March 2018. At the beginning of 2018, CMI expects to start negotiations with UALU to establish the terms of the renewal with the intent to complete negotiation prior to the contract's expiration. If negotiation with the UALU is not successful by 20 March 2018 and the parties do not agree to extend the contract term by mutual agreement for a brief period to allow negotiations to continue, the one-year contract will expire and the factory workers under UALU will have the option to strike.

As regards the German operations, TMG has ongoing negotiations with the labour union regarding the conclusion of a company collective bargaining agreement ("**CBA**"), which contains a new remuneration structure and is envisaged to take effect upon the conclusion of negotiations originally scheduled for the end of 2017, but likely now not expected to finish until early 2018. The labour union could in principle try to seek the conclusion of a CBA by initiating a labour action.

Strikes may cause delay in the Target Group's projects or interruption of business operations of the Target Group. Extended negotiations with labour unions could divert management and employee attention from ensuring effective daily business operations, prevent delivery to customers and hurt the business' reputation.

The Target Company cannot assure that the above risks and uncertainties will not affect the operations of the Target Group. If the risk of strikes materialises, it could have a material and adverse effect on the business, financial position and results of operations of the Target Group.

RISKS RELATING TO THE INDUSTRY OF THE TARGET GROUP

The Target Group's success is dependent on the performance of the general aviation industry and macro-economic cycles.

The business of the Target Group is affected by the global general aviation industry and macro-economic conditions. The Target Group is subject to macro-economic cycles that affect oil prices and personal wealth. This may in turn result in reduced orders or payment delays as its customers and suppliers face economic challenges during recessions. In addition, the general aviation industry has historically experienced impact from downward economic cycles from time to time which lower overall demand for piston engine and aircraft related component replacement parts and repair and overhaul services. As a result, the Target Group may suffer from lower sales and higher credit risk. Demand for piston engine aircrafts can be affected by the general aviation industry's demand, government policies, price and other competitive factors. Change in the global general aviation industry and macro-economic conditions may have material adverse impact on the business, financial condition and results of operations of the Target Group.

Changes on the regulation of aviation fuel may lead to higher fuel price and retirement of certain types of aircrafts

Currently, the USA government is in the research and development process to identify a suitable replacement to 100LL aviation fuel to eliminate lead emissions. It is expected the price of such new aviation fuel will be higher than 100LL aviation fuel. If a new type of aviation fuel is identified and authorised by FAA and the FAA requires the use of using such new aviation fuel to replace 100LL aviation fuel, users of certain types of aircrafts may decide to retire their aircrafts due to the higher fuel price, or change their engines to diesel models depending on the change costs, which may lead to the decrease in demand of the gasoline engine products of the Target Group, and could have a material adverse impact on its business, cash flows and operations.

Political and economic uncertainty in the European Union could adversely impact the business, results of operations, financial condition and prospects of the Target Group

Credit rating downgrades in certain European countries and/or speculation regarding changes to the composition or viability of the EU create uncertain global economic conditions. The UK voluntary voting to exit from the EU, generally denoted as "Brexit", triggered financial volatility, including a drop in value of the British Pound ("**GBP**") in comparison with the USD and the EUR. Moreover, a detailed negotiation will be needed to determine the future relationship of the UK and the EU, and the uncertainty before, during and after the negotiation could have an adverse economic impact and may create further market volatility. Such ongoing uncertainty may have a large impact on the market environment, and result in financial consequences for business operating in the EU and beyond.

The Target Group derives a portion of its revenues from non-US sales and is subject to the risks inherent in doing business outside the U.S, including the EU. For FY2016, approximately 12% of its sales were made to customers in the EU. The future impact of Brexit and continued uncertainty in market conditions could have a material adverse impact on the business, cash flows and operations of the Target Group.

If the Target Group is unable to react quickly to technological change, demand for its products may be affected

The industry the Target Group operates in requires it to continue to innovate, design, develop and manufacture new products and enhancements on a timely and cost effective basis. The competitors of the Target Group may be able to develop technologies and products ahead of it and are more effective than those the Target Group develops. With ongoing technological innovation, there may be new aircrafts not powered by piston engines, which may in turn lead to decreased demand in the products of the Target Group and adversely affect its business and results of operation. In addition, the Target Group's technologies and products could become uncompetitive if new industry standards emerge. It is important for the Target Group to modify its products quickly to remain competitive.

Future terrorist attacks, wars, or other civil disturbances could negatively impact the business of the Target Group

Terrorist attacks, wars or other civil disturbances could result in economic instability and lower the demand of the products and services provided by the Target Group, which could adversely affect its business and results of operations. Terrorist attacks in the past have caused instability in the global economic environment and also the aviation industry. The Target Group cannot foresee the long-term effects of terrorist attacks on its operations.

The information that appears in this Industry Overview has been prepared by Euromonitor International Limited ("**Euromonitor**") and reflects estimates of market conditions based publicly available sources and trade opinion surveys, and is prepared primarily as a market research tool. References to Euromonitor should not be considered as the opinion of Euromonitor as to the value of any security or the advisability of investing in the Company. The Directors believe that the sources of information contained in this Industry Overview are appropriate sources for such information and have taken reasonable care in reproducing such information. The Directors have no reason to believe that such information is false or misleading or that any material fact has been omitted that would render such information false or misleading. The information prepared by Euromonitor and set out in this Industry Overview has not been independently verified by the Group, the Financial Adviser or any other party involved in the proposed acquisition and neither they nor Euromonitor give any representations as to its accuracy and the information should not be relied upon in making, or refraining from making, any investment decision.

COMMISSIONED REPORT FROM EUROMONITOR

This "Industry Overview" section contains information extracted from a commissioned research report prepared by Euromonitor (the "Euromonitor Report") for the purposes of this circular. Established in 1972, Euromonitor is a global research organisation and the private independent provider of business intelligence on industries, countries and consumers. We agreed to pay a fee of approximately US$61,800 for the Euromonitor Report.

Euromonitor did not source any information from research reports commissioned by the Target Company, the Company and/or their associates; however, as per the agreed project methodology, an interview with the Target Group was used as one of the inputs to identify market share of companies.

Research methodologies

In compiling and preparing the Euromonitor Report, Euromonitor used the following methodologies to collect multiple sources, validate the data and information collected, and cross-check each respondent's information and views against those of others:

- Secondary research, which involved reviewing published sources including official statistics such as the Bureau of National Statistics of USA, specialist trade press and associations such as the National Business Aviation Association, company reports including audited financial statements where available, independent research reports, and data based on Euromonitor's own research database.

- Primary research which involved interviews with a sample of leading industry participants and industry experts for and insights on future trends and to verify and cross check the consistency of data and research estimates.

- Review and cross-checks of all sources and independent analysis to build all final estimates including the drivers, opportunities, and future trends of the aircraft piston engine manufacturing market and prepare the final report.

Forecasting bases and assumptions

Euromonitor Report is based on the following assumptions:

- The economy of the USA is expected to maintain steady growth over the forecast period;

- The social, economic, and political environment of the USA is expected to remain stable in the forecast period;

- There will be no external shock, such as financial crisis or raw material shortage that affects the demand and supply of aircraft piston engine manufacturing in the USA during the forecast period; and

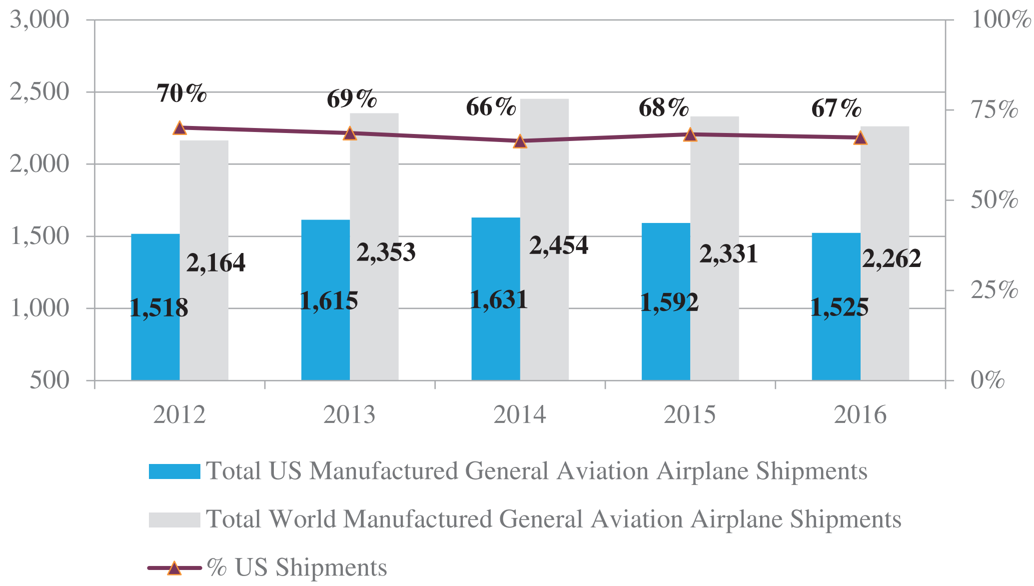
- Key market drivers discussed in the report are expected to boost the development of the aircraft piston engine manufacturing in the USA.

The research results may be affected by the accuracy of these assumptions and the choice of these parameters. The market research was completed in June 2017 and all statistics in the Euromonitor Report are based on information available at the time of reporting. Euromonitor's forecast data comes from analysis of historic development of the market, the economic environment and underlying market drivers, and is cross-checked against established industry data and trade interviews with industry experts.

US place in the Worldwide General Aviation Market

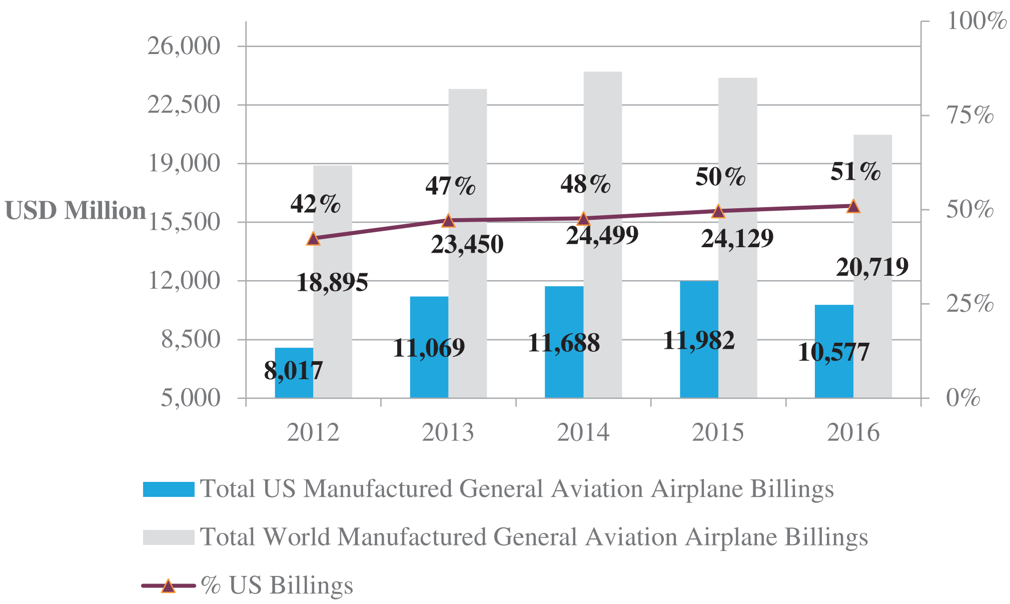
Today the US remains the global leader in terms of general aviation aircraft fleet size and pilot population as well as general aviation aircraft shipments and revenues, the position it has long held. As of 2016, of the 280,000 registered general aviation aircraft worldwide, 77% were in the American fleet; taken together the US, Canadian and European markets comprised a staggering 86% of the total general aviation aircraft fleet. In 2016, Australia, Brazil, China, New Zealand and South Africa accounted for the majority of the remainder. However, in these countries, the majority of aircraft are manufactured elsewhere with the exception of Brazilian business jets.

Chart 1 US General Aviation Aircraft Shipments % Worldwide Shipments, 2012-2016



Source: General Aviation Manufacturers Association

Chart 2 US General Aviation Aircraft Billings % Worldwide Billings, 2012-2016



Source: General Aviation Manufacturers Association

Today the US continues to produce approximately 70% of the world's certified aircraft and accounts for around half of all revenues in general aviation aircraft manufacturing. Facing with a mature and saturated market in North America and Western Europe, the general aviation industry faces unique challenges in accessing presently untapped markets. As economic growth and disposable incomes rise in the newly developed countries, a lack of infrastructure and burdensome regulatory procedures create challenges for market expansion in economies that have also recently cooled. In 2016, growth in Latin American, Asia Pacific and the Middle East and Africa remained soft. However, there are promising signs on the horizon as exemplified by changes taking place in China, the largest potential market.

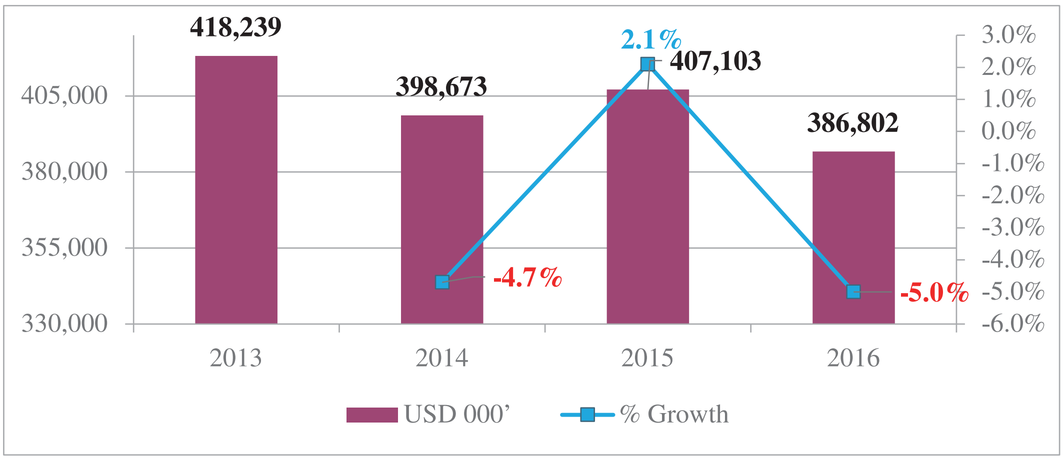
Of particular note, piston engine rotorcraft, which are primarily used for personal ownership and as primary training vehicle, are manufactured almost exclusively in the US. Sales for piston rotorcraft have been trending downward at an even faster rate.

In the **piston engine aircraft segment**, US manufacturers dominate the industry, a position they have held since the late 1920s. While piston aircraft sales declined around 4% worldwide in 2016, the US did regain its position in terms of market share which inched up slightly. Collectively, Diamond Aircraft, Textron's Beechcraft and Cessna brands, and Cirrus piston engine aircraft account for 62% of shipments worldwide.

THE AIRCRAFT PISTON ENGINE MANUFACTURING INDUSTRY IN THE USA

Aircraft Piston Engine Manufacturing in the US

Chart 3 US Aircraft Piston Engine Sales + MRO + Spares Revenue, 2013-2016



Source: Euromonitor estimates from desk research and trade interviews with major piston engine aircrafts manufacturers, leading aircraft piston engine manufacturers / distributors and the relevant trade associations in the USA

The US piston engine sales + MRO + spares market declined 5% Y-o-Y from $407.1 million in 2015 to $386.8 million in 2016. Revenues did demonstrate fluctuations between 2013 and 2016.

Today the industry continues to face significant challenges as demand from OEM manufacturers of piston engine aircraft in markets beyond North America and Europe has failed to materialise. Consumer demand in these countries, particularly in China, India, Russia and Brazil, has not materialised as expected and commercial air flight has become affordable for more and more consumers in the mature markets of North America and Europe.

The industry (US piston engine sales + MRO + spares) is very concentrated with the top 2 players controlling approximately 88% of revenue shares in 2016. Each of the companies operates as either a wholly owned subsidiary or division of a much larger parent company. Faced with decades long relationships between OEM aircraft manufacturers, the leading three companies have focused on technical improvements in engines within their core competency and improving after service channels and developing strategic alliances around the world to tap into markets in the developing world.

Key Types of Aircraft Piston Engine

Today's predominant piston engine for general aviation aircraft is the horizontally opposed air cooled piston engine with four, six and sometimes, eight, cylinders arranged in two lines on both sides of the crankshaft. Engines are classified according to fuel type: diesel or gasoline (compression ignition or spark ignition).

Most engines are considered four strokes — intake, compression, power and exhaust — engines which require two revolutions of the crankshaft to accomplish the four stroke cycle. The number of strokes that occur per revolution vary based on the number of cylinders; with more cylinders, the more evenly spaced the strokes, the more smoothly the engine runs.

Two stroke engines (all strokes accomplished in one revolution of crankshaft) are used in very small ultralight aircraft and some diesel engines. This engine type provides a high power to weight ratio advantage.

Piston aircraft engines are efficient and provide a lower cost of entry into the general aviation aircraft engine market. The majority of piston powered aircrafts tend to be smaller, capable of holding up to 6 passengers and typically fly missions less than 300 miles in distance at speeds up to approximately 240 ktas for single piston aircraft and up to 285 ktas for dual piston engine aircraft.

Value Chain Structure

Inbound Logistics

Aircraft piston engine manufacturing utilises various grades and alloys of iron, steel, aluminum, and titanium and plastic components. Establishing relationships with dependable suppliers of high grade raw materials of consistent quality is of paramount importance.

Production

Aircraft piston engine manufacturing requires a highly skilled workforce in engineering and operations to support research and development, product testing and workflow operations. This industry emphasises quality control and precision manufacturing techniques. Efforts to minimise the number of production lines and an emphasis on automated processes involving robotic manufacturing processes have become industry norms. These processes require electronically controlled quality checks with skilled human oversight.

Aircraft piston engine manufacturers also rely on strategic alliances to power manufacturing via parts manufacturing approval (PMA) agreements. Because of the high level of maturity in traditional markets and as competition for international opportunities increases, established leaders in the industry must work to gain market share by taking it from their competitors.

Marketing and Sales

In the US market, relationships between market leaders in piston engine manufacturing and OEM manufacturers of general aviation single piston and multi piston engine fixed wing aircraft as well as the US military are well established relationships that have existed for many years and/or is a result of vertical integration resulting from merger and acquisition activities.

In the North American and European markets, while general piston engine manufacturing segment remains critically important for manufacturers and must be attended to, today's manufacturers must rely upon network of talented dealers and distributors in the field who can successfully market services (rebuild and overhaul) for aircraft in the existing fleet. Marketing and sales operations must also successfully target the growing opportunities within the light sport aircraft (LSA) and unmanned aircraft systems (UAS) markets both in the US and abroad.

After Sales Service

With nearly 50% of annual revenues for piston aircraft manufacturers generated by operations other than new aircraft sales, industry participants must provide a broad based network of quality maintenance, repair and overhaul (MRO) centers. The high costs and long lifespans of general aviation aircraft mean that aircraft are in operation for many years and quality MRO is a must.

MARKET DRIVERS & CONSTRAINTS

MARKET DRIVERS

Drivers of General Aviation in North America and US

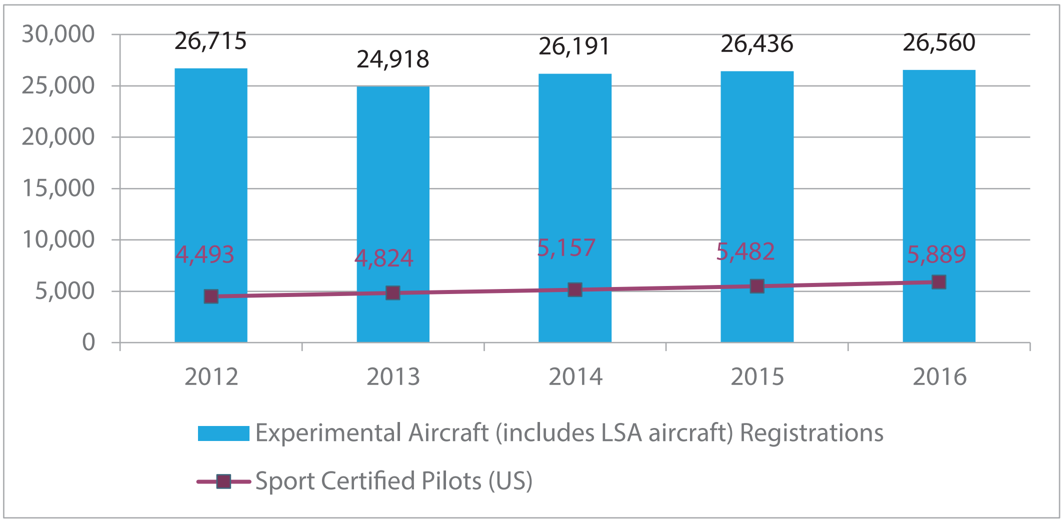
Factors that drive demand for general aviation, in the traditionally strong yet mature markets of North America and Europe, by default, drive demand in the general aviation piston engine manufacturing segment as well. As discretionary incomes rise and unemployment dips, the possibility of participating in general aviation activities and purchasing general aviation aircraft increases, particularly in those segments of the population with annual household incomes greater than US$150,000. Improving conditions for business travel and continued challenges of "flying commercial" in these markets also support the demand for general aircraft piston engines.

Technological Innovation

While these markets have matured in terms of sales, technological innovation by the major players in the US has been in a growth phase in all aspects of the industry — manufacturing processes, product design and aftermarket capacities. Advancements in production have not only supported improvement in quality of product, but have also worked to streamline production costs.

Increasing Interest in Light Sport Aircraft (LSA)

Chart 4 US Experimental Aircraft Registrations and Sport Certified Pilots, 2012 - 2016



Source: General Aviation Manufacturers Association, 2016 Databook

Registrations in the US for LSA remained relatively stable in the period 2012-2016, indicating that interest in the LSA market is not going away. According to Federal Aviation Administration Statistics of the US, during the same period, the number of active sport certified pilots in the US increased from 4,493 in 2012 to 5,889 in 2016. The LSA seaplane is getting considerable attention and fits an unique market niche. As of 2016, there were 136 aircraft models available to the LSA market in the US. However, growth in the LSA market has been slower than analysts predicted in materializing, with new FAA regulations eliminating some of the medical requirements for general aviation aircraft pilots, it is hoped that this market will realise its potential.

Future of Unmanned Aviation Systems (UAS)

Rising interest in applications for unmanned aviation systems (UAS) for civilian use abound in both the US and global markets. While cargo delivery service programs have received the greatest attention, UAS applications are suitable for a host of other purposes in numerous sectors including agriculture, security, property management, and insurance to name just a few.

MARKET CONSTRAINTS

Growth in Business Jet and Turbine Powered Aircraft in General Aviation in the US

While piston engine aircraft have continued to struggle to maintain market share in the general aviation sector, business jet and turbine powered aircraft have demonstrated greater resiliency in the review period (2012-2016), with total number of turbine aircraft sales averaging 827 per year, although this number is still lower than the peak which happened in 2006, it represents a 14% increase over the period 2009-2011 and a marked improvement since 2010 when turbine aircraft shipments reached a low of 588. Technological improvements in modern turboprop aircraft allow them to operate at speeds comparable to small regional jet airliners, while using just two-thirds fuel per passenger. Rising economic prospects and heightened security needs will continue to stimulate business jet travel. Furthermore, while both turboprop and business jet aircraft are priced higher than piston powered aircraft, innovative ride sharing programs are helping to bring these costs down for the general public.

High Costs of Certification, Product Liability and Excess Capacity Pressure Profit Margins

Faced with the perfect storm — burdensome and costly processes for certification and liability insurance for both aircraft piston engines and aircraft, a general downturn in the demand for piston engine aircraft in the industry's traditional strongholds of North America and Europe, and less than forecasted growth in developing markets to date — have simultaneously driven the price of piston engine aircraft upward at a time of declining demand, leaving aircraft piston engine manufacturers carrying excess capacity and shrinking profit margins.

Challenges in the Aftermarket Service Sector

Aftermarket sales and service related activities support more than 50% of aircraft piston engine manufacturers' annual revenues. The vast majority of these activities take place in small owner operated shops in small towns in or near general aviation airports. These locations must meet FAA standards while servicing an ever expanding number of aircraft models comprised of new aircraft and an aging fleet of aircraft with an average age of 38 years for which multiple models exist. Business owners operating in this segment of the market face their own unique challenges.

While much attention has been given to the pilot shortage in the US, a similar trend is occurring for mechanics of general aviation aircraft as older mechanics retire and competition for newly trained mechanics is fierce across all sectors of aviation. Finding mechanics interested in the "less glamorous" world of general aviation and life in small, rural towns has become more difficult. Increasing cost pressures resulting from FAA service manual requirements, declining profit margins on parts, shop overhead costs, including, often, rental of facility costs at airports also impact the viability of this backbone of aircraft maintenance.

ENTRY BARRIERS

Capital Intensive Industry

Like manufacturing industries in mature markets, today's aircraft piston engine manufacturing industry can be classified as highly capital intensive. This industry is characterised by the following:

- Long development cycles — in addition to costs associated with research and development, this industry requires extensive testing before bringing a product to production
- High basic costs — Manufacturing facilities and processes, skilled unionised labor force and very high costs associated with regulatory compliance and liability
- Lower returns on investment — particularly when faced with decreased demand from OEM aircraft manufacturers, manufacturers have placed increased reliance on aftermarket services to drive company revenues and margins
- High costs associated with input materials and manufacturing processes.

Established Industry Players Control Majority of Market

Lycoming Engines and Continental Motors, two companies have been manufacturing airplane piston engines since the early part of the twentieth century. Not only do these companies have longstanding relationships with OEM piston aircraft manufacturers, they are also part of fiscally sound parent companies with extensive vertical integration within the aviation sector. Rotax Engines GmbH & Co KG, the "newest player" to establish market share having entered the industry in the 1970s, now has more than 40 years of experience.

Highly Regulated Industry

The FAA of the US regulates all aspects of aviation in the US. While the FAA's track record of enhancing and ensuring the safety of the world's busiest aviation network speaks for itself, regulations are not only extensive and constantly evolving, for manufacturers in the industry, achieving compliance is time intensive and costly. While considerable efforts have been made, using the FAA, as a model framework, to support standardization of best practices across countries in an increasingly connected world, differences still remain in terms of processes, enforcement and costs associated with compliance between nations. As the UAS industry continues to evolve and become a factor in national airspaces, regulation will necessarily ensue for this sector as well.

COMPETITIVE ENVIRONMENT

In 2016, US sales of aircraft piston engines + MRO + spares were $386.8 million. The industry is dominated by two major players.

Leaders from the start in engine development for piston engine aircraft in the US and Europe, Lycoming Engines and Continental Motors, benefited from tremendous and sustained growth in these markets for most of the twentieth century. In the mid-1970s, Rotax Aircraft Engines entered the market, leveraging the strength of Rotax's longstanding experience in smaller horsepower technologies for the general aviation market. Interestingly, each of the two major players have, over time, become the sole leaders in terms of market share in both volume and revenue, in particular powerhouse segments as measured in terms of horsepower. Therefore, OEM piston engine aircraft manufacturers will utilise engine products from more than one engine manufacturer for different models in their product lines.

Today, confronted with significantly declining demand in the traditional strongholds of North America and Western Europe and developing markets taking longer to develop their general aviation markets than anticipated, industry players focused on growth strategies to take competitors market shares and to expand revenue growth via aftermarket services and to acquire companies specializing in complementary products and technologies.

Lycoming Engines

Lycoming Engines, originally founded in 1907, is now owned by Textron, a global aerospace, defence, security and advanced technologies industrial conglomerate with a market capitalization of more than $12 billion (NYSE: TXT). Lycoming Engines has manufactured more than 300,000 engines in its history and produced more than 700 FAA certified models. Textron Aviation also owns the Beechcraft and Cessna brands of general aviation aircraft, Bell Helicopters and Hawker line of service centres.

Continental Motors

In 1923, Continental Motors Company expanded beyond the manufacture of automobile engines to produce its first aircraft engine in 1929. The aircraft engine portion of the business was acquired by Teledyne Industries in 1969. Headquartered in Mobile, AL, today the company is owned by Aviation Industry Corporation of China (AVIC) which is owned by the government of the People's Republic of China. In 2013, AVIC acquired Thielert Aircraft Engines GmbH, forming Technify Motors to produce Thielert's line of Centurion engines in Germany, adding capacity at the 155 - 355 Hp range.

Rotax Aircraft Engines (BRP - Rotax GmbH & Co KG)

Rotax aircraft piston engines are manufactured by the Austrian company BRP-Rotax GmbH & Co KG, which is owned by Bombardier Recreational Products of Canada, a publicly held company that trades on the Toronto Stock Exchange under the symbol DOO. Founded in 1920, in Dresden, Germany, as ROTAX-WERK AG, the company was purchased by BRP in 1970; the company produced its first certified aircraft engine in 1975. As part of a diversified company whose name is synonymous with engines for a wide variety of small land, sea and air vehicles, Rotax Aircraft Engines aviation benefits from its strengths in technology. The company specialises in the production of two- and four-stroke piston engines for the ultralight aircraft, light aircraft and unmanned aviation systems (UAS) segments.

Austro Engines

Austro Engines, a subsidiary of Diamond Aircraft Industries, an Austrian based manufacturer of aircraft engines. Its key product is a four stroke four cylinder diesel engine used in Diamond aircraft that gained EASA and FAA certification in 2009. In 2013, Wuhu Diamond Aircraft Co., Ltd. was established as a joint venture between Diamond Aircraft and China Electronics Technology Group (CETC); establishing a foothold for Austro in the Chinese LSA segment.

Table 1 US Aircraft Piston Engine Manufacturing + MRO + Spares Industry, Top Companies, 2016

Ranking		Revenue Receipts (2016) USD 000'	Market Share (2016)
1	Company A	186,012	48.1%
2	Continental Motors Group Ltd (including CMS and TMG)	152,682	39.5%
3	Company B	9,264	2.4%
4	Company C	1,265	0.3%
	Others	37,579	9.7%
	Total	386,802	100%

Source: Euromonitor estimates from desk research and trade interviews with major piston engine aircrafts manufacturers, leading aircraft piston engine manufacturers / distributors and the relevant trade associations in the USA

Audited data if available is usually not industry / service specific and includes other products / services. Leading industry players' ranking will therefore be estimated on publicly available data and the trade opinion survey (not just the companies themselves).

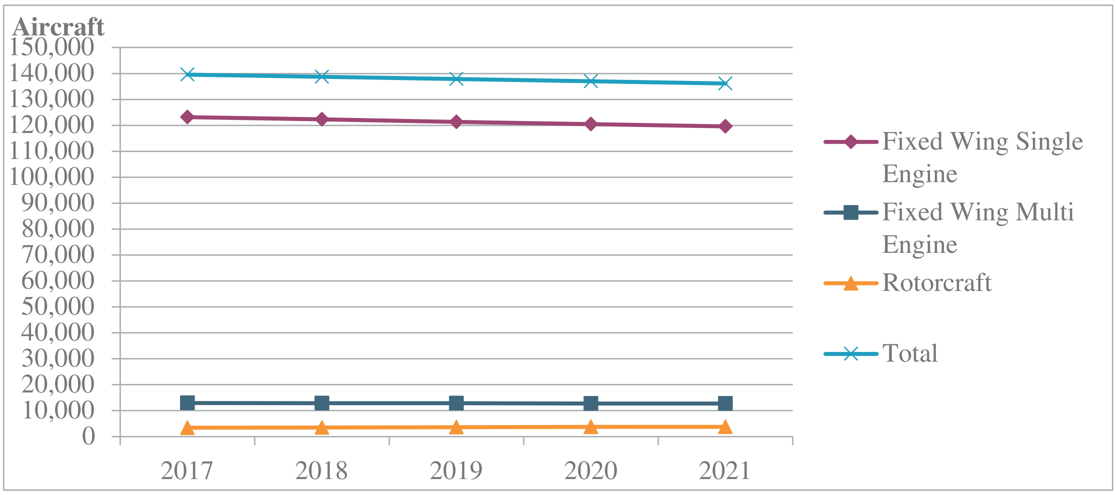
Company A — Established in 1845, and headquartered in Pennsylvania, the company manufactures aircraft engines, including a line of horizontally opposed, air-cooled, four-, six- and eight-cylinder engines.

Company B — With its global headquarters in Austria, the company develops and manufactures powertrains for a range of land, sea, and airborne vehicles. Type of vehicles include snowmobiles, watercrafts, all-terrain vehicles, and light and ultralight aircrafts.

Company C — Founded in 2007, the company is an Austrian manufacturer of aircraft engines. The company produces rotary and piston engines for renowned manufacturers of general aviation aircraft and unmanned aerial vehicles.

GENERAL FUTURE OUTLOOK

Chart 5 US Active General Aviation and Air Taxi Aircraft Forecast, 2017-2021



Source: FAA Aerospace Forecast

For the forecast period, 2017-2021, the US fleet size for piston powered aircraft is expected to remain nearly constant trending slightly downward, with fixed wing aircraft trending slightly downward and piston powered rotorcraft trending upward. This means that new aircraft growth will remain basically flat, forcing industry players to seek opportunities in non-traditional markets and/or LSA and UAS aircraft, and developing the aftermarket segment of the market. Growth for these companies will be extremely difficult to achieve unless other markets are developed as there is very little room for any of the major players to improve margins, particularly following the resizing efforts they all undertook following the Great Recession in 2008.

Challenges Ahead For Piston Engine Aircraft in the General Aviation Sector

Table 2 US Active General Aviation Fleet Size Forecast, 2017-2037

		2017	2021	2025	2029	2033	2037
Fixed Wing Piston	units	138,915	134,650	130,230	125,640	121,315	117,520
Turboprop	units	9,285	9,075	9,420	10,180	11,230	12,585
Turbo Jet	units	14,100	15,480	16,965	18,565	20,225	22,040
Rotorcraft	units	10,890	11,615	12,365	13,165	14,055	15,065
Experimental	units	28,970	30,640	31,835	32,970	34,120	35,310
Sport Aircraft	units	2,685	3,315	3,965	4,610	5,255	5,885
Others	units	4,955	4,950	4,955	4,970	5,005	5,015
Total General Aviation Fleet	units	209,800	209,725	209,735	210,100	211,205	213,420

Source: FAA Aerospace Forecast, Federal Aviation Administration

Table 3 US Active General Aviation Hours Forecast, 2017-2037

		2017	2021	2025	2029	2033	2037
Fixed Wing Piston	000' hours	12,604	11,865	11,451	11,104	10,892	10,754
Turboprop	000' hours	2,538	2,554	2,662	2,881	3,175	3,561
Turbo Jet	000' hours	4,445	5,250	5,894	6,511	7,125	7,736
Rotorcraft	000' hours	3,413	3,754	4,092	4,406	4,745	5,124
Experimental	000' hours	1,372	1,515	1,640	1,765	1,883	2,007
Sport Aircraft	000' hours	218	275	335	398	463	529
Others	000' hours	163	163	164	165	166	167
Total General Aviation Hours	000' hours	24,753	25,375	26,239	27,230	28,449	29,876

Source: FAA Aerospace Forecast, Federal Aviation Administration

According to FAA Aerospace Forecast, fleet growth is likely to be minimal, just 0.1% CAGR between 2017 and 2037, which represents an increase of just 3,620 aircraft for the forecast period across all sectors of general aviation. That growth is expected to be led by turbine and rotorcraft aircraft, with the fixed wing piston aircraft fleet expected to decrease over the forecast period. While general aviation hours are expected to increase by 0.9% CAGR between 2017 and 2037, those numbers will be driven by increases from the turbine, rotorcraft and experimental sectors that will compensate for the anticipated decline in hours for piston engine powered aircraft. Competition from the commercial aviation sector will continue as demand continues to grow in that sector despite slower than expected economic growth.

Diesel Powered Aircraft May Provide Growth Opportunity

While the present fleet of piston powered diesel fueled aircraft is small relative to total fleet size, and the anticipated diesel revolution has not taken hold, there are signs that more and more diesel powered engines are being introduced around the world.

While diesel engines have a higher price point than their gas fueled counterparts, they offer several key advantages over the course of their lifetime that can make these engines more cost effective in the long term. Diesel engines are simpler, use much less fuel and generally require less maintenance. Additionally, for many parts of the world, diesel fuel is significantly less expensive and more readily available than is gasoline. Given the high return on investment, for now, the larger markets for diesel fueled aircraft are operations that require large numbers of planes, i.e., flight schools, fleet operators and surveillance aircraft versus the general aviation enthusiast.

Diesel fueled UAS aircraft are proving very viable. In 2014, US based Mooney Aircraft was purchased by a Chinese investment group to begin producing aircraft for the Chinese market where diesel fuel is more than 70% less expensive and more readily accessible than avgas fuel.

Timing and Size of Market for Piston Engine Aircraft in the Developing World

Despite the high hopes of many analysts and industry leaders alike, the emergence of the market for piston powered aircraft in general aviation in the developing economy countries has been significantly slower than expected. While much of the developing world, from the outside, would seem "primed" for a ramp up in fixed wing powered aircraft similar to what occurred in the US and Europe following the end of World War II, these regions have simply not developed as quickly as analysts had projected for a variety of reasons.

These markets are coming of age when piston engine alternatives already exist in the general aviation sector, the entire realm of UAS is emerging and commercial airlines dominate air travel. Much like the product life cycle for landline telephones has been bypassed for many segments in many of these economies, perhaps piston powered aircraft will not experience a similar trajectory.

However, at the same time the sheer size of these markets, technological advances in power generated by piston engines, the lower price point for piston engines compared with other general aviation engines, means that this market still holds promise for substantial growth. The slower than expected rebound from the world economic crisis of 2008 has delayed anticipated growth as well.

FUTURE OPPORTUNITIES

Growth in OEM Segments in Global Markets Outside North American and Europe

Out to 2037, GDP growth in the developing world is expected to outpace that of the developed world, driven largely by the economies of India and China. Markets exist in China, India, Brazil and Argentina and to a lesser extent the more advanced economies of sub-Saharan Africa for the future of general aviation across all engine segments.

In particular, China presents significant growth opportunities for general aviation in terms of sheer size — an increasingly affluent population and geography — as the country transitions from a largely agrarian society to a rapidly expanding manufacturing and service based economy.

Significant opportunity exists for the emergence of new OEM manufacturers of piston engine aircraft to emerge in China. GDP growth in China is expected to average 4.9% over the forecast period 2016-2037. With their extensive manufacturing experience, US manufacturers are well positioned to provide this market with not only engines, but also subsystems and parts.

Acquisition and Licensing Opportunities in Mature Markets of North America and Western Europe

Manufacturers that have traditionally relied upon the US and Western European market must rely on future growth opportunities that emphasise acquisitions in avionics, subsystems and parts, thereby lowering the costs of inputs and improving their competitive position in terms of product offerings to both OEM and service centers. Additionally, opportunities exist to acquire companies that serve as fixed-base operator and MRO operations currently and those that have the capacity for PMA operations in competitors' engines.

Growth in Light Sport Aircraft (LSA) and Development of the UAS Market

According to the FAA Aerospace Forecast, during the forecast period to 2037, growth of the LSA fleet is expected to grow at an annual rate of 4.1% per year, representing an additional of 3,355 aircraft, more than doubling its 2015 fleet size.

The market for UAS aircraft and technologies represents the most dynamic market for growth in aviation presently. If regulators establish practical and implementable rules for "Beyond Visual Line for Sight" (BVLOS) and multiple UAS operation by single pilot, the commercial demand for UAS will be significant.

FUTURE CHALLENGES

Challenges Confronting Growth in Developing Markets

While the markets outside the North America and Western Europe do present the potential for future opportunities for growth for piston engine manufacturing, they also represent significant challenges.

While economic growth in these countries will outpace that of developed economies during the forecast period out to 2037, anticipated economic growth has not occurred at the rate previously anticipated. This has been particularly true in China and India; furthermore, in India, the growth of consumer spending has not yet occurred. Effects of recessions in Russia and Brazil have lasted longer than expected, although conditions are expected to improve in both regions heading into 2018 and beyond.

In many of these countries, growth in the aircraft piston engine sector has been slow due to undeveloped infrastructure and access to airspace for general aviation. In both China and India very restrictive regulations govern the use of airspace in these countries and gaining access to airspace has been a challenge for all forms of aviation other than that for military use.

Further compounding these challenges, as all forms of aviation seemingly "come of age" at the same time for many of these countries, a shortage of qualified pilots, mechanics and technological know - now exists across all sectors of aviation. For now, until the needs of the commercial air transportation sector are met, it will remain very difficult to attract qualified technical expertise, pilots and mechanics to serve the general aviation sector including piston engine powered aircraft.

Stagnant and Declining Growth in Piston Aircraft in Traditional Markets of North America and Europe

Very mature markets for piston engine aircraft exist in both of these regions. Over time as the market has matured, and the age of the piston engine aircraft fleet has continued to age, yet function very well for the general aviation enthusiast, end consumers have become increasingly price sensitive. Price sensitivity is also exacerbated by rising costs associated with ancillary costs associated with aircraft ownership such as regulatory compliance, licensing, insurance and fuel costs. Furthermore, increases in discretionary incomes in these markets have not been evenly distributed, with the majority of additional discretionary income accruing to the segment of the population with the greatest wealth, which in turn, has helped drive the increased demand for turbine engine powered aircraft.

KEY LAWS, RULES AND REGULATIONS APPLICABLE TO THE TARGET GROUP'S BUSINESS IN THE US

US Federal Aviation Administration

The US Department of Transportation, a Cabinet level post within the Executive branch of the US federal government, operates the FAA. The FAA is responsible for regulating all aspects of civil aviation. In this role, the FAA:

- Issues and enforces regulations and minimum standards covering manufacturing, operation and the maintenance of aircraft
- Certifies pilots and airports
- Operates the nation's air traffic control system
- Registers aircraft and records documents reflecting title or interest in aircraft and their parts
- Aids in promoting safe civil aviation abroad and works to provide technical assistance and oversight and negotiates bilateral airworthiness agreements.
- Supports research, engineering and development in aviation.

The FAA administers its rules via Federal Aviation Regulations, part of Title 14 of the US Code of Federal Regulations, referred to as "FARs" or "14 CFRs" in the aviation industry. While tens of thousands of regulations exist, those of particular import for the general aviation industry include the following:

- Part 23 — Governs airworthiness standards for general aviation aircraft
- Part 21 — Governs certification procedures for products and parts
- Part 61 — Governs certification of pilots, flight instructors and ground instructors (Pilot certifications relate to types of activities conducted by pilots and are often referred to as Part XX regulations for this reason)
- Part 135 — Certifies operators of aircraft who conduct operations for hire

On August 30, 2017, new rules go into effect governing Part 23 of the FARs; these changes have received substantial support from the US general aviation industry as the new rules should support innovation, streamline certification processes while maintaining safety. The Part 23 rewrites are part of a worldwide effort with foreign regulatory agencies expected to follow suit.

While still under FAA auspices, the following are of note for the US general aviation industry:

- American Society for Testing and Materials (ASTM) Standards for light sport aircraft (LSA) - Standards accepted by the FAA for all LSA, including fixed wing aircraft. As of April 2017, the European Aviation Safety Agency (EASA) announced its plans to adopt these same standards.

- ADS-B avionic equipment - By January 1, 2020, all aircraft, including general aviation aircraft, flying in controlled airspace must be equipped with ADS-B systems, a requirement supported by the general aviation industry. These requirements are part of the FAA's Next Generation (NextGen) Air Transportation System, requiring air traffic control systems to move from radar based system with radio communications to satellite based system.

- The General Aviation Revitalization Act of 1994 amended FAA regulations regarding product liability for general aviation aircraft.

Environmental Protection Agency (EPA)

Under the Clean Air Act, the Environmental Protection Agency (EPA) has the authority in consultation with the FAA to regulate emissions from aircraft. Avgas is a specialized fuel that contains tetraethyl led (TEL) used to power piston engine aircraft. Avgas is the only remaining transportation fuel in the US that contains TEL, making avgas emissions the largest contributor to lead emissions in the US. TEL has not yet been banned for use in avgas, because no operationally safe alternative is currently available.

Given the serious health issues associated with lead in the environment, the FAA has a stated goal of finding a replacement for unleaded avgas and the EPA is expected to rule against the continued use of TEL in aviation fuels. Since late 2011, FAA officials and aviation industry leaders have been working together to address the issue via the Unleaded Avgas Transition Plan (UAT Plan):

- 2012 — The FAA Modernization and Reform Act required the FAA to develop an R&D program to qualify an unleaded aviation fuel available and to safely transition the fleet of piston engine aircraft to that fuel.

- 2013 — Piston Aviation Fuels Initiative (PAFI) — government/industry group charged with overseeing this initiative. FAA Technical Center Testing Program — began soliciting candidates for fuel testing.

- 2016 — Final (Round 2) of fuel testing underway with finalists from Shell and Swift.

- 2018 (target timing) — Unleaded aviation gasoline fully evaluated and ready to be authorized for use by general aviation fleet.

US Department of Homeland Security

The Transportation Security Administration (TSA), formed in 2001 in the aftermath of the 9/11 terrorist attacks on the US, is an agency of the US Department of Homeland Security that operates the Alien Flight Student Program (AFSP). The current requirements were issued in 2004.

Alien Flight Student Program (AFSP) -Non US citizens, who wish to receive instruction in any of the four categories of flight training in the US, must participate in and undergo a security threat assessment. This includes checks against law enforcement, immigration and intelligence databases as well as finger print based and biometric based screening.

Vision 100 — Century of Aviation Reauthorization Act — Section 612 — Transferred administration of the program from the US Department of Justice to Homeland Security, and also prohibits any certified flight instructor from providing training to foreign nationals on aircraft before legal requirements of the AFSP are met.

Certification Regulations — Part 25 Aircraft Engines — Production and Maintenance

Regulation 14CFR Part 33 — Airworthiness Standards: Federal Aviation Regulations (FARs) cover the certification of aircraft engines for Part 23 aircraft. Specifically, Sections 33.31 − 33. 57 apply to reciprocating (piston) engine power plants and their testing requirements.

Manufacturers must also be mindful of Series 33 Advisor Circulars which include Airworthiness Directives applicable to aircraft piston engine manufacturing.

In addition, special considerations for manufacturers of LSA aircraft and component parts exist.

The FAA oversees manufacturing and airworthiness related activities through a system of Field Offices. These offices assist with

- Production approval and certification (manufacturing)
- Airworthiness certification
- Manufacturing facilities approval
- Manufacturing designee oversight and assistance through the design approval process.

FAA regulations also apply to recurrent airworthiness standards as well and thus, are important considerations for OEM, PMA manufacturers and MRO operations.

Once an engine model has been issued an FAA certification, the engine must meet aircraft installation requirements found in Subpart E of the applicable aircraft certification requirements.

Additionally, the following regulations are important regulations for aircraft engine repair locations, which, in the general aviation industry are co-located at distributor locations:

- 14 CFR Part 43 which applies to Maintenance, Preventative Maintenance, Rebuilding and Alterations.
- 14 CFR Part 65 which applies to Certification of Airmen Other than Flight Crew (i.e. mechanics).

Certification Regulations — Part 25 Aircraft Engines — Distribution and Dealerships

The FAA does not directly regulate distributors; however, accreditation of a distributor's quality system, via ISO 9001 certification and Voluntary Industry Distributor Accreditation Program recognition through the Aviation Suppliers Association is strongly encouraged as best practice.

Additionally, distributors must complete FAA Form AC8050-5 and submit an application fee so that aircraft on site are registered. Just like any other sales location, aircraft parts and aircraft distributors and dealers must comply with the respective state Department of Revenue.

KEY LAWS, RULES AND REGULATIONS APPLICABLE TO THE TARGET GROUP'S BUSINESS IN GERMANY

Applicable law regarding production / testing facilities (for aircraft engines)

German public law is characterised by its sector separating approach. Therefore, there is no concept of a general or overall operating permit. Instead, separate operations or activities are subject to separate administrative permission processes.

As far as public law provisions for production facilities (including engine test standards) are concerned, the main sources of environmental legislation (dealing with e.g. protection of soil and groundwater, emissions and waste management) and consequently licence requirements include amongst other things:

- the German Federal Emission Control Act (Bundes-Immissionsschutzgesetz);
- the German Federal Water Act (Wasserhaushaltsgesetz) and the corresponding Water Acts of the individual states;
- the German Closed Substance Cycle Waste Management Act (Kreislaufwirtschaftsgesetz) and the corresponding state legislation;
- the German Federal Soil Protection Act (Bundes-Bodenschutzgesetz); and
- the German General Police and Public Order Law of the individual states.

Engine production and testing sites may require an emission permit issued under the German Federal Emission Control Act.

Liability for environmental damage

Under German civil law, anyone causing pollution may be liable to compensate the aggrieved party for the resulting damage. The German Environmental Liability Act (Umwelthaftungsgesetz) provides for a strict liability with respect to harmful effects on the environment.

In 2007, Germany introduced the Environmental Damages Act (Umweltschadensgesetz) (the "**EDA**") as a matter of public (administrative) law. The EDA entitles authorities to take measures to avoid environmental damage or, if damage has occurred, to enforce the cleaning up of the contamination and restoration of the damaged area to its state prior to such contamination. Enforcement of the EDA is only possible against individuals or legal entities acting within their professional activities. The relevant environmental damage can include damage to biodiversity, waters or the soil.

In general, under German environmental law, the liability for soil and groundwater contamination is a strict, non-fault based liability (including investigation and remedial measures) imposed by the competent authorities by way of administrative orders. A number of persons may be held responsible, namely

- the owner and/or possessor (i.e. operator) of the site;
- the original polluter as well as any legal successor (Gesamtrechtsnachfolger) of the polluter;
- in certain circumstances the former owner of the site; and
- the person/entity responsible under general principles of commercial or corporate law for the legal entity owning the real estate.

The competent authorities have a broad discretion as to whom of several responsible persons (polluter, owner and lessee) it decides to issue clean-up orders or orders to carry out an inspection to determine the degree of environmental damage. In addition, public authorities have a broad discretion concerning the way in which they determine the necessary measures to be undertaken by the responsible person.

Construction of aircraft engines — certification requirement

The regulatory framework regarding the construction and sale of aircraft and aeronautical parts and products (e.g. aircraft engines) in Germany is not only governed by German law, but also by (directly applicable) EU law. The competent German authority, the Luftfahrt-Bundesamt (Federal Aviation Authority), operates in an increasing number of cases in close coordination with the European Aviation Safety Authority ("**EASA**").

In 2002, the EU adopted the first set of a new generation of aviation safety rules based on Regulation (EC) No 1592/2002, which also established the EASA as the cornerstone of the European aviation safety system. This initial set of rules covered airworthiness and environmental certification and maintenance of aeronautical products as well as the training and licensing of aeronautical mechanics and technicians.

In 2008, by virtue of Regulation (EC) No 216/2008, the EU extended the common aviation safety rules and the corresponding responsibilities of EASA to aircraft operations and aircrew licensing and training. In 2009, the EU adopted a second extension of the common rules covering safety aspects of aerodrome operations and provision of air navigation services and air traffic management (Regulation (EC) No 1108/2009).

Aviation safety rules are adopted by the European Commission on the basis of technical opinions issued by the EASA. Proper implementation of the rules is regularly monitored by the European Commission with the assistance of EASA, which carries out regular inspections in all member states. Enforcement actions can be taken if safety deficiencies are detected and not corrected. These can involve suspension of the mutual recognition of certificates or penalties imposed on certificate holders.

Every aircraft designed and manufactured in Europe (with its parts and components) requires EASA certification. The EASA, rather than authorities of EU member states, was entrusted with the responsibility of issuing (type) certificates. For instance, the EASA is entirely responsible for the certification of aircraft types and other aeronautical products. The EASA also issues certificates for organisations located in third countries. The national authorities of member states however continue to issue, under EASA monitoring, individual certificates to aircraft and most organisations and personnel located in their territories. All certificates issued on the basis of EU law are valid in all EU member states, which guarantees a uniform level of safety.

Currently, the scope of competences of EASA encompasses all aspects related to airworthiness and environmental certification of aeronautical products, parts and appliances. In addition, the scope of community safety rules and of the corresponding responsibilities of EASA, were extended to the training and licensing of crews, flight operations (of both community and third country operators), aerodrome safety and safety of air traffic management and provision of air navigation services. These competences will be gradually exercised with the adoption of the related implementing rules.

The applicable Regulation (EU) No 748/2012 of 3 August 2012 lays down implementing rules for the airworthiness and environmental certification of aircraft and related products, parts and appliances, as well as for the certification of design and production organisations. The regulation governs certification of aircraft and related products, parts and appliances, and of design and production organisations. If the requirements of the regulation are met, the EASA issues a type certificate for the aircraft or related product.

Registration as owner of an aircraft

In Germany, the owner and, if different, the operator of an aircraft have to be recorded in the German aircraft register (Luftfahrzeugrolle). Aircraft that are not registered elsewhere and that are owned by German nationals or by companies that are owned and effectively controlled by German nationals can be registered in the German aircraft register, as well as aircraft owned by citizens or companies of other EU member states and other countries applying EU aviation law, provided the owner is residing or domiciled in Germany or has a process agent in Germany. Aircraft owned by nationals or companies from other countries and based in Germany can be registered in the German aircraft register under special circumstances.

Foreign Trade — Export licences

The foreign trade with commodities of strategic importance, mainly weapons, armaments and dual-use items, is subject to government control. Within the framework of its legal and international commitments, the export control policy of the federal government is oriented towards the security need and foreign political interests of the Federal Republic of Germany.

Export licences are granted by the German Federal Office of Economics and Export Control (Bundesamt für Wirtschaft und Ausfuhrkontrolle) for export of products classified as military items under the German Foreign Trade and Payments Ordinance (Außenwirtschaftsverordnung). Such classification is applicable, e.g. if the products are (potentially) assembled in unmanned aerial vehicles.

As regards such and other products subject to the restrictions of the German export control regime for military items, licences will have to be applied for in the future. Subject to the general political environment and developments, licences required for exports in the future may be restricted or even prohibited.

KEY LAWS, RULES AND REGULATIONS APPLICABLE TO THE TARGET GROUP'S BUSINESS IN THE PRC

Foreign Investment

Foreign investment is subject to government control in the PRC. According to Catalogue of Industries for Guiding Foreign Investment (revised in 2017), the Special Management Measures for the Market Entry of Foreign Investment (Negative List for the Market Entry of Foreign Investment) list, in a unified manner, the restrictive measures for the market entry of foreign investment. Foreign investors shall not engage in prohibited items in the Special Management Measures for the Market Entry of Foreign Investment, and shall not establish foreign-invested partnership enterprises when engaging in restricted items with the requirements on proportion of foreign investment.

Import, export and sale of aircraft engines is not included in the Negative List for the Market Entry of Foreign Investment. Therefore, an enterprise with foreign investment that engages in import, export or sales of aircraft engines will not be restricted or prohibited by the PRC government.

Foreign Trade

The PRC Government apply a uniform administration system to the import and export of goods and technology. According to Foreign Trade Law, Regulations on the Administration over Technology Import and Export , and Regulations on the Administration over Import and Export of Goods, the PRC Government shall permit the free import and export of goods and technologies, but the State may take any necessary measures for the import and export of weapons, ammunitions and other military supplies to maintain national security.

Foreign trade operators engage in goods or technology import and export shall go through the record-filing registration formalities with the competent department of foreign trade under the State Council or its entrusted institutions. Where a foreign trade operator fails to go through the record-filing registration formalities, the customs authority shall refuse to handle customs clearance procedures for goods imported or exported by the operator.

Customs

According to Customs Law of the PRC, the declaration of import or export goods and the payment of duties may be made by consignees or consigners themselves, or by their entrusted customs brokers that have registered with the customs authority. Consignors and consignees of imports and exports, and customs brokers engaged in customs declaration shall be registered with the customs authority pursuant to the law. No party may engage in customs declaration business without registration with the customs authority pursuant to the law.

Both consignees of import goods and consigners of export goods shall make a truthful declaration and submit their import or export licenses and relevant papers to the customs authority for examination. In the absence of an import or export license, no goods whose importation is restricted by the State may get through customs.

Administration of the Airworthiness of Civil Aircraft

According to Regulations for the Administration of the Airworthiness of Civil Aircraft, any units or individuals of the PRC intend to import any model of civil aircraft manufactured in foreign countries, if it is imported for the first time and to be used for civil aviation activities, the units or individuals exporting that civil aircraft shall apply to the CAAC Civil Aviation Administration of China for examination of the model. The CAAC shall, upon receipt of the application, conduct the examination in accordance with the relevant provisions. If the model is proved to be up to standard, a Model Approval Certificate shall be issued to permit the import.

If the export country has already signed an airworthiness agreement for imported civil aircraft with the PRC Government, the CAAC may directly affirm the model design approval given by the civil airworthiness authority of the export country. In addition, having signed an airworthiness agreement for imported civil aircraft by the export country of relevant aircrafts with the PRC government is a prerequisite for applying for Model Approval Certificate.

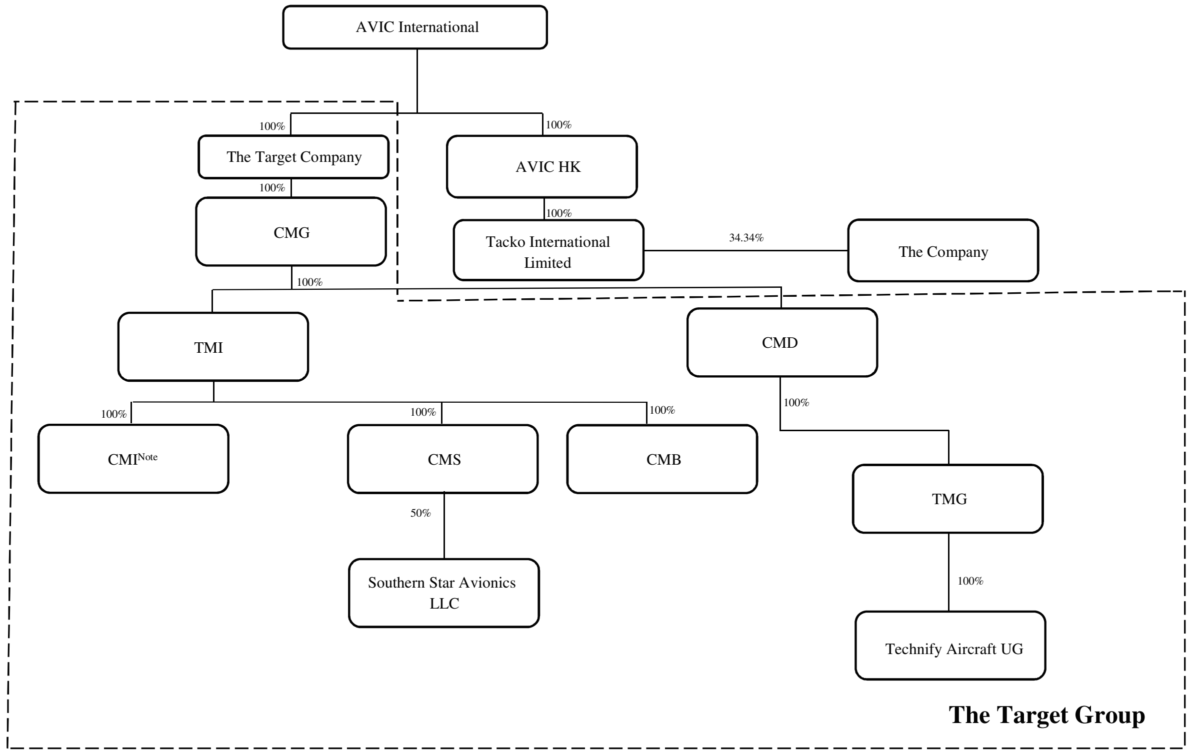
MILESTONES OF THE TARGET GROUP

The Target Group has achieved the following key milestones:

1905	Continental Motors Manufacturing Company signed a contract with the Greater Muskegon Chamber of Commerce to move its operation to Muskegon, Michigan.
1940	Continental Motors formed the corporation Continental Aviation and Engineering Corporation for the purpose of supplying aircraft engines to the US military.
1966	Continental Motors opened a location in Mobile, Alabama.
1999	Continental Motors acquired substantially all of Mattituck Aviation Corporation's assets and certain of its liabilities relating to its business as a supplier and distributor of products and services to the general aviation market place and as a piston aircraft rebuilder and overhauler.
2011	AVIC International acquired Continental Motors Inc. and Continental Motors Services (Mattituck Services).
2013	CMG acquired the assets of Thielert Aircraft Engines in Germany (now TMG) to produce Thielert's line of Centurion engines in Germany.
2014	CMB was established for PRC marketing, warehouse/distribution and customer support.
2014	CMI acquired assets of Southern Avionics in Mobile, Alabama, the USA for interiors & avionics installation & repair.
2015	CMI acquired assets of United Turbine in Miami, Florida, the USA, which offers full MRO services for PT6 engines.
2015	CMI acquired assets of Danbury Aerospace, Inc. in San Antonio, Texas, the USA for manufacturing and sales of Titan Engine and PMA parts that can be used as FAA approved replacements on Lycoming® engines and parts.

SHAREHOLDING OF THE GROUP AND THE TARGET GROUP BEFORE AND AFTER ACQUISITION COMPLETION

Set out below the shareholding structure of the Group and the Target Group as at the Latest Practicable Date.



Note: CMI also owns 1,000 preferred shares of Mangrove Cell 1 PC, a protected cell of Mangrove Insurance Solutions, PCC, a protected cell captive insurance company.

TMI

TMI was formed on 1 December 2010 under the laws of the state of Delaware. TMI has authorised capital of 10,000 shares of stock with a par value of US$1.00 per share. CMG (previously named Hong Kong Tianfa General Technology Limited) is the sole stockholder of TMI, holding one (1) share of common stock of TMI.

CMI

CMI (previously named Teledyne Continental Motors, Inc.) was duly incorporated on 6 December 2001 under the laws of the state of Delaware. On 3 January 2010, Aerosance, Inc., a Delaware corporation, was merged into CMI, with CMI being the surviving corporation. On 20 April 2011, Teledyne Continental Motors, Inc. changed its name to CMI.

CMI has authorised capital of 1000 shares of common stock at a stated par value of US$0.01 per share. The initial stockholder of CMI was Teledyne Technologies Incorporated ("***Teledyne***"), which sold its shares of stock in CMI to TMI. On 19 April 2011, TMI became the sole stockholder of CMI, holding 1,000 shares of common stock.

CMS

Teledyne Mattituck Services, Inc. was duly incorporated on 23 September 1999 under the laws of the state of Delaware. On 20 April 2011, Teledyne Mattituck Services, Inc. changed its name to Mattituck Services, Inc. On 15 July 2014, Mattituck Services, Inc. changed its name to CMS.

CMS has authorised capital of 1,000 shares of common stock at a stated par value of US$0.01 per share. Teledyne Investment, Inc. was the initial sole stockholder of CMS holding 100 shares of common stock of CMS and on 28 December 2007, Teledyne Investment, Inc. transferred its 100 shares to Teledyne. On 19 April 2011, TMI acquired CMS and became the sole stockholder of CMS holding 100 shares of common stock of CMS.

Zulu Flight Training, Inc. ("Zulu")

Zulu was incorporated on 23 March 2012 under the laws of the state of Delaware. Zulu has authorised share capital of 1,000 shares of capital stock with a par value of US$0.01 per share. CMI was the sole stockholder of Zulu holding 1,000 shares of common stock of Zulu. Zulu filed a Certificate of Dissolution with the Delaware Secretary of State on 25 May 2015.

United Turbine Corp.

As at 30 January 2015, CMS acquired United Turbine Corp's business for a total consideration of US$9,079,000, comprising identified assets that amounted to US$8,024,000 and goodwill that amounted to US$1,055,000. The acquisition was settled by cash and cash equivalents.

The reason for acquiring this business is to enlarge the Target Group's range of MRO services for aircraft engines that can be offered to its customers. The acquisition of United Turbine added a specific type of engine, PT-6, to the engine overhaul capabilities already at CMS. The acquired United Turbine Corp's business is now part of CMS' business and is not a corporation any more.

Danbury AeroSpace, Inc.

As at 19 July 2015, CMI acquired Danbury AeroSpace, Inc's business for a total consideration of US$14,991,000, comprising identified assets amounted to US$12,965,000 and goodwill amounted to US$2,026,000. The acquisition was settled by cash and cash equivalents.

Danbury AeroSpace, Inc. was a manufacturer of parts and piston engines for the general aviation segment. The reason for acquiring the assets of this business is to enlarge the Target Group's range of products that can be offered to its customers. The acquisition was completed as an asset purchase of the manufacturing and intellectual property assets of Danbury AeroSpace, Inc. with the corporate entity remaining with the original owner.

Southern Avionics and Communications, Inc.

As at 21 November 2014, CMS acquired Southern Avionics and Communications, Inc's business for a total consideration of US$850,000, comprising identified assets amounted to US$764,000 and goodwill amounted to US$86,000. The acquisition was settled by cash and cash equivalents.

Before such acquisition, Southern Avionics was a supplier for avionics systems and aircraft interior repair. CMS through this acquisition brought such skill in house. The facility of Southern Avionics and Communications, Inc. has been consolidated with the main MRO facility of CMS in Fairhope in February of 2017.

Southern Star Avionics, LLC ("SSA")

SSA was duly formed on 18 March 2003 under the laws of the state of Alabama, USA. The initial members of SSA were Star Aviation, Inc. and Southern Avionics and Communications, Inc. ("**Southern Avionics**"). On 21 November 2014, Southern Avionics assigned its 50% membership interest in SSA to CMS. As of 21 November 2014, Star Aviation, Inc. and CMS were the sole members of SSA, with each owning 50% of the membership interest in SSA, and there has not been any change in ownership of the membership interests in SSA since then. SSA was principally engaged in designing and installing modifications to aircrafts.

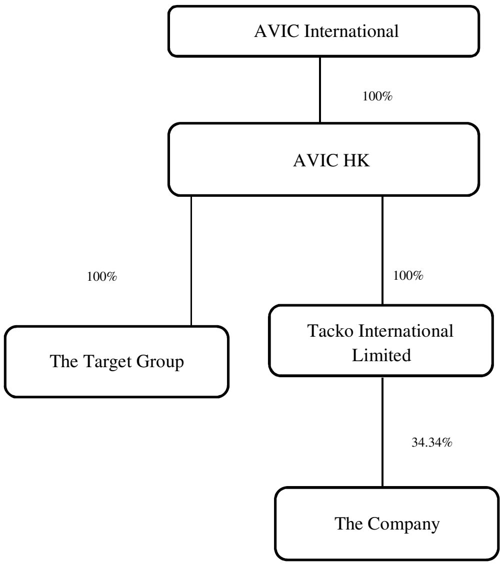
Technify Motors GmbH ("TMG")

TMG was incorporated on 1 November 2012 as a shelf company under the name Brillant 1578. GmbH by VRB Vorratsgesellschaften GmbH as its sole shareholder. It was incorporated with a share capital of EUR 25,000 and was first registered with the commercial register of the local court (Amtsgericht) of Berlin on 6 November 2012. On 12 December 2012, VRB Vorratsgesellschaften GmbH sold and transferred its interest in TMG to Honka Investment Ltd, a British Virgin Islands limited liability company. Subsequently TMG moved its statutory seat to Chemnitz. The amount of its share capital remains unaltered. Honka Investment Ltd changed its company name to Continental Motors Deutschland Ltd in July 2012.

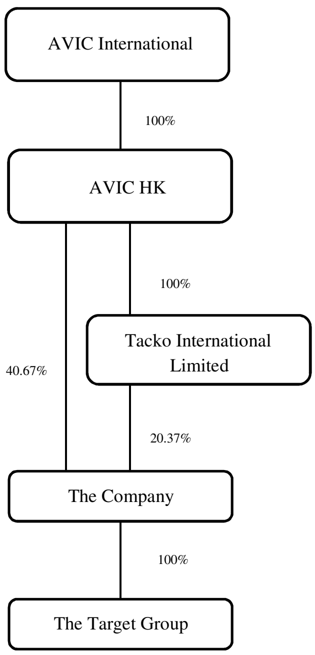
Technify UG

Technify UG was incorporated on 19 February 2013 as a shelf company under the name Bambino 199. V V UG (haftungsbeschränkt) by VRB Vorratsgesellschaften GmbH as its sole shareholder. It was incorporated with a share capital of EUR 500 and was first registered with the commercial register of the local court (Amtsgericht) of Berlin on 28 February 2013. On 28 August 2013, VRB Vorratsgesellschaften GmbH sold and transferred its interest in Technify UG to TMG. Technify UG subsequently changed its name to Technify Aircraft UG (haftungsbeschränkt) and moved its statutory seat to Chemnitz. Its share capital has not been changed.

Prior to Acquisition Completion, AVIC International will transfer the entire issued share capital of the Target Company to AVIC HK. Set out below the shareholding structure of the Group and the Target Group after the transfer of the Target Company to AVIC HK and immediately before Acquisition Completion.



Set out below the shareholding structure of the Group after Acquisition Completion.



LOAN SETTLEMENT ARRANGEMENT

Set out below is a summary of outstanding loans owed to or guaranteed by related parties of the Target Group as at 30 June 2017.

No.	Lender	Borrower	Loan balance as at 30 June 2017	Interest rate	Guarantor/ Collateral	Date of loan agreement	Term of loan	Proposed plan prior to Acquisition Completion
1.	The Export-Import Bank of China	TMI	US$180 million	6 Month Libor + 300bp	Aviation Industry and AVIC International	15 April 2011	15 Years	AVIC HK to purchase the loan receivable from the Export-Import Bank of China
2.	Bank of China Limited	TMG	EUR46.975 million	EURIBOR + 1.4%	AVIC International	30 June 2016	30 June 2016 to 29 May 2019	AVIC HK to purchase the loan receivable from the Bank of China Limited
3.	CATIC International Finance Limited[1]	TMI	US$48.2 million (in aggregate)	Ranging from nil to 5.88% p.a.	Nil	Various (from 1 January 2012 to 14 April 2017)	Various	TMI will repay the loan with funds received by way of new equity investment in the Target Group

[1] CATIC International Finance Limited is a wholly-owned subsidiary of AVIC HK.

As a condition precedent to Acquisition Completion, each loan receivable identified in Item 1 and 2 above shall be purchased from the respective banks by AVIC HK. AVIC HK will subsequently sell the two loans to the Target Company in return for the issuance by the Target Company of interest free, unsecured and repayable on demand loan note(s) in the same aggregate principal amount as the two loans ("**Shareholder's Note(s)**"). Such Shareholder's Note(s) together with the entire issued share capital of the Target Company will be sold to the Company pursuant to the terms of the Acquisition Agreement. It is also a condition precedent to Acquisition Completion that the Target Group will repay its loan in Item 3 above using funds resulting from additional indirect equity investment by AVIC International in TMI. prior to Acquisition Completion. As a result, there will be no outstanding loan or guarantee arrangement between AVIC International or AVIC HK and the Company after Acquisition Completion.

Summary

The Target Group is one of the leading manufacturers of and services providers to general aviation aircraft piston engines worldwide. The Target Group has an established brand name and an operational history of over a century. Its first gasoline engine product line started operation in 1904 and its services arm started business in 1946. Through a series of acquisitions, its core businesses include (a) the design, development and production of aircraft piston engines fuelled by gasoline and diesel fuels as well as engine spare parts; and (b) aftermarket services and supports for general aviation aircraft.

The manufacture business segment of the Target Group contributed over 90% of its revenue during the Track Record Period. The Target Group provides customers with both whole engines and engine parts. Whole engines are sold to both OEM customers and aftermarket customers. OEM customers are aircraft manufacturers. Aftermarket customers include distributors and airplane owners. Engine parts are mostly sold to aftermarket customers for replacement.

In the general aviation market, as at 2014, the average age of aircraft in use was approximately 37 years while the average replacement cycle of engines was around 12 years or less depending on the degree of utilisation. As a result, aftermarket sales tend to contribute more revenue than OEM sales. Going forward obtaining type certificates and securing OEM customers are essential in locking in aftermarket sales in this highly regulated general aviation market.

On the manufacture arm, the Target Group has five major gasoline product lines (200 Series that generates 100-125 HP, 300 Series that generates 195-225 HP, 400 Series that generates 225-260 HP, 520 Series that generates 250-325 HP and 550 Series that generates 280-350 HP) and three major diesel product lines (CD100 Series that generates 135-155 HP, CD200 Series that is expected to generate 265 HP and CD300 Series that generates 300 HP). In addition, the Target Group has two experimental gasoline product lines (Titan 300 Series that generates 150-200 HP and Titan 500 Series that generates 260-270 HP).

The service business contributed less than 10% of the revenue of the Target Group during the Track Record Period and the Target Group is increasing its footprint in the services business. Through a series of acquisitions, the Target Group now provides repair and maintenance services for not only piston engines but certain types of turbine aircraft engines. It also provides repair and maintenance as well as avionics and interior installation services for piston aircraft.

Principal Strengths

The Directors consider that the Target Group has the following principal strengths:

The Target Group has a longstanding manufacturing heritage in the piston aircraft engine manufacturing industry

General aviation is a highly regulated market by national government aviation safety organisations. The Target Group has been in the engine manufacturing industry since 1904 delivering its first certified aircraft engine in 1929 and its engine products have been used in the top 3 (in terms of fleet size) aircraft manufacturers of fixed wing piston powered aircraft, Beechcraft, Cessna and Cirrus Aircraft since 1930. Through the years the Target Group has developed state of the art design and technological capacity in terms of both products and manufacturing processes.

The Target Group offers a diversified product portfolio of engines for a broad range of aircrafts

The Target Group stands apart from other major competitors in the field in its ability to produce engines ranging across market sectors dominated by both Lycoming and Rotax and in its capacities to produce both gasoline and diesel fuelled variations. Long known for its dominance of the market in the over 250 HP engines, the recent addition of the CD100 line of engines for training aircraft and the Titan line of engines for kit aircraft hold promise if the Target Group can capture the anticipated uptick in this market quickly. In addition to its solid position in the top 3 aircraft manufacturers mentioned above, the Target Group engines power multiple models of diesel fuelled aircraft produced by Diamond Aircraft.

The Target Group has strong research and development capacity

In addition to environmental concerns associated with avgas powered engines, diesel fuelled engines hold substantial promise for the future of general aviation both inside the US and in the developing world for a variety of reasons, including lower fuel costs and improved access to fuel in areas that lack avgas. The Target Group's history of innovation in diesel engine technology uniquely positions it to capture these opportunities.

The Target Group has meaningful presence in key markets

With main operations in the US and Germany, the Target Group has established a manufacturing presence in both North America and Europe, the two regions of the world that presently account for more than 70% of the world market for piston engine powered aircraft. With the support of its controlling shareholder, Aviation Industry, the Target Group also has access to PRC, the world's largest growing consumer class in the world's fastest growing economy.

The Target Group enjoys support from its controlling shareholder

The controlling shareholder of the Target Group, Aviation Industry, is a PRC state-owned aerospace and defence company. In 2016, it was ranked 143rd in the Fortune Global 500 lists with revenue over US$60 billion. Aviation Industry provides the Target Group with resources needed to develop new markets, form strategic alliances within the industry for both vertical and horizontal integration and the ability to expand operations to meet growing demand in the developing world, especially in PRC.

Strategies

The Target Group aims to strengthen its leading position in the aircraft piston engine market through the following strategies:

Expand the gasoline product offerings of the Target Group to tap into competitor's market share

As a strategic move to expand its market share, the Target Group acquired the assets of Danbury AeroSpace, Inc. in 2015 which produces Titan engines and Titan engine parts under the PMA aviation regulation concept. The Titan products allow the Target Group to access the market segment filled by Lycoming®, a key competitor of the Target Group during the Track Record Period. Through such acquisition, the Target Group aims to increase its market share of the OEM new aircraft engine supply and also increase its market access with PMA parts of Lycoming®.

Expand the diesel product offerings of the Target Group to capture the market growth opportunity

While the present fleet of piston powered diesel fuelled aircraft is small relative to total fleet size, there are signs that more and more diesel powered engines are being introduced around the world. In the past, diesel technology could not be used in small and sports aircraft due to an unfavourable power-to-weight ratio. The Target Group has sought to improve the power-to-weight ratio of its diesel engines through using lighter materials, a modern turbocharger and common rail technology. Certain clients use the diesel engines of the Target Group in their UAS aircrafts, while the market for UAS aircraft and technologies represents the most dynamic market for growth in aviation presently. Currently the Target Group has a number of models of diesel engines in commercial production, entering production and under development. Please refer to the subsection headed "*Products and Services Overview — Piston engines — c. Continental diesel engine product*" below.

Expand the service offerings of the Target Group through acquisitions

In 2014, the Target Group acquired the assets of Southern Avionics and Communications, Inc. whose principle business is to provide installation and modification services of avionics and interior for small aircrafts. In 2015, the Target Group acquired United Turbine, whose principle business is to provide maintenance, repair and overhaul services for certain types of turbine engines. In 2015, the

Target Group established a senior staff position, vice president and general manager of CMS, directly responsible for the growing MRO business segment. By establishing this position, the Target Group aims to expand its MRO business and enter the higher value general aviation markets by providing a broader range of MRO services.

Establish strong presence of the Target Group in PRC market

PRC presents significant growth opportunities for general aviation in terms of sheer size, an increasingly affluent population and geography, as the country transitions from a largely agrarian society to a rapidly expanding manufacturing and service based economy. Significant opportunity exists for the emergence of new OEM manufacturers of piston engine aircraft to emerge in China. The Target Group set up CMB in 2014 for product sales, service and distribution in PRC and plans further development to provide technology development and engineering support for the growing number of new OEM aircraft developers being established in PRC.

According to Catalogue of Industries for Guiding Foreign Investment issued by the National Development and Reform Commission and the Ministry of Commerce, CMB, as a foreign investor, is required to establish a joint venture with a domestic party (who must be the controlling shareholder holding more than 50% ownership of the joint venture) for it to engage in any businesses related to, among others, designing, manufacturing and maintenance of aircrafts for trunk lines, regional aircrafts, and design and manufacturing of unmanned aerial vehicles. Moreover, designing, manufacturing and maintenance of general aircrafts are limited to Sino-Foreign Cooperative Joint Venture.

Upon Acquisition Completion, the Company will endeavour to look for an appropriate party to invest in the joint venture with CMB as and when necessary.

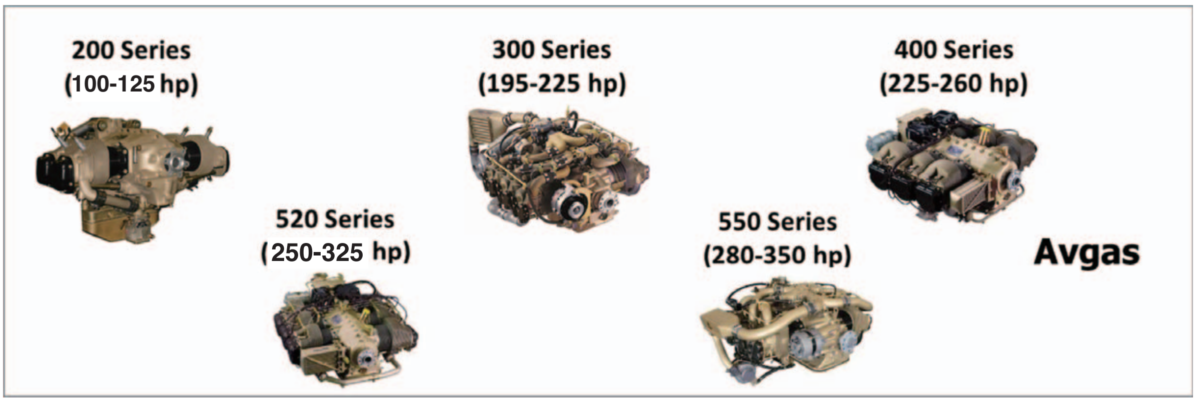
Products and Service Overview

The Target Group is principally engaged in the research, design, manufacturing and sales of aircraft piston engines fuelled by gasoline or diesel and engine spare parts and the provision of aftermarket service and support for general aviation aircraft through factory owned service centres.

Piston Engines

The engine products of the Target Group can be categorised into 3 categories and 10 series as set out below.

a. *Continental gasoline engine product*



The gasoline engine product is the traditional business line of the Target Group that can be traced back to 1904. As set out below, the Target Group has five gasoline product lines. The typical pricing for new engines is in the US$22,000 to US$100,000 range, with rebuilt and overhauled engines having a pricing of between US$2,500 to US$7,500 per engine less than their new equivalent.

One primary focus of the Target Group is on the high horsepower sub-segment represented by the 520 Series and 550 Series used in new production premium performance gasoline piston engine aircrafts. However, as aircraft and engines have relatively long life spans, the Target Group still provides aftermarket sales of engines for existing aircraft in the low and mid horsepower range. The key series sold and supported by the Target Group are:

(i) *200 Series*

The 200 Series engine generates 100-125 HP. A new 200 Series engine is priced at approximately US$25,000 to US$48,000 depending upon options and configuration.

(ii) *300 Series*

The 300 Series engine generates 195-225 HP. A new 300 Series engine is priced at approximately US$44,000 to US$75,000 depending upon options and configuration.

(iii) *400 Series*

The 400 Series engine generates 225-260 HP. A new 400 Series engine is priced at approximately US$35,000 to US$44,000 depending upon options and configuration.

(iv) *520 Series*

The 520 Series engine generates 250-325 HP. A new 520 Series engine is priced at approximately US$44,000 to US$83,000 depending upon options and configuration.

(v) *550 Series*

The 550 Series engine generates 280-350 HP. A new 550 Series engine is priced at approximately US$46,000 to US$96,000 depending upon options and configuration.

b. *Continental Titan series gasoline engine product*

The Titan Series engines generate 150-270 HP. These engines were added to the Continental product line in 2015 and contributed a little more than 1.0% of the Target Group's revenue in 2016. Such engines are currently used in the experimental aircraft market segments. In addition, the Titan engine products are being certified for use in OEM aircraft currently powered by Lycoming®. There are two series of engines available in the Titan line, the 4 cylinder 300 series and the 6 cylinder 500 series.

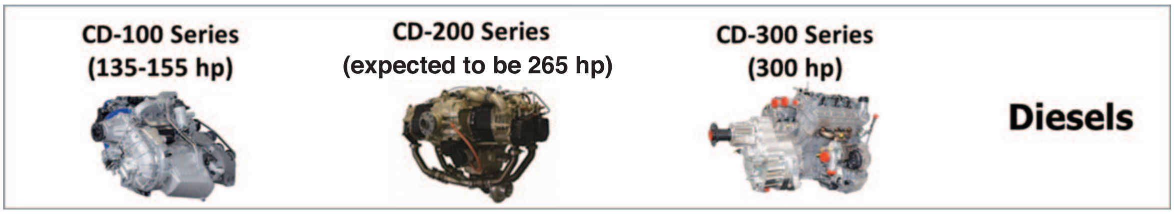
(i) *Titan 300 series engine*

Titan 300 series engines have a horsepower range of 150-200 HP. Titan 300 series base engines are priced at approximately US$24,000. However, due to the nature of the kit/experimental market, which allows substantial customisation, the engine's final price can be much higher based on options and configuration.

(ii) *Titan 500 series engine*

Titan 500 series engines have a horsepower range of 260-270 HP. Titan 500 series base engines are priced at approximately US$45,000. However, due to the nature of the kit/experimental market, which allows substantial customisation, the engine's final price can be much higher based on options and configuration.

c. *Continental diesel engine product*



One focus of the Target Group's diesel-powered engines is on high use aircraft (e.g. pilot training and passenger transport) since it has several advantages in that market segment, including: (i) its engines are easier and more efficient to operate and maintain on a longer-term basis, compared to other piston-powered engines; and (ii) diesel is more fuel and cost efficient compared to leaded avgas (the leading alternative to diesel).

As set out below, the Target Group has three diesel product lines.

(i) *CD100 Series*

CD135 and CD155 represent a common platform capable of delivering either 135 or 155 HP. These products are in commercial production since 2003. Such engines are used in propeller-driven aircrafts which usually hold four passengers or less. Diesel engines with the 135 horse power rating are priced at approximately €33,000 for a base engine to approximately €55,000 for a full installation kit and the diesel engines with the 155 horse power rating are priced at approximately €39,000 for a base engine to approximately €60,000 for a full installation kit.

CD155R is a diesel engine which generates 155 HP intending to target the general aviation and UAV markets. It is now under development and is expected to finish certification in the middle of 2018.

CD155 Pusher is a diesel engine which generates 155 HP and is designed for pusher applications intending to target the general aviation and UAV markets. It has completed development and was certified by EASA on 18 October 2017.

(ii) *CD200 Series*

A new diesel engine model under the CD200 series which is expected to generate 265 HP and finish certification in 2018. It is intended to target the mid-horsepower aircraft segment in the general aviation and UAV markets.

(iii) *CD300 Series*

CD300 Series are diesel engines intending to target the general aviation and UAV markets. It was certified by EASA in June 2017. The engine is currently being installed for testing in a single engine, fixed wing OEM aircraft.

Aftermarket Spare Parts

The Target Group manufactures a full line of aftermarket parts for the repair, maintenance and overhaul of both Continental and Lycoming branded engine products, such as cylinders, crankshafts, crankcases, ignition systems, gear boxes. Sales of aftermarket spare parts accounted for 30%-42% of total revenue of the Target Group during the Track Record Period.

MRO Services

The Target Group offers a wide range of aviation services including but not limited to (i) overhaul or repair of Continental, Lycoming, and P&W PT6 aviation engines, (ii) major power plant and airframe maintenance, (iii) factory engine sales and engine installations, (iv) avionics sales, repair and installation, (v) aircraft interior upgrades and refurbishment, (vi) supplemental type certificate installations, and (vii) fixed-base operator services.

The Target Group started its services business back in 1999 when it acquired Teledyne Mattituck Services, Inc. Traditionally, it provided maintenance, repair and overhaul services for engines parts. Overhaul typically means a complete disassembly, inspection, repair, reassembly, test, and approval for return to service within the fits and limits specified by the manufacturer's overhaul data. An overhaul engine can normally be resold in the aftermarket at a lower price than new engines.

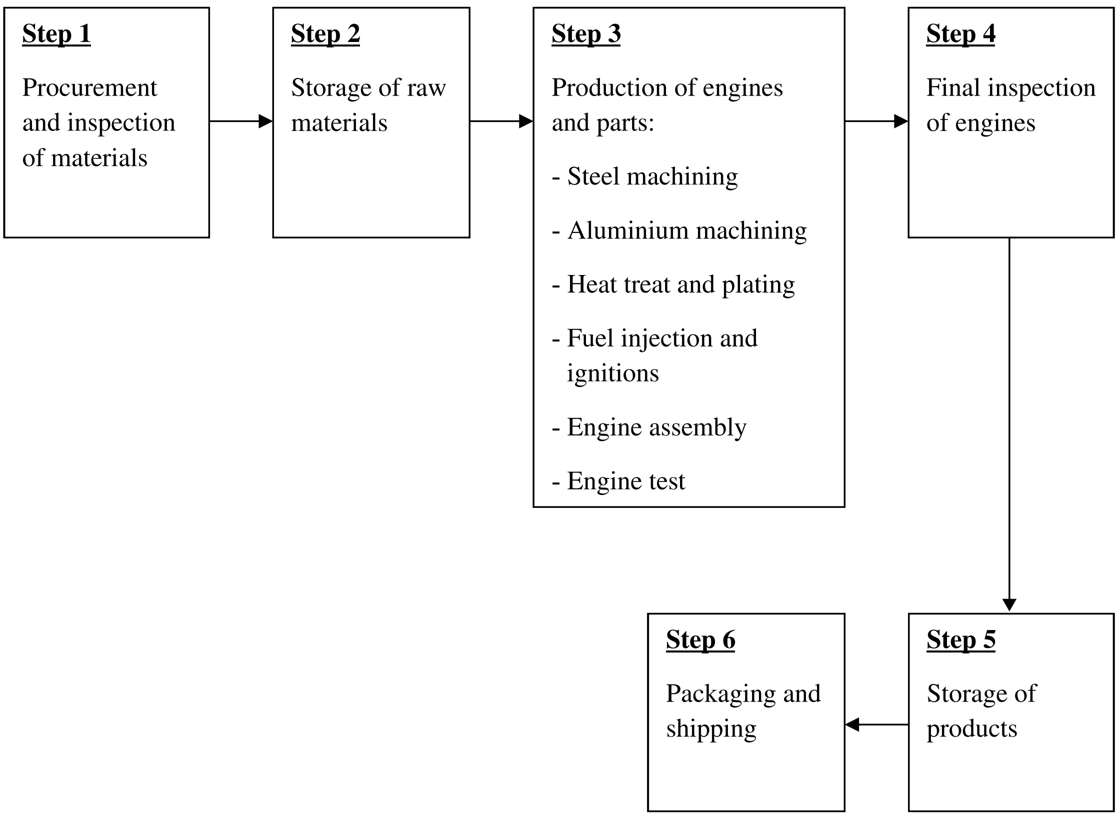
After its acquisition of Southern Avionics and Communications, Inc. and United Turbines Corp., the Target Group now also provides installation and modification services of avionics and interior for small aircrafts and maintenance, plus repair and overhaul services for certain types of turbine engines.

Production Process

The Target Group carries out its manufacturing activities at its production facilities located in Mobile, Alabama, the USA and Sankt Egidien, Germany.

The Target Group's factories produce the major parts and components, while the rest are out-sourced parts. Both the USA and German manufacturing sites perform machining and assembly operations in a variety of components used in the manufacturing of engines the Target Group produces. Manufacturing operations include components such as crankshafts, camshafts, crankcases and cylinders. The Target Group regularly reviews and maintains high quality suppliers globally that supply the out-sourced parts thereby maintaining core technology control while maximising the cost benefit of a global supply chain. The engine components produced by the Target Group are mainly used for the manufacture of the engines of the Target Group, as well as aftermarket parts that are used to maintain all of its engine products. In addition, the sites manufacture or assemble PMA parts that are used for the repair, maintenance and overhaul of Lycoming® branded engine products. All engine components purchased either directly from third parties or manufactured by the Target Group before being used internally or sold to customers must pass quality control and testing to ensure the quality of the final product. All engines manufactured by the Target Group are tested before delivery to the customer.

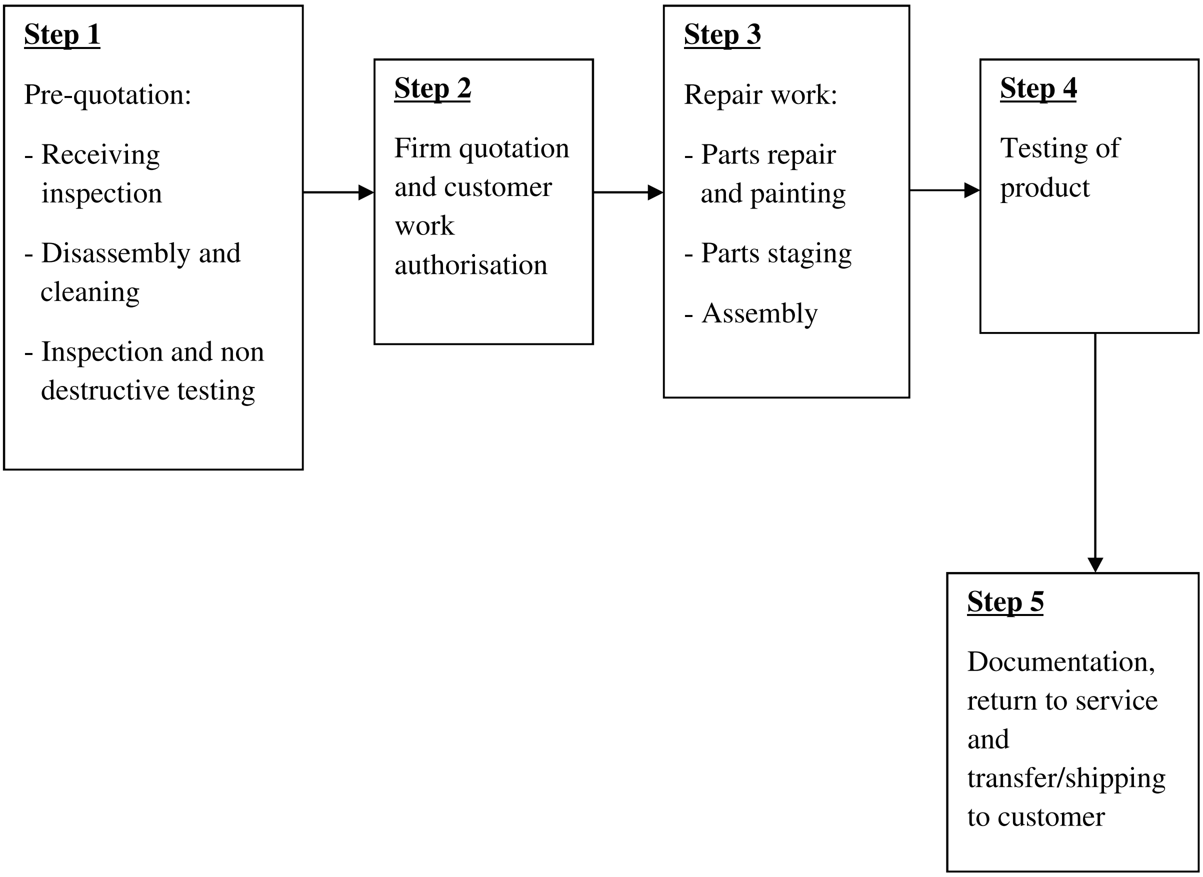
Set out below is an operation flow of the Target Group's engines manufacturing arm which comprises CMI and TMG:



Service Process

The Target Group provides its MRO services at its service centers in Fairhope, Alabama, the USA and Miami, Florida, the USA. Its MRO maintenance centre in Fairhope has recently completed a million-dollar renovation to establish a maximum, single shift, annual work capacity of 450 engine overhauls and 25,000 billable aircraft/avionics repair hours.

Set out below is CMS's work flow that applies to any aspect of the MRO business performed by CMS:



Property

The facilities of the Target Group in Mobile, Fairhope and Miami in the USA are leased. The manufacturing centre in Mobile has building space of approximately 606,016 square feet and land area of approximately 46 acres. The service centre in Fairhope has a total building area of 107,947 square feet. The service centre in Miami has shop area of approximately 30,000 square feet, office space and parking area of 6,000 square feet.

The Target Group owns two of its operation sites in Germany, one in St. Egidien, Germany and one in Altenburg, Germany. The manufacturing centre in St. Egidien has a total area of 35,521 square metres. The service centre in Altenburg has a total area of 21,499 square metres.

The Target Group leases the office space for its third German operation site which includes a small engineering office in Hamburg, Germany. The rental area in Hamburg has a size of approximately 300 square metres.

The Target Group does not own any land or property in the PRC. Its CMB subsidiary leases office space of 135 square metres and warehouse space provided by local logistic company (Beijing Hangji International Logistics Co., Ltd.) to support staff and parts storage in support of its PRC customer base.

Production Capacity

The Target Group is in the process of consolidating its current manufacturing operations in Mobile into a single new manufacturing facility of 255,250 square feet nearby to enhance its operational efficiency, energy efficiency and personnel productivity.

The total capital expenditure for this project is expected to be around US$40.3 million to be financed by external bank loans and internal resources. The Target Group will retain one building currently dedicated to its engineering development projects and have a new building constructed. The new building to be constructed will be funded by third parties and leased to the Target Group at standard commercial terms for a period of 20 to 25 years with options to extend based on the then market conditions. The retained building will continue its lease with the current landlord. The Target Group expects that project to be completed towards the end of 2019.

Suppliers

The five largest suppliers of the Target Group for each of FY2014, FY2015, FY2016 and 1H2017 are suppliers of engine parts and components located either in the USA or Europe and are independent from the Target Group, the Company and/or their associates. These suppliers contributed approximately 16.3%, 15.6%, 13.8% and 13.3% of the total cost of sales for FY2014, FY2015, FY2016 and 1H2017 respectively.

For the Track Record Period, the raw material and engine component suppliers generally offer the Target Group credit terms of 30 days to 60 days from date of goods received or invoices issued. The credit term extended by such suppliers may vary, depending on, among others, the Target Group's credit rating, the relationship with the particular supplier and the volume and prices of their purchases.

Utilities

Currently, the utilities used by the Target Group include electricity, water, and natural gas and are provided by the approved and regulated local utility suppliers for these commodities. During the Track Record Period, the Company did not experience any disruption in its operation due to any serious shortage of supply of utilities.

Inventory

The Target Group has a warehouse for the storage of raw materials, out-sourced parts and finished products in its manufacturing centres and service centres in the USA, PRC and Germany. For each of FY2014, FY2015, FY2016 and 1H2017, the Target Groups' inventory amounted to approximately US$39 million, US$46 million, US$52 million and US$60 million, respectively. It is the intention of the Target Group to maintain its inventory level at a turnover period of between 125 days to 170 days. However, occasional fluctuations in purchasing, production and shipment patterns may result in the inventory turnover period falling outside this range. For each of FY2014, FY2015, FY2016 and 1H2017, the Target Groups' inventory turnover periods were approximately 129 days, 139 days, 129 days and 149 days, respectively.

As at 31 December 2014, 2015 and 2016 and 30 June 2017, the Target Group's obsolete inventory amounted to US$3.9 million, US$3.7 million, US$2.6 million and US$3.3 million, respectively.

Quality Control

The manufacturing processes and products of the Target Group are subject to strict quality assurance. A data recording and specification system facilitates seamless electronic traceability of all manufactured products. The Target Group also has production certification, which is FAA approved in the USA and EASA approved in Germany in respect of production of specific product based on demonstrated production processes and quality systems.

As for out-sourced parts, all suppliers must meet the quality standards set by the Target Group. They are normally required to submit samples of the relevant out-sourced parts for testing. All externally supplied raw material and engine components are checked for conformity with the required quality and specifications, either through routine inspection or sample testing, depending on whether the suppliers have strong quality control capabilities and have consistently provided the Target Group with high quality supplies.

Inspection is also conducted throughout the process during the production process. In addition, production is overseen by dedicated quality control inspectors according to pre-determined standards and inspection conditions. Any abnormalities discovered are rectified immediately and recorded. The production equipment operators of the Target Group are required to adhere strictly to standard equipment operating procedures.

Sales and Marketing

OEM New Engines

The Target Company sells factory new engines in two different market segments, OEM new aircraft and as aftermarket replacement engines. Engines are sold alone as a completely tested and ready to install unit.

Pricing is negotiated with each OEM independently and is either annually adjusted, or in limited cases based on jointly negotiated multi-year contracts that specify pricing and annual pricing adjustments. For OEM relationships not managed by a multi-year contract, the relationship is governed by the company's standard Purchase Order and Terms and Conditions. Where an annual pricing change is instituted, this is done either through issuing a pricing letter for OEMs without a multi-year contract, or strictly following the pricing terms defined in the multi-year contracts for OEMs with such agreements.

Once an engine selection is made for an airframe, it is difficult to easily switch to a different engine source since (i) airframe and engine are certified together; and (ii) cost for recertification is very high.

Aftermarket Engines

The average airframe life is above 30 years while the average engine life is around 12 years or 1,200 to 2,200 hours of use (whichever occurs first). Airplanes typically replace their engines over 3 times using the following options: (i) factory new engines, (ii) factory rebuilt engines or (iii) third party overhaul.

The aftermarket engines are sold through international resellers. Resellers place orders at a "Distributor Net" price. Aftermarket engines require the return of a used engine, which may be used to produce a rebuilt engine in accordance with FAA regulations. Failure to return a core requires payment of a core charge by the customer.

Aftermarket Spares

The aftermarket spares are used in regular engine maintenance, engine repairs and engine overhauls when the overhaul engine has parts that cannot be reused.

During the Track Record Period, the Target Group sold aftermarket spares to a group of distributors until CMI entered into an exclusive distribution agreement with Aviall Services, Inc. in April 2016. Since then, Aviall Services, Inc. has been the exclusive distributor of CMI for the aftermarket parts for repair, maintenance and overhaul of both Continental and Lycoming® branded engine products. Pricing is based on a set distributor net price and a market list price.

Customers

The key end customer groups of the Target Group are (i) manufacturers of new piston powered aircraft; (ii) owners or maintainers of existing general aviation aircraft; and (iii) experimental and kit aircraft owners.

The Target Group has maintained stable and long-term relationships with their customers. As of 31 December 2014, 2015 and 2016 and 30 June 2017, the Target Group had 1,598, 2,114, 1,902 and 712 customers, respectively. The growth in orders from 2014 to 2015 reflects the impact of acquisitions while the drop in orders from 2015 to 2016 reflects the consolidation of distributors into the Aviall Master Distribution program.

The Target Group's business is global with primary revenue predominantly originated in North America. For FY2014, FY2015, FY2016 and 1H2017, approximately 77.8%, 78.7%, 79.8% and 77.3% of the Target Group's revenue was generated from customers from North America. Set out below is the geographical breakdown of the Target Group's revenue for FY2014, FY2015, FY2016 and 1H2017.

Region of customer	2014		2015		2016		Six months ended 30 June 2017	
	Amount (US$'000)	*% of the Target Group's revenue*	*Amount (US$'000)*	*% of the Target Group's revenue*	*Amount (US$'000)*	*% of the Target Group's revenue*	*Amount (US$'000)*	*% of the Target Group's revenue*
North America	125,650	77.8%	128,788	78.7%	162,980	79.8%	76,829	77.3%
Europe	19,737	12.2%	20,187	12.3%	25,357	12.4%	11,651	11.7%
Others	16,057	10.0%	14,714	9.0%	15,978	7.8%	10,952	11.0%
Total	161,444	100%	163,689	100%	204,315	100%	99,432	100%

Major Customers

The five largest customers of the Target Group contributed approximately 35.6%, 31.8%, 46.8% and 60.8% of the total sales for FY2014, FY2015, FY2016 and 1H2017, respectively. One of the Target Group's OEM customers is Cirrus Design Corporation ("**Cirrus**"), which is a subsidiary of Aviation Industry and a general aviation airframe manufacturer in the USA. The Target Group reported an amount of sales to Cirrus of approximately US$20 million, US$19 million, US$20 million and US$8 million which accounted for 12.5%, 11.6%, 9.8% and 8.4% of its total revenue in FY2014, FY2015, FY2016 and 1H2017, respectively.

Contractual Model

The Target Group typically operates under one of two contractual types: (i) Purchase Order and Terms of Sale issued for groups of products; and (ii) Master Purchase Agreement which is an agreement entered into by the parties that defines all aspects of the relationship, products, pricing structures and terms.

The Target Group entered into an exclusive distribution agreement with Aviall Services, Inc. (Aviall) in April 2016 which will be effective until 31 December 2026. Since then, Aviall has been the exclusive distributor of CMI for the aftermarket parts worldwide excluding PRC. Pricing is based on a set distributor net price and a market list price.

The Target Group sells product ranging from pre-pay for retail style transactions with aircraft owners through credit terms that typically are 45 days or less. However, certain customers may receive better terms.

Warranty Policy

The Target Group provide warranties on their products to all of their customers. Under the warranty, the Target Group typically agrees to repair and replace defective parts for a period of one to three years. For FY2014, FY2015, FY2016 and 1H2017, the warranty costs amounted to US$2.23 million, US$2.42 million, US$4.06 million and US$1.08 million, respectively.

Product Return Policy

The product return policy of the Target Group is managed in accordance with its warranty terms. During the Track Record Period, the Target Group confirmed it did not receive any material product returns or make any large-scale product recalls due to quality defects, which would have a material adverse impact on the business financial condition or results of operations of the Target Group.

Research and Development

The research and development activities of the Target Group focus on designing and developing new models of piston engines as well as improving various aspects of the engine performance, such as fuel efficiency, reliability and ease of operation. As of the Latest Practicable Date, the Target Group had 18 effective patents.

For FY2014, FY2015, FY2016 and 1H2017, the research and development costs of the Target Group, amounted to US$4.3 million, US$5.4 million, US$5.2 million and US$2.3 million respectively, which accounted for 2.65%, 3.32%, 2.53% and 2.28% of its revenue, respectively.

Employees

As at the Latest Practicable Date, the Target Group employs 463 employees in the USA, 193 employees in Germany and 11 employees in PRC.

Training and Remuneration

The Target Group places significant emphasis on staff training and development. It is the policy and process of the Target Group to develop future leaders and managers through training, schooling and practical experience. The Target Group retains a coaching and mentoring firm to help existing and new leaders to grow and learn. It has also in place an educational assistance plan to financially support its full-time employees to undertake approved courses of study.

The Target Group conducts periodic performance reviews for all of its employees and their salaries and bonuses are performance-based.

Employee Relations

The Target Group has not experienced any strikes or other labour disturbance which have materially affected their business, financial condition or results of operations during the Track Record Period and as of the Latest Practicable Date.

CMI is operating under a one-year contract with the United Autoworker's Local Union 1639 (the "**UALU**") that covers the wages, benefits and holidays of factory workers which will expire on 20 March 2018. CMI expects to negotiate the terms of the renewal prior to the expiration date. The formal negotiation schedule will not be set until January 2018.

If negotiations with the UALU are not successful and the contract is allowed to expire on 20 March 2018, under US labour laws, CMI will continue to have a duty to negotiate with UALU in good faith and will be restricted from unilaterally altering the terms of employment for the union employees until the negotiations have reached a good faith impasse. To facilitate negotiation, the UALU and CMI would have the option of requesting a mediator with a view towards enabling the parties to reach a settlement. If negotiations were to ultimately reach an impasse (whether it be at the time of expiration of the agreement or after), the parties could operate without a contract, and the factory workers could strike, which would disrupt business operations.

As regards the German operations, TMG has ongoing negotiations with the labour union regarding the conclusion of a company collective bargaining agreement ("**CBA**"), which contains a new remuneration structure and was originally envisaged to take effect at the end of 2017. Currently the main topics under the current negotiations are about setting up clear definitions on job descriptions covering all functions performed within TMG, and establishing remuneration range for each job description. As at the Latest Practicable Date, the negotiations are proceeding cordially and are making progress, the Target Group expects that negotiations will continue through the end of this year and will likely to conclude in early 2018, delaying the implementation of the CBA.

If CBA is entered into as expected, the compensation levels and criteria of TMG are expected to change. However, it is unlikely to have a material impact to TMG; and in any event, TMG would not be precluded from taking offsetting actions to control compensation costs.

On the other hand, if the negotiation fails and the CBA is not entered into, the level of compensation and other employment conditions will continue to be governed by provisions outside of a CBA. The labour union could in principle try to seek the conclusion of a CBA by initiating a strike.

Employee Benefits

The Target Group operates a geographically diverse business with operations and team members in multiple countries.

In accordance with applicable USA laws and regulations, the Target Group set benefit plans that meet the requirements and makes payments as mandated related to social security and medicare contributions; worker's compensation insurance; and state and federal unemployment insurance. The Target Group also maintains compliant retirement benefit plans for its employees in the USA that include a Defined Contribution Plan (401k) for salary based employees and a Defined Benefit Plan for certain historic members of the union and a Defined Contribution Plan for newer members of the union. The Target Group also has health care insurance covering its employees in the USA. Other employee benefits for employees in the USA include memberships in a credit union, an onsite fitness centre, and tuition reimbursement for higher education. As of the Latest Practicable Date, the Target Group has complied with all statutory labor laws and regulations applicable to its operations in the USA in all material aspects.

In accordance with applicable German laws and regulations, the Target Group has made contributions to social insurance scheme for its employees in Germany. As of the Latest Practicable Date, the Target Group has complied with all statutory labor laws and regulations applicable to its operations in Germany and the European Union in all material aspects.

In accordance with applicable PRC laws and regulations, the Target Group has made contributions to social security insurance funds (including pension plans, medical insurance, work-related injury insurance, unemployment insurance, and maternity insurance) and housing funds for its employees in PRC. As of the Latest Practicable Date, the Target Group has complied with all statutory social insurance and housing fund obligations applicable to it under PRC laws and regulations in all material aspects.

Insurance

Insurance Policies

The Target Group maintains a robust general insurance and product liability insurance program to minimise the risk of unexpected material impacts to the business due to contractual, general, natural or product liability events. The Target Group maintains two primary policy structures, general and business risk and product liability each placed with high quality insurers. The general insurance program is placed with Ironshore Specialty Insurance Company under traditional terms based on a US$2 million per occurrence base. It is further supported with an umbrella liability policy placed with ACE Property and Casualty Insurance Company (Chubb). The product liability program is placed through Lloyds of London as managed by Marsh Risk & Insurance Services (Marsh), with multiple insurers led by Allianz Global Risks US Insurance Company and supported by 10 other direct insurers and 10 other insurers operating through the reinsurance market.

The product liability insurance program operates a Self Insured Retention based program that means the Target Group is responsible for first dollar cost of liability capped at a maximum liability that is set each year during the negotiations for the insurance renewal. Upon expending the Self Insured Retention, the Target Group's insurers will be responsible for all remaining product liability expenses for that policy year, subject to policy limits.

The Target Group also maintained a provision to reflect the risk of adverse payments based on expected outflow of resources to cover the product claims and liabilities and any related costs which has been deemed effective and adequate by the Group's auditors and managers to meet the projected risks.

Captive Insurance Program (Mangrove Insurance Solutions, PCC)

The Target Group participates in a captive insurance program, which enables the Target Group to purchase insurance through reinsurance markets that would not otherwise be available. By participating in a captive insurance program, the Target Group has been able to significantly reduce the costs of acquiring liability insurance.

The Target Group participates in the captive insurance program through the rental of a protected cell of Mangrove Insurance Solutions, PCC, a protected cell captive insurance company domiciled in Washington D.C. ("**Mangrove**"). Specifically, CMI is a party to a participation agreement, dated 23 May 2011, by and among CMI and Mangrove, pursuant to which CMI agreed to acquire 1,000 preferred shares with respect to Mangrove Cell 1 PC, a protected cell of Mangrove. The preferred shares were issued pursuant to a Subscription Agreement, dated as of 23 May 2011. CMI is also a party to a certain management agreement, dated as of 23 May 2011, by and among Marsh Management Solutions, Inc., CMI, and Mangrove, pursuant to which March Management Solutions, Inc. was appointed as the manager of Mangrove. CMI paid Marsh Management Solutions, Inc. an annual fee of US$45,650.00 for the period between 1 July 2016 and 30 June 2017.

Insurance claims during the Track Record Period

During the Track Record Period, the Target Group did not bring any claims in relation to its PRC operations but brought an aggregate of approximately 167 claims against damage events for which compensation was sought in relation to its US operations. Of these claims, 6 claims fall within the scope of its general liability and automobile policies, 49 claims fall within the scope of its aviation product liability policies and 112 claims fall within the scope of its workers' compensation policies. An aggregate amount of compensation received based on the aforementioned claims amounted to approximately US$4.7 million, of which general liability and automobile claims, product liability claims and workers compensation claims accounted for US$14,600, US$4,610,000 and US$68,000, respectively.

During the Track Record Period, the Target Group brought a total of five claims against damage events for which compensation was sought in relation to its German operations. Three of those damage events fall within the scope of the transport insurance and one of those damage events falls within the scope of the aviation liability insurance and the aviation hull insurance, respectively. An aggregate amount of compensation received based on the aforementioned claims amounted to EUR 14,722.51.

Legal Proceedings and Compliance

Excluding the Target Group's product liability program as referred to under the heading "Insurance" above, during the Track Record Period, the Target Group was not involved in any litigation, arbitration or administrative proceeding that, individually or in the aggregate, could have had a material adverse effect on the business, financial condition or results of operations of the Target

Group, and as of the Latest Practicable Date, there was no existing or threatened litigation, arbitration or administrative proceeding against the Target Group or any of its directors that, individually or in aggregate, could have a material adverse effect on the business, financial condition or results of operations of the Target Group.

During the Track Record Period and, as of the Latest Practicable Date, the Target Group was in compliance with all relevant USA, Germany and PRC laws and regulations in all material respects and had obtained all material permits and licenses required for the Target Group's operations in the USA, Germany and the PRC.

Environmental Protection

The Target Group is required to comply with the environmental protection laws and regulations in the USA, Germany and the PRC. The Target Group has confirmed that its current operations are in compliance with the applicable laws and regulations on environmental protection in all material respects. As at the Latest Practicable Date, the Target Group has confirmed that it was not subject to any unresolved governmental enforcement action relating to alleged violation of environmental protection laws or regulations except for ongoing environmental investigation, cleanup, monitoring and site closure obligations and activities being performed by the Target Group's USA operation pursuant to regulatory requirements of the governmental environmental protection agency having jurisdiction nor had the Target Group been fined for contravening environmental protection laws or regulations.

Intellectual Property Rights

Trademarks

As at the Latest Practicable Date, the Target Group had one trademark application and 13 registered trademarks in US, two registered trademarks in EU, and one national German trademark.

Prior to the acquisition of CMI by AVIC International, Teledyne, the then owner of CMI, was involved in a dispute with Continental Aktiengesellschaft ("**Continental AG**") regarding "Continental" trademarks and reached a settlement agreement on 24 June 2009, pursuant to which:

(1) Continental AG agreed to not use the "Continental" mark anywhere in the world in connection with aerospace vehicle power plants, piston engines or turbine engines or parts and controls specifically designed for such power plants, and engines or services related to such power plants and engines; and

(2) Teledyne agreed not to use the "Continental" mark anywhere in the world in connection with i) parts or accessories for automobiles and motor cycles, and ii) tires, and unless such goods are used with aerospace vehicle power plants, piston engines or turbine engines, rubber goods, goods made of rubber-like materials or plastic materials, and goods made substantially of rubber or plastic which were formerly made of such materials but are now made or made in the future of metal or other materials.

All of Teledyne's right, title and interest in such settlement agreement with Continental AG mentioned above were assigned to CMI in 2011.

Patents

As at the Latest Practicable Date, the Target Group had seven patents in USA, which are related to manufacturing of engines, one patent application and 11 patents in Europe, among which five of them are related to a "method for operating a self-compressing aircraft engine", one of them is related to a "common-rail high-pressure pump", and the rest are related to an "engine-management system for diesel aircraft engines".

Knowhow

The Target Group possessed certain know-how related to the operation of stroke piston machines with kerosene, which is necessary for the development of certain engine control devices needed for the operation of aircraft engines.

Besides self-owned know-how, as at the Latest Practicable Date, there was an in-force license agreement with between the Target Group and Daimler AG pursuant to which Daimler AG granted a non-exclusive, non-sublicensable license to the Target Group to develop, manufacture, sell, use and advertise products that use the underlying patents, technology and know-how of a specified diesel engine (OM640 EU4).

Health and Safety Compliance

Pursuant to health and safety laws and regulations in the USA, Germany and PRC, the Target Group is required to ensure a safe production and working environment for its employees by providing them with adequate protective clothing and gear, safety education and training and having dedicated safety management personnel, among other requirements. The Target Group has processes and procedures in place to ensure compliance with health and safety laws.

In respect of the Target Group's German and PRC operations, during the Track Record Period, the Target Group confirmed it was not involved in any material breach of any relevant health and safety laws and regulations, and there were no incidents resulting in material injuries to its employees during the production process.

In respect of the Target Group's US operations, while instances of non-compliance with applicable health and safety laws and regulations have occurred during the Track Record Period, representatives of the Target Group have noted that, with respect to such instances, neither the quantity, scope nor fines, where imposed, constitute trends or costs that are material in nature to the Target Group or its operations. As confirmed by the Target Group, the total fines of such non-compliance was US$12,300.

In connection with employee safety, the Target Group is obligated under US workers' compensation laws to pay benefits to employees injured in the line and scope of their employment (whether or not such injuries arise from violations of health or safety laws). The Target Group maintains processes to handle workers' compensation claims and has established quarterly review to track the status and to manage new claims should they arise. As of the Latest Practicable Date, the Target Group has disclosed that it has fourteen (14) active US workers' compensation claims with an outstanding amount of approximately US$0.4 million which the Target Group is responsible for. Representatives of the Target Group have confirmed that these claims do not represent a growing trend or reflect year over year change that are outside of company risk management.

After the completion of the Acquisition, it is expected that following candidates will be proposed to continue to serve as senior management of the Target Group.

Board of directors of CMG

Name	Age	Proposed Position
Yu Yimin	60	Chairman of CMG board of directors
Pan Linwu	53	Vice chairman of CMG board of directors
Rhett Ross	53	Director, President and CEO of CMG
Andrew Roberts	57	Director of CMG
Robert Wilson	60	Director of CMG
Yu Xiaodong	45	Director and Executive Vice President of CMG, General Manager of CMB, Managing Director of TMG

Mr. Yu Yimin, aged 60, Chairman of CMG. In November 2007, he was appointed as the Deputy General Manager of AVIC International. He holds a Master's degree in Management Science and Engineering from Beihang University, and a Bachelor's degree in Corrosion and Protection of Aviation Materials from Nanchang Institute of Aviation Industry. He was appointed to the role of Chairman and CEO of CMI (formerly known as Teledyne Continental Motors, Inc.) in April 2011. He has also been a researcher level senior engineer since September 2013. He was the Chairman of the board of directors of AVIC International Trade & Economic Development Ltd. from 2010 to 2014.

Mr. Pan Linwu, aged 53, Vice Chairman of CMG. He has been an Executive Director of the Company since February 2008 and the Deputy Chairman of the Company since January 2013. He holds a Master's degree in Aeronautical Engineering from Beihang University, an EMBA from Cheung Kong Graduate School of Business, a Bachelor's degree in Engineering from Beihang University and a Specialised Diploma in Financial Accounting from Beijing Open University. In 1989, Mr. Pan served as the Deputy Head of the General Administration Division of the Audit Department of the Ministry of Aero-Space Industry. In September 1993, he was transferred to AVIC International and served as the Deputy Director of the Audit Division and was promoted to Director in May 1996. Mr. Pan had been the Chief Financial Officer of AVIC International since 2001, and he was also appointed as the Deputy General Manager of AVIC International in April 2012. In addition, he was the Executive Director of AVIC International Holdings Limited from June 2012 to February 2017. He was also a Director of Tacko International Limited, which is a substantial shareholder of the Company from October 2013 to April 2017.

Mr. Rhett Ross, aged 53, Director, President and CEO of CMG, mainly responsible for overseeing the day-to-day work of every aspect of the Target Group. He holds a Master's degree in Engineering and a Bachelor's degree in Nuclear Engineering from the University of Florida. In 2000, he became the Senior Systems Engineer of Teledyne Energy Systems, Inc; in 2001, he became the General Manager, then the President of Teledyne Energy Systems, Inc. He was appointed in November 2007 by Teledyne Technologies, Inc. as the President of Teledyne Continental Motors (Piston Engines). In 2011, CMI was acquired by AVIC International and he was appointed as a Director of CMI. In 2014, he was also appointed as the Vice President of AVIC International.

Mr. Andrew Roberts, aged 57, Director of CMG. In April 2002, he was appointed as the Executive Vice President of Northwest Airlines, Inc. In 2014, he was appointed as the CEO of Align Aerospace LLC, and he resigned from the positions of CEO and Director in 2015. In 2015, he was appointed as a Director of Sky West, Inc.

Mr. Robert Wilson, aged 60, Director of CMG. In 1981, he was appointed as the Senior Design Engineer at Solar Turbines, a division of Caterpillar Inc. In 1989, he joined Textron Lycoming and was appointed as the Manager of Preliminary Design and New Business, and in 1990 became the Director of Advanced Product Development. In 1994, he was appointed as the Director of another division when Textron Lycoming was acquired by AlliedSignal Engines. In 1999, he was appointed to the role of Vice President of the hydromechanical product line as AlliedSignal Engines was acquired and became Honeywell Aerospace. In 2001, he was appointed as the Vice President of a product line and in 2002 became the Vice President and General Manager of Defence Avionics Systems of Honeywell Aerospace. In 2005, he was appointed as the President of Business and General Aviation Business of Honeywell Aerospace. He currently holds board positions with TurbineAero, Inc., Genesys Aerosystems Group, Inc., Frustum Inc. and CMG.

Mr. Yu Xiaodong, aged 45, Director and Executive Vice President of CMG, General Manager of CMB and Managing Director of TMG, mainly responsible for the Target Group's sales, customer services and support, and development of OEM customers in PRC. He holds a Master's degree in Economics from the University of International Business and Economics, Beijing. In 1997, he first joined AVIC International as a project manager. In 2001, he was appointed as an assistant to the General Manager; and in 2004, he was appointed as the Deputy Director of the Operations and Management Division of the International Cooperation Department. In 2005, he was appointed as the Director of the Organisation and Performance Division of the Human Resources Department and in 2007, he was appointed to the role of Deputy Manager of the Human Resources Department. In 2010 and 2012, he was appointed as the Manager and the Head of the Auditing Department of AVIC International. In January 2016, he was appointed as the General Manager of CMB.

Senior Management of the Target Group

Name	Age	Proposed Position
Rhett Ross	53	Director, President and CEO of CMG
Karen Hong	50	CFO of CMG
Yu Xiaodong	45	Director and Executive Vice President of CMG, General Manager of CMB and Managing Director of TMG
Stephen Ginger	61	Executive Vice President and General Counsel of CMG
Michael Skolnik	37	Executive Vice President of Global Operations of CMG
Jürgen Schwarz	47	Executive Vice President of Engineering of CMG and Managing Director of TMG

For detailed biographies of Mr. Rhett Ross and Mr. Yu Xiaodong, please refer to the part headed "Board of directors of CMG" of this section.

Ms. Karen Hong, aged 50, CFO of CMG, mainly responsible for monitoring the financial statements and all financial related activities of the Target Group. She holds a Master of Arts in Economics from the University of Detroit Mercy and a Master of Business Administration from the University of Michigan. In January 2016, she joined Milacron Holdings Corporation as their Global Controller for the DME division. In June 2017, she joined CMG as its CFO with responsibilities for the USA, EU and PRC facilities.

Mr. Stephen Ginger, aged 61, Executive Vice President and General Counsel of CMG, mainly responsible for handling all legal matters of the Target Group. He was awarded a Juris Doctor degree from Southwestern University School of Law and a Bachelor's degree in English from California State University, Dominguez Hills. He was appointed as a Senior Counsel and claims coordinator of CMG in 2003.

Mr. Michael Skolnik, aged 37, Executive Vice President of Global Operations of CMG, mainly responsible for all operations, promotion, facilities, safety and relative activities at any and all CMG factory locations. He was awarded a Master's degree in Mechanical Engineering and a Bachelor's degree in Engineering from Oakland University. In 2007, he joined Teledyne Continental Motors, Inc. as a business unit leader and was appointed as the Manufacturing Engineering Director in 2008. In 2013, he was appointed as the Associate Vice President in Operations of CMI and was promoted to the role of Vice President in 2014. In 2016, he was appointed as the Executive Vice President of Global Operations of CMG.

Mr. Jurgen Schwarz, aged 47, Executive Vice President of Engineering of CMG and Managing Director of TMG, mainly responsible for overseeing the engineering department of the Target Group. He holds a Diploma in Mechanical Engineering from the University of Esslingen. In 1996, he was appointed as a project manager for engine design and later became the Head of Engine Design and

Mechanical Engineering in Mercedes AMG. In 2005, he was appointed as the Head of Product and Process Engineering and later became the Head of Motorsports Sales and Application Engineering in Mahle GmbH. In 2015, he was appointed as the Senior Vice President of Engineering of CMG and became the Managing Director of TMG in 2017.

Save as disclosed above, the above proposed directors and senior management have not held directorship positions in any public companies in the past three years.

Save as disclosed above, none of the above proposed directors and senior management is connected with any other directors, senior management or substantial or controlling shareholders of the Target Group or the Company.

As at the Latest Practicable Date, none of the above proposed directors and senior management has any interest in the shares of the Target Group or the Company within the meaning of Part XV of the SFO.

Save for disclosed above, there is no other information required to be disclosed pursuant to Rule 13.51(2) or Paragraph 41(3) of Appendix 1A of the Listing Rules.

Set out below is the management discussion and analysis on the Target Group for FY2014, FY2015 and FY2016, and 1H2016 and 1H2017.

Results of Operations

The following table sets forth selected items of the consolidated statements of profit or loss for the years/periods indicated:

	For the year ended 31 December			Six months ended 30 June	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000* *(unaudited)*	*US$'000*
Revenue	**161,444**	**163,689**	**204,315**	**101,191**	**99,432**
Cost of sales	(112,110)	(111,907)	(138,883)	(67,980)	(67,955)
Gross profit	**49,334**	**51,782**	**65,432**	**33,211**	**31,477**
Selling expenses	(9,609)	(10,233)	(11,043)	(5,571)	(4,583)
General and administrative expenses	(36,069)	(27,152)	(33,956)	(18,407)	(16,718)
Other operating income/(expenses), net	92	35	(119)	162	87
Finance costs	(8,769)	(8,785)	(10,793)	(5,285)	(5,386)
Share of profit of a joint venture	2	1	14	17	35
Profit/(loss) before tax	**(5,019)**	**5,648**	**9,535**	**4,127**	**4,912**
Income tax credit/(expense)	(2,610)	5,945	(4,163)	(1,363)	(1,308)
Profit/(loss) for the year/period	**(7,629)**	**11,593**	**5,372**	**2,764**	**3,604**

Revenue

The Target Group's revenue was generated from its two business segments: (i) engines and parts business; and (ii) repair and maintenance business. The following table sets forth a breakdown of its business revenue for the years indicated:

	For the year ended 31 December						For the six months ended 30 June			
	2014	% to total revenue	2015	% to total revenue	2016	% to total revenue	2016	% to total revenue	2017	% to total revenue
	US$'000		*US$'000*		*US$'000*		*US$'000* (*unaudited*)		*US$'000*	
Engines and parts business	154,784	*95.87*	150,160	*91.73*	185,074	*90.58*	90,148	*89.09*	93,018	*93.55*
Repair and maintenance business	6,660	*4.13*	13,529	*8.27*	19,241	*9.42*	11,043	*10.91*	6,414	*6.45*
Total revenue	**161,444**	*100.00*	**163,689**	*100.00*	**204,315**	*100.00*	**101,191**	*100.00*	**99,432**	*100.00*

The Target Group's revenue increased by US$2.3 million, or 1.39%, from US$161.4 million for FY2014 to US$163.7 million for FY2015, which was mainly attributable to the impact of acquisitions that gave the Target Group access to adjacent markets [(1)], which was offset by the reduced value in purchases from its top five customers from US$57.4 million for FY2014 to US$51.9 million for FY2015.

The Target Group's revenue then further increased by US$40.6 million, or 24.82%, to US$204.3 million for FY2016, mainly attributable to: (i) the Target Group increasing inventory available in the marketplace; (ii) the acquisitions completed in 2015 that provided access to adjacent markets and further created new growth opportunities; and (iii) the increased sales of UAV (drone) applications using diesel engines.

For 1H2017, the total revenue of the Target Group was US$99.4 million, representing a slight decrease of 1.74% as compared to the corresponding period the previous year. This was mainly caused by a decrease in repair and maintenance service income which was partially offset by an increase in the sale of engines.

The seemingly fluctuating performance of the repair and maintenance business was mainly caused by the acquisitions in 2015, which enlarged the Target Group's range of MRO services and increased its revenue attributable to this sector from US$6.7 million for FY2014 to US$13.5 million for FY2015. The post-acquisition integration of the acquired businesses progressed in FY2016 and furthered adjacent markets for the Target Group and as a result increased this sector's revenue by US$5.7 million year-on-year. However, revenue from repair and maintenance business dropped from US$11.0 million for 1H2016 to US$6.4 million for 1H2017, mainly due to weakened general aviation and oil sector markets that resulted in lower maintenance needs, increased competition, and difficulty in retaining sales talents.

Cost of sales

The Target Group's cost of sales decreased slightly by US$0.2 million, or 0.18%, from US$112.1 million for FY2014 to US$111.9 million for FY2015. The decrease was primarily attributable to cost saving initiatives implemented in factory operations.

The Target Group's cost of sales increased by US$27.0 million, or 24.11%, to US$138.9 million for FY2016 as compared with FY2015, which was in line with the increase in revenue of 24.82% for the same period.

The Target Group's costs of sales decreased by US$25,000, or 0.04%, to US$68.0 million for 1H2017 as compared with 1H2016, mainly due to the decrease in revenue of 1.74% for the same period.

Gross profit and gross profit margin

As a result of the foregoing, the Target Group's gross profit increased slightly by US$2.5 million, or 4.96%, from US$49.3 million for FY2014 to US$51.8 million for FY2015, with a slight improvement in gross profit margin from 30.56% for FY2014 to 31.63% for FY2015.

The Target Group's gross profit then further increased by US$13.6 million, or 26.36%, to US$65.4 million for FY2016 as compared with FY2015, accompanied with a slight increase of gross profit margin from 31.63% for FY2015 to 32.03% for FY2016, which was primarily attributable to UAV sales which contributed to an increase in gross profit. The change in gross profit on a dollar basis is directly attributable to (i) the increased volume of higher margin spare parts sales; and (ii) the higher volume of UAV sales that yielded higher overhead absorption at the TMG operation resulting in FY2016 gross margin of 30.02% comparing to the 23.16% of FY2015; partially offset by the costs associated with the closure of the San Antonio factory which began in the fourth quarter of 2016.

The Target Group's gross profit decreased by US$1.7 million, or 5.22%, to US$31.5 million for 1H2017 as compared with 1H2016. Gross profit margin decreased by 1.1 percentage points for the same period. The slide in gross profit was a consequence of the drop in revenue and the decline of margin due to change of volume and mix.

Selling expenses

	For the year ended 31 December			For the six months ended 30 June	For the six months ended 30 June
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
Warranty expenses	2,234	2,415	4,058	2,023	1,079
Salaries and wages	2,862	2,888	3,003	1,477	1,478
Staff benefits	689	660	485	227	248
Advertising	631	409	872	593	582
Depreciation	97	108	73	51	8
Others	3,096	3,753	2,552	1,200	1,188
Total selling expenses	**9,609**	**10,233**	**11,043**	**5,571**	**4,583**

The Target Group's selling expenses increased by US$0.6 million, or 6.49%, from US$9.6 million for FY2014 to US$10.2 million for FY2015, which was primarily attributable to the impact of additional sales costs acquired with the acquisitions made in 2015.

The Target Group's selling expenses increased by US$0.8 million, or 7.92%, to US$11.0 million for FY2016, which was mainly as a result of costs associated with increased marketing activities to increase the Target Group's visibility in the global market and the increase in warranty expenses due to the significant increase in revenue for the period.

The Target Group's selling expenses decrease by US$1.0 million, or 17.73%, to US$4.6 million for 1H2017. Such decrease was a result of a drop in warranty expenses.

General and administrative expenses

Set out below is a breakdown of general and administrative expenses

	For the year ended 31 December			For the six months ended 30 June	For the six months ended 30 June
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
Salaries and wages	7,072	7,775	8,128	3,602	4,066
Staff benefits	1,819	1,544	915	499	547
Environmental compensation expenses	261	92	174	—	—
Depreciation	700	701	475	274	206
Provision/(reversal of provision) for bad debt	(138)	687	(217)	—	345
Legal and professional fees	1,638	2,132	2,022	1,011	1,140
Others	9,030	10,897	11,675	6,118	6,664
Product liability and other related expenses	10,224	(3,800)	3,982	3,156	696
Intangible assets amortization	1,185	1,691	1,634	867	785
Engineering expenses	4,278	5,433	5,168	2,880	2,269
Total general and administrative expenses	**36,069**	**27,152**	**33,956**	**18,407**	**16,718**

The Target Group's general and administrative expenses decreased by US$8.9 million, or 24.72%, from US$36.1 million for FY2014 to US$27.2 million for FY2015, followed by an increase of US$6.8 million, or 25.06%, to US$34.0 million for FY2016, mainly because of a reduction in the product liability and other related expenses.

For 1H2017, the Target Group's general and administrative expenses decreased by US$1.7 million, or 9.18%, from US$18.4 million for 1H2016 to US$16.7 million for 1H2017, mainly due to reduction in consulting services costs and general insurance costs.

In order to manage expenses and risks relating to aviation product liability, the Target Group maintains a product liability insurance program, which consists of a Self Insured Retention(2) and a layer of coverage by the insurers subject to policy limits. The Target Group maintained a provision to reflect the risk of payments based on the expected outflow of resources to cover the product claims and liabilities and any related costs. In FY2014, FY2015, FY2016 and 1H2017, the Target Group recorded net product liability provision/(reversal of such provision) and other related expenses of US$10.2 million, (US$3.8 million), US$4.0 million and US$0.7 million respectively. These amounts included a net reversal of product liability provision of US$2.3 million, US$14.9 million, US$5.1 million and US$3.5 million in FY2014, FY2015, FY2016 and 1H2017, respectively, mainly as a result of the close, resolution or settlement of certain cases brought forward from previous years. As a result, the Target Group reassessed the provision amounts for outstanding product liability claims at the end of each period during the Track Record Period.

Other operating income/(expenses), net

	For the year ended 31 December			For the six months ended 30 June	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000* (unaudited)	*US$'000*
Distributorship fee income	—	—	75	25	50
Reversal of provisions for deposits	—	619	136	—	—
Gain/(loss) on disposal of items of property, plant and equipment, net	(1)	—	(75)	31	—
Impairment of items of property, plant and equipment	—	—	(306)	—	—
Impairment of goodwill	—	—	(86)	—	—
Exchange gains/(losses), net	(277)	(631)	61	(5)	16
Others	370	47	76	111	21
Total other operating income/(expenses), net	**92**	**35**	**(119)**	**162**	**87**

The Target Group's net other operating income/(expenses), which is largely composed of reversal of provision for deposits, impairment of items of property, plant and equipment, and net exchange gains/(losses), has declined from an income of US$92,000 for FY2014 to US$35,000 for FY2015, and further plunged to expenses of US$119,000 for FY2016.

The impairment of items of property, plant and equipment of US$306,000 for FY2016 was attributable to the provision made by the Target Group's management on certain idle property, plant and equipment in its San Antonio factory. Closure of such factory began in the fourth quarter of 2016.

The impairment of goodwill of US$86,000 for FY2016 was made in relation to the goodwill arising from the acquisition of Southern Avionics and Communications, Inc's business.

The Target Group's net other operating income decreased by US$75,000, from US$162,000 for 1H2016 to US$87,000 for 1H2017.

Finance costs

Both TMI and TMG have been carrying the acquisition financings since they were acquired by AVIC International. Although the primary loan costs have been stable, FY2016 reflected a US$2 million increase in loan costs due to increased interest payments and increased loan guarantee costs.

For the 1H2017, the Target Group's finance costs remained fairly stable, at approximately US$5.4 million, which was higher than that for the same period last year by merely US$0.1 million.

Share of profit of a joint venture

The Target Group's share of profit of a joint venture has remained minimal at US$2,000, US$1,000, US$14,000, US$17,000 and US$35,000 for FY2014, FY2015, FY2016, 1H2016 and 1H2017, respectively.

Income tax credit/(expense)

	For the year ended 31 December			For the six months ended 30 June	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
				(unaudited)	
Current — Elsewhere					
Charge for the year/period	225	359	288	212	217
Underprovision/(overprovision) in prior years	124	—	(225)	(104)	93
Deferred	2,261	(6,304)	4,100	1,255	998
Total tax charge/(credit) for the year/period	2,610	(5,945)	4,163	1,363	1,308

The Target Group recorded an income tax expense of US$2.6 million for FY2014 but enjoyed an income tax credit of US$5.9 million for FY2015. The income tax credit in FY2015 resulted from the income tax expense of US$0.4 million and deferred tax credit of US$6.3 million, which was mainly contributed by the recognition of deferred tax assets during FY2015. If not for this tax credit, the Target Group would show a much more consistent net profit position.

The Target Group recorded an income tax expense of US$1.3 million for 1H2017, a slight decrease of US$0.1 million as compared to the US$1.4 million recorded for 1H2016.

Deferred tax expenses of US$998,000 was recognised for 1H2017 mainly because of the goodwill arising from business combinations of US$1,337,000 and the accelerated depreciation and amortisation for tax purposes of US$765,000, offset by the provisions made amounted to US$609,000 and the capitalisation of inventories of US$435,000.

In FY2016, the Target Group recorded a lower current income tax as compared to FY2015 because of acquisitions made in the FY2015 which lead to a larger deductible amount for amortization of tax deductible goodwill and intangible assets.

The deferred tax expense in FY2014 was mainly resulted from the taxable temporary difference in relation to the goodwill arising from business combinations. In FY2015 and FY2016, the deferred tax movements mainly represented temporary differences arising from provisions, capitalised inventory costs, depreciation of property, plant and equipment and amortisation of intangibles, goodwill arising from business combinations and tax losses.

In FY2015, TMI Group recorded a deferred tax credit of approximately US$6.4 million in profit or loss and other comprehensive income, of which approximately US$9.9 million was deferred tax assets arising from ordinary and usual course of business and approximately US$3.5 million was deferred tax liability arising from acquisitions.

Below is a breakdown of the mentioned deferred tax assets:

		(US$ million)
	Deferred tax asset arising from:	
	Provisions (product liability, warranty, inventories)	5.3
+	Temporary differences relating to capitalised inventory costs	4.9
+	Deferred warranty revenue	1.1
+	Tax losses	5.8
	Deferred tax liability mainly arising from:	
-	Accelerated depreciation and amortisation of PPE, capitalised research and development costs	7.2
	The deferred tax assets	**9.9**

TMI and its subsidiaries ("**TMI Group**") was loss making from the financial years 2011 to 2013 and became profitable in FY2014. As FY2014 was the first profitable year for the TMI Group after the consecutive years of losses, the directors of TMI remained conservative and agreed that deferred tax assets should not be recognised in that year. In FY2015, TMI Group continued to generate profit and its directors were of the view that TMI demonstrated the required trend of continuous profitability and also based on the then profit forecasts, TMI Group would have sufficient profits to fully utilise the deferred tax assets within the period allowed under the relevant tax regulations.

Profit/(loss) for the year

As a result of the foregoing, the Target Group's profit for the year increased by US$19.2 million from a loss of US$7.6 million for FY2014 to US$11.6 million for FY2015. Its net profit margin improved from -4.73% for FY2014 to 7.08% for FY2015.

The Target Group's profit for the year then reduced by US$6.2 million to US$5.4 million for FY2016, and its profit margin dropped to 2.63% for the same period. The main reason for such decrease of profit and profit margin was the change from a tax credit in FY2015 to a tax expense in FY2016. Had the same effective tax rate, i.e. 43.66%, for FY2016 been applied to the profit before tax for FY2015, the profit for FY2015 would have been US$3.2 million with a net profit margin of 1.94%, which is slightly lower than but close to the 2.63% achieved in FY2016.

For 1H2017, the Target Group recorded a profit of US$3.6 million, an increase of US$0.8 million, or 30.39% from US$2.8 million for 1H2016. Its profit margin also improved from 2.7% to 3.6% for the same period.

Consolidated Balance Sheet

The following table sets forth the Target Group's consolidated statements of financial position as at 31 December 2014, 2015 and 2016 and 30 June 2017:

	As at 31 December			**As at 30 June**
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Non-current assets				
Property, plant and equipment	34,343	38,730	34,165	31,789
Goodwill	106,714	109,373	109,153	109,453
Other intangible assets	105,831	111,626	115,185	119,036
Investment in a joint venture	35	36	50	85
Deferred tax assets	—	468	—	—
Prepayment	216	177	142	125
Total non-current assets	**247,139**	**260,410**	**258,695**	**260,488**
Current assets				
Inventories	39,054	46,419	52,001	59,638
Trade and other receivables	12,012	24,700	16,582	17,060
Due from fellow subsidiaries	5,968	3,254	3,734	2,344
Prepayments	5,139	5,071	3,874	2,556
Restricted bank balance	8,083	—	—	—
Cash and cash equivalents	13,191	9,419	14,105	8,460
Total current assets	**83,447**	**88,863**	**90,296**	**90,058**

	As at 31 December			As at 30 June
	2014	2015	2016	2017
	US$'000	*US$'000*	*US$'000*	*US$'000*
Current liabilities				
Trade payables, other payables and accruals	21,013	25,123	22,718	19,795
Interest-bearing loans and borrowings	346	5,959	21,600	21,600
Deferred revenue	184	122	466	143
Provisions and other liabilities	6,558	2,972	4,164	4,109
Due to the immediate holding company	1,176	437	741	1,216
Due to fellow subsidiaries	3,991	23,895	38,670	49,298
Tax payable	152	277	4	78
Total current liabilities	**33,420**	**58,785**	**88,363**	**96,239**
Net current assets/(liabilities)	**50,027**	**30,078**	**1,933**	**(6,181)**
Total assets less current liabilities	**297,166**	**290,488**	**260,628**	**254,307**
Non-current liabilities				
Interest-bearing loans and borrowings	257,568	256,367	222,824	216,128
Deferred revenue	3,020	3,239	4,234	4,321
Provisions and other liabilities	36,940	23,004	15,849	13,112
Defined benefit obligations	751	983	853	558
Due to the immediate holding company	868	2,153	2,318	2,194
Deferred tax liabilities	5,961	—	3,714	4,927
Total non-current liabilities	**305,108**	**285,746**	**249,792**	**241,240**
Net assets/(liabilities)	**(7,942)**	**4,742**	**10,836**	**13,067**
Equity/(Deficiency in assets)				
Share capital	20,000	20,000	20,000	20,000
Reserves	(27,942)	(15,258)	(9,164)	(6,933)
Total equity/(deficiency in assets)	**(7,942)**	**4,742**	**10,836**	**13,067**

Discussion of key balance sheet items

Property, plant and equipment

As at 31 December 2014, 2015 and 2016 and 30 June 2017, property, plant and equipment amounted to US$34.3 million, US$38.7 million, US$34.2 million and US$31.8 million, respectively, representing 10.39%, 11.09%, 9.79% and 9.07% of the Target Group's total assets, respectively.

The Target Group's property, plant and equipment increased from US$34.3 million as at 31 December 2014 to US$38.7 million as at 31 December 2015, mainly because of its business combinations in FY2015.

The Target Group's property, plant and equipment then decreased by US$4.5 million, or 11.79%, to US$34.2 million as at 31 December 2016, primarily due to the depreciation expenses amounted to US$6.0 million.

The Target Group's property, plant and equipment further decreased by US$2.4 million, or 6.95%, to US$31.8 million as at 30 June 2017, mainly caused by the depreciation expenses of US$3.1 million incurred for 1H2017.

Other intangible assets

	Net Book Value			
				As at
	As at 31 December			**30 June**
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Development programs in progress	16,160	7,291	15,328	19,790
Trademarks	20,777	20,269	19,489	19,235
Product technology, licence and completed programs	64,556	77,036	73,783	73,644
Customer relationships	3,946	6,356	5,772	5,480
Others	392	674	813	887
Total	**105,831**	**111,626**	**115,185**	**119,036**

As at 31 December 2014, 2015, 2016 and 30 June 2017, intangible assets amounted to US$105.8 million, US$111.6 million, US$115.2 million and US$119.0 million, respectively, representing 32.01%, 31.96%, 33.01% and 33.96% of the Target Group's total assets, respectively.

The Target Group's intangible assets increased from US$105.8 million as at 31 December 2014 to US$111.6 million as at 31 December 2015, mainly because of its business combinations in FY2015.

The Target Group's intangible assets then further increased by US$3.6 million, or 3.19%, to US$115.2 million as at 31 December 2016, primarily due to the capitalised development costs of US$8.3 million.

The Target Group's intangible assets increased by another US$3.8 million, or 3.34%, to US$119.0 million as at 30 June 2017, mainly resulted from the addition of development costs of US$4.8 million.

Goodwill

As at 31 December 2014, 2015, 2016 and 30 June 2017, goodwill amounted to US$106.7 million, US$109.4 million, US$109.2 million and US$109.5 million, respectively, representing 32.28%, 31.31%, 31.28% and 31.22% of the Target Group's total assets, respectively.

Goodwill increased from US$106.7 million as at 31 December 2014 to US$109.4 million as at 31 December 2015 as a result of its two acquisitions completed during FY2015 [(1)]. It then decreased slightly by US$0.2 million to US$109.2 million as at 31 December 2016 because of impairment and exchange realignment, but later on rebounded to US$109.5 million, as at 30 June 2017 also due to the exchange realignment.

Inventories

Set out below is a breakdown of inventories as at the indicated dates:

	As at 31 December						As at 30 June	
	2014		**2015**		**2016**		**2017**	
	US$'000	*% to total*	*US$'000*	*% to total*	*US$'000*	*% to total*	*US$'000*	*% to total*
Raw materials	25,009	*64.04*	31,902	*68.73*	34,824	*66.97*	42,018	*70.46*
Work in progress	10,949	*28.03*	11,620	*25.03*	13,019	*25.04*	13,944	*23.38*
Finished goods	3,096	*7.93*	2,897	*6.24*	4,158	*7.99*	3,676	*6.16*
Total inventories	**39,054**	*100*	**46,419**	*100*	**52,001**	*100*	**59,638**	*100.00*

As at 31 December 2014, 2015, 2016 and 30 June 2017, inventories amounted to US$39.1 million, US$46.4 million, US$52.0 million and US$59.6 million, respectively, representing 11.81%, 13.29%, 14.90% and 17.01% of the Target Group's total assets, respectively.

The Target Group's inventories increased from US$39.1 million as at 31 December 2014 to US$46.4 million as at 31 December 2015 and further increased by US$5.6 million, or 12.03%, to US$52.0 million as at 31 December 2016, primarily due to the acquisitions completed in 2015.

As at 30 June 2017, the Target Group's inventories went up to US$59.6 million, an increase of US$7.6 million as compared to the level as at 31 December 2016, which was primarily attributable to the Target Group retaining additional inventories as additional safety buffers to reduce inventory lead time.

Inventories turnover days

	For the year ended 31 December			For the six months ended 30 June
	2014	**2015**	**2016**	**2017**
Inventories turnover days	129	139	129	149

The Target Group's average inventory turnover days have always been over 4 months for FY2014, FY2015, FY2016 and 1H2017, which is mainly because of (i) the age of the Target Group's business which has resulted in a large product mix with an extended useful service life that must be supported and (ii) a focus on inventory management practices.

The increase in average inventory turnover days from 129 days in FY2014 to 139 days in FY2015 was mainly a result of the impact of the United Turbine and Danbury AeroSpace acquisitions (1) in 2015 that increased inventory levels.

The average inventory turnover days decreased by 10 days to 129 days in FY2016, which is mainly because of management focus on improving inventory management practices supported by increased volume of sales.

The average inventory turnover days increased by 20 days to 149 days for 1H2017, mainly because of the increase of inventory as at 30 June 2017 as mentioned above.

Trade and other receivables

Set out below is a breakdown of trade and other receivables as at the indicated dates:

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Trade receivables, net	11,136	22,623	14,220	14,988
Other receivables	876	2,077	2,362	2,072
Total	**12,012**	**24,700**	**16,582**	**17,060**

As at 31 December 2014, 2015, 2016 and 30 June 2017, trade and other receivables amounted to US$12.0 million, US$24.7 million, US$16.6 million and US$17.1 million, respectively, representing 3.63%, 7.07%, 4.75% and 4.87% of the Target Group's total assets, respectively.

The Target Group's trade and other receivables increased substantially from US$12.0 million as at 31 December 2014 to US$24.7 million as at 31 December 2015, primarily due to slower collections of receivables from customers.

The Target Group's trade and other receivables then decreased by US$8.1 million, or 32.87%, to US$16.6 million as at 31 December 2016, primarily due to an emphasis by management and finance on maintaining strong collections to terms.

The Target Group's trade and other receivables increased slightly by US$0.5 million, or 2.88%, to US$17.1 million as at 30 June 2017.

Trade receivables turnover days

	For the year ended 31 December			For the six months ended 30 June
	2014	**2015**	**2016**	**2017**
Trade receivables turnover days	24	38	33	27

The Target Group's average trade receivables turnover days increased from 24 days in FY2014 to 38 days in FY2015, which is mainly as a result of an increase in trade receivables; and management focusing on other business activities that resulted in slower collections in general.

The average trade and other receivables turnover days decreased slightly to 33 days in FY2016. The main reason for such decrease was due to management returning attention to good business cash management practices.

The average trade and other receivables turnover days decreased from 33 days for FY2016 to 27 days for 1H2017. Major reasons for this decrease were the improved management on account receivables.

Trade payables, other payables and accruals

The following table sets forth a breakdown of trade payables, other payables and accruals as at the indicated dates:

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Trade payables	5,713	9,788	5,992	8,988
Other payables	1,496	1,280	2,581	1,611
Accruals	13,804	14,055	14,145	9,196
Total	**21,013**	**25,123**	**22,718**	**19,795**

As at 31 December 2014, 2015, 2016 and 30 June 2017, the Target Group's trade payables, other payables and accruals were US$21.0 million, US$25.1 million, US$22.7 million and US$19.8 million, respectively. The increase in trade payables, other payables and accruals as at 31 December 2015 was primarily attributable to an increase in loan interest payments and trade payables from the acquisitions it completed. It subsequently decreased by US$2.4 million to US$22.7 million as at 31 December 2016 which was attributable to reduced trade payables, and further decreased by US$2.9 million to US$19.8 million as at 30 June 2017, mainly because of less purchases resulting from inventory control.

Trade payables turnover days

	For the year ended 31 December			For the six months ended 30 June
	2014	**2015**	**2016**	**2017**
Trade payables turnover days	17	25	21	20

The Target Group's average trade payables turnover days in FY2014, FY2015, FY2016 and 1H2017 was 17 days, 25 days, 21 days and 20 days, respectively, which are within the 60 days credit period granted by the Target Group's suppliers. The change in payables rate reflect the impact of the acquisition of United Turbine and Danbury Aerospace in 2015 [(1)] that resulted in an increase in payable aging while transitioning from the business processes into the Target Group systems. FY2016 and 1H2017 saw a return to more typical payment patterns.

Cash Flows

	For the year ended 31 December			For the six months ended 30 June	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
Net cash flows from operating activities	13,409	4,130	28,818	8,300	5,388
Net cash flows used in investing activities	(11,489)	(36,359)	(10,955)	(4,719)	(4,981)
Net cash from/(used in) financing activities	(5,102)	29,894	(13,064)	(5,463)	(6,186)
Net increase/(decrease) in cash and cash equivalents	**(3,182)**	**(2,335)**	**4,799**	**(1,882)**	**(5,779)**
Cash and cash equivalents at beginning of the year/period	**18,170**	**13,191**	**9,419**	**9,419**	**14,105**
Effect of foreign exchange rate changes, net	(1,797)	(1,437)	(113)	45	134
Cash and cash equivalents at end of year/period	**13,191**	**9,419**	**14,105**	**7,582**	**8,460**

Net cash flows from operating activities

For each of FY2014, FY 2015, FY2016 and 1H2017, the Target Group's cash inflow was principally derived from its sales of engines and parts and provision of repair and maintenance services. Its cash used in operating activities was principally for payments to suppliers and employees, and taxes and professional fees.

For 1H2017, the Target Group had generated a net cash inflow from operating activities of US$5.4 million, which was primarily contributed by profit before tax for the six months of US$4.9 million.

For FY2016, the Target Group had generated a net cash inflow from operating activities of US$28.8 million, which was primarily contributed by profit before tax for the year of US$9.5 million, and decrease in trade and other receivables of US$8.3 million. These cash inflows were partially offset by an increase in inventories of US$5.6 million and a decrease in provisions and other liabilities of US$5.9 million.

For FY2015, the Target Group had generated a net cash inflow from operating activities of US$4.1 million, which was primarily contributed by profit before tax for the year of US$5.6 million. These cash inflows were partially offset by an increase in trade and other receivables of US$9.5 million and a decrease in provisions and other liabilities of US$17.4 million.

For FY2014, the Target Group had generated a net cash inflow from operating activities of US$13.4 million, which was primarily contributed by an increase in trade payables, other payables and accruals of US$7.5 million. These cash inflows were partially offset by a decrease in provisions and other liabilities of US$11.4 million.

Net cash flows used in investing activities

The Target Group's cash outflow from investing activities comprises purchase of property, plant and equipment, additions to other intangible assets and acquisition of businesses.

For 1H2017, the Target Group's net cash used in investing activities was US$5.0 million, mainly attributable to purchase of property, plant and equipment of US$2.1 million and additions to other intangible assets of US$5.0 million, and offset by the cash inflows from disposal of items of property, plant and equipment.

For FY2016, the Target Group's net cash used in investing activities was US$11.0 million, mainly attributable to purchases of property, plant and equipment of US$4.0 million, and additions to other intangible assets of US$8.8 million mainly attributable to the capitalisation of development costs.

For FY2015, the Target Group's net cash used in investing activities was US$36.4 million, mainly attributable to purchases of property, plant and equipment of US$5.7 million, additions to other intangible assets of US$6.7 million, and acquisition of businesses of US$24.1 million.

For FY2014, the Target Group's net cash used in investing activities was US$11.5 million, mainly attributable to purchases of property, plant and equipment of US$4.0 million and additions to other intangible assets of US$6.9 million.

Net cash from/(used in) financing activities

The Target Group's cash flow from/(used in) financing activities comprises mainly new bank loans, repayment of bank loans and interest paid.

For 1H2017, the Target Group's net cash used in financing activities was US$6.2 million, which was primarily due to repayment of bank loans of US$10.8 million and interest paid of US$5.4 million and offset by procurement of a loan from a fellow subsidiary of US$10.0 million.

For FY2016, the Target Group's net cash used in financing activities was US$13.1 million, which was a result of repayment of bank loans of US$17.6 million and interest paid of US$10.8 million and offset by procurement of bank loans and loans from a fellow subsidiary of the Target Group of US$15.8 million.

For FY2015, the Target Group's net cash generated in financing activities was US$29.9 million, which was a result of new bank loans and loans from a fellow subsidiary of the Target Group of US$46.4 million, offset by the repayment of bank loans of US$11.5 million and interest paid of US$8.8 million.

For FY2014, the Target Group's net cash used in financing activities was US$5.1 million, which was a result of interest paid of US$8.8 million, partly offset by a loan from a fellow subsidiary of the Target Group of US$4.0 million.

Note (1): During the Track Record Period, the Target Group completed three acquisitions as set out below.

(i) Southern Avionics and Communications, Inc.

As at 20 November 2014, CMS completed the acquisition of Southern Avionics and Communications, Inc's business for a total consideration of US$850,000. The Target Group settled this acquisition by cash. The reason for acquiring this business was to enlarge the Target Group's range of MRO services that can be offered to its customers.

(ii) United Turbine Corp.

As at 30 January 2015, CMS completed the acquisition of United Turbine Corp's business for a total consideration of US$9,079,000. The acquisition was settled by cash and cash equivalents. The reason for acquiring this business was to enlarge the Target Group's range of MRO services for aircraft engines that can be offered to its customers.

(iii) Danbury AeroSpace, Inc.

As at 19 July 2015, Continental Motors, Inc. (***CMI***) completed the acquisition of Danbury AeroSpace, Inc's business for a total consideration of US$14,991,000. The acquisition was settled by cash and cash equivalents. The reason for acquiring this business was to enlarge the Target Group's range of products that can be offered to its customers.

Note (2): Self Insured Retention is the Target Group's responsibility as first dollar cost of liability capped at a certain maximum liability.

INDEBTEDNESS

Bank borrowings

The table below sets out the Target Group's interest-bearing bank borrowings as at the dates indicated:

	As at 31 December						As at 30 June	
	2014		2015		2016		2017	
	US$'000	*Effective interest rate (%)*	*US$'000*	*Effective interest rate (%)*	*US$'000*	*Effective interest rate (%)*	*US$'000*	*Effective interest rate (%)*
Current								
- Finance lease payables	346	3.65%	359	3.65%	—	—	—	—
- Bank loan - secured	—	—	—	—	20,000	4.22%	20,000	4.44%
- Bank loan - unsecured	—	—	4,000	2.17%	—	—	—	—
- Bank loan - unsecured	—	—	1,600	2.17%	1,600	2.17%	1,600	2.17%
Non-current								
- Finance lease payables	471	3.65%	112	3.65%	—	—	—	—
- Bank loan - secured	200,000	3.41%	200,000	3.49%	170,000	4.22%	160,000	4.44%
- Bank loan - unsecured	—	—	4,933	2.17%	3,333	2.17%	2,533	2.17%
- Bank loan - secured	57,097	1.99%	51,322	1.58%	49,491	1.46%	53,595	1.50%
Total interest - bearing loans and borrowings	**257,914**		**262,326**		**244,424**		**237,728**	

The current secured bank loan of US$20.0 million and the non-current secured bank loan of US$160.0 million were interest-bearing with an interest rate of approximately 4.44% per annum as at 30 June 2017 and is guaranteed by the Target Company's immediate holding company and ultimate holding company.

The current unsecured bank loan of US$1.6 million and non-current unsecured bank loan of approximately US$2.5 million were interest-bearing with an interest rate of approximately 2.17% per annum as at 30 June 2017.

Another non-current secured bank loan of US$53.6 million was interest-bearing with an interest rate of approximately 1.50% per annum as at 30 June 2017 and is secured by an irrevocable letter of guarantee issued by the Bank of China, Beijing.

The Target Group's total loans and borrowings decreased from US$262.3 million as at 31 December 2015 to US$237.7 million as at 30 June 2017, mainly because of the gradual repayment of matured debt obligations.

Except for the non-current secured bank loan of US$53.6 million as mentioned which was denominated in Euro, all borrowings of the Target Group were denominated is USD.

Bank borrowings of the Target Group during the Track Record Period were at floating interest rates.

Due to fellow subsidiaries

The Target Group's amount due to fellow subsidiaries was US$4.0 million, US$23.9 million, US$38.7 million, and US$49.3 million as at 31 December 2014, 2015 and 2016, and 30 June 2017, respectively. Amount due to fellow subsidiaries surged in FY2015 because of its borrowing from CATIC International Finance Limited for the acquisitions made in that year.

Saved as the disclosed above, the Target Group did not have any other borrowings, mortgages, charges, debentures or debt securities, issued or outstanding, and authorised or otherwise created by unissued, or other similar indebtedness, finance lease commitment, liabilities under acceptances, acceptance credits, hire purchase commitments, contingent liabilities or guarantees. In addition, the Target Group currently do not have any external financing plans.

Other than as disclosed in this circular, there had been no material change in the Target Group's indebtedness since 30 June 2017 up to the Latest Practicable Date.

COMMITMENTS AND CONTINGENT LIABILITIES

Capital expenditure

During the Track Record Period, the Target Group's capital expenditure has principally consisted of purchase of building and leasehold land, machinery and equipment, leasehold improvements, and construction in progress and intangible assets other than goodwill. The table below sets out the Target Group's capital expenditure during the period indicated:

	For the year ended 31 December			For the six months ended 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Building and leasehold land	136	170	9	—
Machinery and equipment	924	6,981	2,821	854
Leasehold improvement	109	—	45	—
Construction in progress	3,260	4,444	1,162	1,216
Intangible assets other than goodwill	6,890	11,313	8,803	4,987
Total	**11,319**	**22,908**	**12,840**	**7,057**

OFF-BALANCE SHEET COMMITMENTS AND ARRANGEMENTS

As at the Latest Practicable Date, save for the operating lease commitments tabulated below, the Target Group had not entered into any material off-balance sheet arrangement.

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Within one year	296	1,746	843	722
In the second to fifth years, inclusive	715	1,984	1,230	1,390
After five years	583	3,325	3,032	2,885
	1,594	7,055	5,105	4,997

CONTINGENT LIABILITIES

As at the Latest Practicable Date, there was not any pending or potential material legal proceedings involving the Target Group, or to our Directors' knowledge, threatened against the Target Group which could have a material adverse effect on the Target Group's business or operations. As at the Latest Practicable Date, other than as disclosed in the sub-section headed "Indebtedness" in this section, the Target Group did not have any material contingent liabilities.

REMUNERATION POLICIES

The Target Group employed 667 team members globally as at the Latest Practicable Date, at a total compensation cost of approximately US$22.1 million for 1H2017. CMG, the major holding company of the Target Group, is governed by a board of directors consisting of six directors and has created a compensation committee that includes three of the six directors, namely, Mr. Pan Linwu, Mr. Yu Xiaodong and Mr. Andrew Roberts. The compensation committee has responsibility for reviewing and recommending compensation proposals to the board of directors, including the compensation and bonus plan of executives and team members, compensation budgets and balanced scorecards for calculating bonuses. Further, the board of directors has the responsibility to review and approve or return for further consideration the recommendations of the compensation committee.

Beyond these board level requirements, the Target Group's operations in USA maintains policies and procedures that cover hiring, termination, discipline, compensation, promotion, performance reviews, bonus structures, and other policies necessary for effective operation or mandated by law. These policies are tailored to meet the requirements of the local, state and federal rules of the USA. The Target Group operates a bonus program for all salaried employees in the Target Group. The program is based on measurement against an annually approved balanced scorecard. The policy stipulates that the scorecard is published and tracked. Based on an employee's job classification, they are eligible for a percentage of base pay bonus. The bonus percentage ranges from 2.25% up to 10% excluding executive team members. As part of the annual review, the balanced scorecard is graded from 0 to 100. A score greater than 59 is required to allow a payout. From 60 to 100, the payout varies from a 50% multiplier against the bonus percentage to a 150% multiplier.

The Target Group does not currently have a stock option or other similar stock based incentive program.

The Target Group engaged third party training providers to provide executive development and leadership training to its management team in the past. Other than within its current benefit structure, the Target Group does not have any specific, specialised or contracted training schemes.

KEY FINANCIAL RATIOS

		For the year ended/as at 31 December			For the six months ended/as at 30 June
		2014	2015	2016	2017
Current ratio	*1*	2.5x	1.5x	1.0x	0.9x
Quick ratio	*2*	1.3x	0.7x	0.4x	0.3x
Gearing ratio	*3*	N/A	55.3x	22.6x	18.2x
Net debt to equity ratio	*4*	N/A	53.3x	21.3x	17.5x
Return on equity	*5*	N/A	244.5%	49.6%	N/A
Return on assets	*6*	N/A	3.3%	1.5%	N/A
Interest coverage	*7*	0.4	1.6	1.9	N/A

1. Current ratio is calculated by dividing total current assets by total current liabilities as of the end of the year.

2. Quick ratio is calculated by dividing current assets (net of inventories) by total current liabilities as of the end of the year.

3. Gearing ratio is calculated by dividing bank borrowings by total equity as of the end of the year.

4. Net debt to equity ratio is calculated by dividing net debt by total equity as of the end of the year. Net debt is defined to include total debts (bank borrowing) net of cash and cash equivalents.

5. Return on equity is calculated by dividing profit by total equity as of the end of the year and multiplying the resulting value by 100%.

6. Return on assets is calculated by dividing profit by total assets as of the end of the year and multiplying the resulting value by 100%.

7. Interest coverage is calculated by dividing profit before interest and income tax by finance costs for the year.

Current ratio

The Target Group's current ratio was 2.5x, 1.5x, 1.0x and 0.9x as at 31 December 2014, 2015, 2016 and 30 June 2017, respectively. The fluctuation of the current ratio during the Track Record Period was mainly due to increase in interest-bearing loans and borrowings and due to fellow subsidiaries.

Quick ratio

The Target Group's quick ratio was 1.3x, 0.7x, 0.4x and 0.3x as at 31 December 2014, 2015, 2016 and 30 June 2017, respectively. The fluctuation of the quick ratio during the Track Record Period was mainly due to increase in interest-bearing loans and borrowings and due to fellow subsidiaries.

Gearing ratio

The Target Group's gearing ratio was 55.3x, 22.6x and 18.2x as at 31 December 2015 and 2016 and 30 June 2017, respectively. The decrease of gearing ratio during the Track Record Period was mainly due to increase in net assets which were attributable to improved net profits. Gearing ratio of the Target Group as at 31 December 2014 was not applicable because of its net liabilities position.

Net debt to equity ratio

The Target Group's net debt to equity ratio was 53.3x, 21.3x and 17.5x as at 31 December 2015 and 2016 and 30 June 2017, respectively. The decrease of net debt to equity ratio during the Track Record Period was mainly due to increase in net assets which were attributable to improved net profits. Net debt to equity ratio of the Target Group as at 31 December 2014 was not applicable because of its net liabilities position.

Return on equity

The Target Group's return on equity was 244.5% and 49.6% for FY2015 and FY2016, respectively. The decrease in return on equity was mainly because of the decrease in profit for the year, reason of which has been disclosed above. Return on equity of the Target Group for FY2014 was not applicable because it was loss making and had a net liabilities position.

Return on assets

The Target Group's return on assets was 3.3% and 1.5% for FY2015 and FY2016, respectively. The decrease in return on assets was mainly because of the decrease in profit for the year, reason of which has been disclosed above. Return on assets of the Target Group for FY2014 was not applicable because it was loss making.

Interest coverage

The Target Group's interest coverage was 0.4x, 1.6x and 1.9x for FY2014, FY2015 and FY2016, respectively. The fluctuation of interest coverage during the Track Record Period was mainly due to increase in profit before interest and income tax, reason of which has been disclosed above.

FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Target Group's principal financial instruments comprise cash and bank balances, trade and other receivables, balances with group companies, financial liabilities included in trade payables, other payables and accruals and interest-bearing loans and borrowings. The main purpose of these financial instruments is to provide finance for the Target Group's operations.

The main risks arising from the Target Group's financial instruments are interest rate risk, credit risk and liquidity risk. These risks are managed by the Target Group's financial management policies and practices described below.

Interest rate risk

The Target Group's exposure to interest rate risk relates principally to the Target Group's interest-bearing loans and borrowings from financial institutions. The Target Group mitigates the risk by monitoring closely the movements in interest rates and reviewing its banking facilities regularly.

The sensitivity analysis below has been determined based on the exposure to interest rates for variable-rate bank borrowings at the end of each of the Track Record Period. The analysis is prepared assuming the amount of liability outstanding at the end of each of the Track Record Period was outstanding for the whole year. A 100 basis point increase or decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the reasonably possible change in interest rates.

	Increase/ (decrease) in basis points	**Increase/ (decrease) in profit before tax**	**Increase/ (decrease) in equity***
		US$'000	*US$'000*
As at 31 December 2014			
London Interbank Offered Rate ("LIBOR")	100	(2,000)	—
LIBOR	(100)	2,000	—
Euro Interbank Offer Rate ("EURIBOR")	100	(571)	—
EURIBOR	(100)	571	—
As at 31 December 2015			
LIBOR	100	(2,105)	—
LIBOR	(100)	2,105	—
EURIBOR	100	(513)	—
EURIBOR	(100)	513	—
As at 31 December 2016			
LIBOR	100	(1,949)	—
LIBOR	(100)	1,949	—
EURIBOR	100	(495)	—
EURIBOR	(100)	495	—
As at 30 June 2017			
LIBOR	100	(1,841)	—
LIBOR	(100)	1,841	—
EURIBOR	100	(536)	—
EURIBOR	(100)	536	—

* *Excluding retained profits*

Sensitivity analysis on bank deposits is not presented as the directors of the Target Company consider that the Target Group's exposure to interest rate fluctuations on bank deposits is insignificant.

During the Track Record Period, the Target Group had not entered into any financial instruments for hedging purposes.

Credit risk

The Target Group trades only with recognised and creditworthy third parties. In addition, receivable balances are monitored on an ongoing basis and the Target Group's exposure to bad debts is not significant.

With respect to credit risk arising from the other financial assets of the Target Group, which comprise trade and other receivables, amounts due from group companies and cash and bank balances, the Target Group's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

Since the Target Group trades only with recognised and creditworthy third parties, there is no requirement for collateral. Concentrations of credit risk are managed by customer. As at 31 December 2014, 31 December 2015, 31 December 2016 and 30 June 2017, the Target Group had certain concentrations of credit risk as 11%, 6%, 39% and 39%, respectively, of the Target Group's trade receivables were due from one of the Target Group's key customers.

Liquidity risk

The Target Group monitors its risk to a shortage of funds using a recurring liquidity planning tool. This tool considers the maturity of both its financial instruments and financial assets and projected cash flows from operations.

The Target Group's objective is to maintain a balance between continuity of funding and flexibility through the funding from group companies and bank borrowings.

Treasury policy

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

The Target Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions and the risk characteristics of the underlying assets. The Target Group is not subject to any externally imposed capital requirements. No changes were made in the objectives, policies or processes for managing capital during the Track Record Period.

NO MATERIAL ADVERSE CHANGE

Up to the date of this document, there has been no material adverse change in the Target Group's financial or trading position since 30 June 2017, the end of period reported in the Accountant's Report of the Target Company set out in Appendix III to this circular, and there has been no event since 30 June 2017 which would materially affect the information shown in the Accountant's Report of the Target Company set out in Appendix III to this circular.

I. FINANCIAL SUMMARY

Financial information of the Group for FY2014, FY2015, FY2016, 1H2017 are disclosed in the following documents which have been published on the websites of the HKEX news (www.hkexnews.hk) and the Company (http://www.avic.com.hk):

- the annual report of the Company for FY2014 published 17 April 2015 (pages 45 to 208);

  http://www.hkexnews.hk/listedco/listconews/SEHK/2015/0417/LTN20150417007.pdf

- the annual report of the Company for FY2015 published 8 April 2016 (pages 45 to 200);

  http://www.hkexnews.hk/listedco/listconews/SEHK/2016/0408/LTN20160408654.pdf

- the annual report of the Company for FY2016 published 7 April 2017 (pages 54 to 224); and

  http://www.hkexnews.hk/listedco/listconews/SEHK/2017/0407/LTN201704071006.pdf

- the interim report of the Company for 1H2017 published 13 September 2017 (pages 14 to 46).

  http://www.hkexnews.hk/listedco/listconews/SEHK/2017/0913/LTN20170913155.pdf

The following is a summary of the results and financial information of the Company for FY2014, FY2015, FY2016 and 1H2017, details of which were extracted from the annual reports of the Company for FY2014, FY2015 and FY2016 and the interim report of the Company for 1H2017.

Selected items from the consolidated statement of profit or loss

	FY2014 *(audited)* *HK$'000*	**FY2015**(note A) *(audited)* *HK$'000*	**FY2015**(note B) *(restated)* *HK$'000*	**FY2016** *(audited)* *HK$'000*	**1H2016** *(unaudited)* *HK$'000*	**1H2017** *(unaudited)* *HK$'000*
CONTINUING OPERATIONS						
Revenue	70,856	2,198,590	2,154,988	102,786	64,587	29,740
Cost of sales	(65,033)	(2,015,599)	(1,974,454)	(74,269)	(36,028)	(20,980)
Gross profit	5,823	182,991	180,534	28,517	28,559	8,760
Other income and gains	27,447	35,029	34,550	12,765	9,846	4,570
Profit/(loss) before tax from continuing operations	6,438	191,314	205,573	(742,978)	(342,907)	(64,705)
Income tax credit/ (expense)	(491)	(107,854)	(108,057)	6,685	(5,761)	(2,302)
Profit/(loss) for the year/period from continuing operations	5,947	83,460	97,516	(736,293)	(348,668)	(67,007)
Attributable to:						
Owners of the parent	27,266	41,820	48,989	(715,699)	(350,902)	(57,374)
Non-controlling interests	(21,319)	41,640	48,527	(20,594)	2,234	(9,633)
DISCONTINUED OPERATION						
Profit/(loss) for the year/period from a discontinued operation			(14,056)	27,362	(5,091)	—
Attributable to:						
Owners of the parent			(7,169)	29,857	(2,596)	—
Non-controlling interests			(6,887)	(2,495)	(2,495)	—
Earnings/(loss) per share attributable to ordinary equity holders of the parent						
- Basic and diluted for profit/(loss) from continuing operations	HK0.59 cent	HK0.76 cent	HK0.89 cent	(HK12.97 cents)	(HK6.36 cents)	(HK1.04 cents)

Selected items from the consolidated statement of financial position

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Total assets	8,680,613	6,417,546	5,703,073	5,909,022
Total liabilities	5,318,852	3,085,888	3,176,320	3,376,965
Net assets	3,361,761	3,331,658	2,526,753	2,532,057
Total equity attributable to:				
Shareholders of the Company	2,783,371	2,737,534	1,973,272	1,968,232
Non-controlling interests	578,390	594,124	553,481	563,825
Total equity	3,361,761	3,331,658	2,526,753	2,532,057

Note A: The figures are extracted from the Company's published annual report for FY2015, with the financial performance of 浙江東陽金牛針織製衣有限公司, a non-wholly owned subsidiary of the Company, included in "Continuing operations".

Note B: The figures are extracted from the Company's published annual report for FY2016, with the financial performance of 浙江東陽金牛針織製衣有限公司, a non-wholly owned subsidiary of the Company, included in "Discontinued operation".

No dividend was declared, distributed or paid by the Company for FY2014, FY2015, FY2016 and 1H2017.

The Company has no items which are exceptional or extraordinary because of size, nature or incident for FY2014, FY2015, FY2016 and 1H2017.

Ernst & Young, the auditor of the Company did not issue any qualified opinion on the consolidated financial statements of the Group for FY2014, FY2015 and FY2016.

II. MANAGEMENT DISCUSSION AND ANALYSIS ON THE COMPANY FOR FY2014, FY2015, FY2016, AND 1H2016 AND 1H2017

Below texts are extracted from the Company's annual report for FY2015 and FY2016, and its interim report for 1H2017.

1H2016 and 1H2017

For IH2017, the Group recorded revenue from continuing operations of HK$29,740,000 (1H2016: HK$64,587,000) and loss attributable to owners of the parent of HK$57,374,000 (1H2016: HK$353,498,000). Basic loss per share amounted to HK¢1.04 (1H2016: HK¢6.40). The return on equity, calculated on the basis of profit attributable to owners of the parent as a percentage of equity attributable to owners of the parent, was -3% (1H2016: -15%). The improvement in loss position was mainly attributable to the decrease in the losses of certain investments held by the Group for 1H2017 as compared to the same period in 2016, as well as a one-off gain on disposal of convertible loans recorded.

Business review

Property development and investment business

Currently, two projects are in progress for the property development and investment business. One is located at the Southern side of Zhongshan Road of the Shahekou District of the Dalian City ("Dalian Project"), and another is situated in a newly developed residential area with communal facilities in the Liangjiangxin District of Chongqing ("Chongqing Project").

For 1H2017, the control policies of the Chinese government on the real estate industry continued to vary according to the segments and cities in general. On the one hand, the Chinese government continued to promote destocking in the high-inventory second-tier, third-tier and fourth-tier cities and promote property upgrade among buyers for their own use. On the other hand, the contractionary control measures featuring "purchase restriction, credit restriction, price restriction and sales restriction" were intensively introduced in the first-tier and popular second-tier and third-tier cities. At the same time, to deleverage the financial system, the Chinese government tightened the credit policies on real estate industry by stricter monitoring of banks' credit extension to real estate industry. Affected by this external environment, the trading volume of Dalian Project showed a downward trend. Dalian Project comprises four parcels of land having a total site area of approximately 46,938 square meter (excluding communal site area). A large-scale development project, the International Square, is being constructed comprising offices, retail shops and residential buildings. The total saleable area of Dalian Project upon completion is approximately 350,488 square meter. Dalian Project is currently in the normal development and construction phase, and pre-sale of certain residential and office space of the International Square has commenced since June 2013. Saleable area of 142,311 square meter has been completed as at 30 June 2017, of which 92,175 square meter was sold, 18,299 square meter was available for rent and included in investment properties, and the remaining was included in completed properties held for sale. As at 30 June 2017, the total saleable area of properties under development was approximately 208,177 square meter. Chongqing Project comprises twelve parcels of land with a total site area of approximately 375,252 square meter and is currently in the early development phase. As at 30 June 2017, the properties under development and completed properties held for sale amounted to HK$4,326,947,000 (31 December 2016: HK$4,105,317,000) and investment properties amounted to HK$325,391,000 (31 December 2016: HK$315,866,000). The customer deposits, which represent the proceeds of the pre-sale of properties, amounted to HK$1,367,722,000 (31 December 2016: HK$920,238,000). For 1H2017, the property development and investment business segment recognised revenue and gross profit of HK$29,740,000 (1H2016: HK$64,587,000) and HK$8,760,000 (1H2016: HK$28,559,000), respectively, and recorded loss of HK$46,841,000 (1H2016: profit of HK$2,288,000).

Trading business

The trading business segment recorded no revenue (1H2016: Nil) and no profit or loss (1H2016: Nil) for 1H2017.

Financial review

Assignment of convertible loans

The fully-impaired convertible loans to 上海藍沛新材料科技股份有限公司, an available-for-sale investment, were assigned to an independent third party at a consideration of HK$87,151,000 during 1H2017. As a result, a gain on disposal of convertible loans of HK$87,151,000 (1H2016: Nil) was recognised.

Convertible bonds

The Group held convertible bonds issued by Peace Map Holding Limited ("PMH") and AVIC Joy Holdings (HK) Limited ("AVIC Joy"), respectively, both are listed companies in Hong Kong. These convertible bonds are hybrid instruments that include non-derivative host contracts and the embedded derivatives. The non-derivative host contracts, representing the bond components, have been designated as available-for-sale investments. The embedded derivatives, representing the conversion options, have been designated as derivative financial instruments. The Group's derivative financial instruments are managed and their performance is evaluated on a fair value basis. Any fair value gain or loss is recognised in profit or loss. Fair values are stated based on valuations performed by independent professionally qualified valuers, which are mainly influenced by the prices of the underlying securities and the time value of the derivative financial instruments. The Group's portfolio of derivative financial instruments as at 30 June 2017 consisted of the derivatives at fair values of HK$68,000 (31 December 2016: HK$9,277,000) and HK$184,000 (31 December 2016: HK$2,061,000) embedded in the convertible bonds issued by PMH and AVIC Joy, respectively. During 1H2017, a fair value loss on derivative financial instruments of HK$11,086,000 (1H2016: HK$72,027,000) was recognised in respect of the derivatives embedded in the convertible bonds issued to PMH and AVIC Joy, which was mainly due to the drop in the share prices of both companies.

Equity investment at fair value through profit or loss

The Group held shares issued by PMH and classified the investment as an equity investment at fair value through profit or loss. During 1H2017, the Group recorded a fair value loss on equity investment at fair value through profit or loss of HK$25,905,000 (1H2016: HK$137,904,000) due to the drop in the share price of PMH.

Impairment of an available-for-sale investment

The Group held shares issued by AVIC Joy and classified the investment as an available-for-sale investment. Due to the significant decline in the share price of AVIC Joy during 1H2017, an impairment of an available-for-sale investment of HK$48,485,000 (1H2016: HK$94,907,000) was recorded.

Joint venture and associates

During 1H2017, the Group recorded share of losses of the joint venture and associates in an aggregate of HK$11,047,000 (1H2016: HK$45,855,000).

Liquidity, capital structure and financial resources

The Group has consistently maintained sufficient working capital. As at 30 June 2017, the Group had current assets of HK$5,294,512,000 (31 December 2016: HK$4,969,966,000), including cash and bank balances and time deposits in an aggregate of HK$670,377,000 (31 December 2016: HK$605,925,000). The Group's current liabilities as at 30 June 2017 were HK$2,211,905,000 (31 December 2016: HK$1,692,802,000).

As at 30 June 2017, the Group's equity attributable to owners of the parent amounted to HK$1,968,232,000 (31 December 2016: HK$1,973,272,000), comprising issued capital of HK$551,959,000 (31 December 2016: HK$551,959,000) and reserves of HK$1,416,273,000 (31 December 2016: HK$1,421,313,000). The Group's interest-bearing debts, including loans from a fellow subsidiary of HK$1,162,523,000 (31 December 2016: HK$1,234,637,000), loans from an intermediate holding company of HK$489,756,000 (31 December 2016: HK$475,419,000) and interest-bearing bank borrowings of Nil (31 December 2016: HK$230,134,000) are mainly denominated in Renminbi and arranged on a fixed rate basis. The Group's gearing ratio, calculated on the basis of the interest bearing debts as a percentage of equity attributable to owners of the parent plus the interest-bearing debts, was 46% (31 December 2016: 50%). The Group's banking facilities are mainly utilised for general working capital requirements.

Treasury policy

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

The Group manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. The Group is not subject to any externally imposed capital requirements. Except for the composition of debt in the calculation of the gearing ratio, no changes were made in the objectives, policies or processes for managing capital during the Track Record Period.

Exposure to interest rate risk

During the Track Record Period, the Group has no significant interest rate risk because the Group's interest-bearing debts, including loans from fellow subsidiaries and an intermediate holding company and interest-bearing bank borrowings, are arranged on a fixed rate basis. During the Track Record Period, the Group has not used any financial instruments to hedge its exposure to interest-rate risk.

Exposure to foreign currency risk

The Group's foreign currency exposures primarily arise from certain sales or purchases by operating units in currencies other than the unit's functional currency. In view of the fact that the Group tries to match its assets and liabilities with the same currency, the Group's exposure to foreign currency risk is minimal.

Material acquisitions and disposals

Save for the transactions described elsewhere in the Company's published interim report for 1H2017, the Group had no other material acquisitions or disposals during 1H2017. As set out in the Company's announcement dated 7 September 2016, the Company is considering a series of business and asset reorganisation proposals which include the acquisition of certain assets and the disposal of the Group's real estate development business in China.

Contingent liabilities

Details of the significant contingent liabilities of the Group can be found in note 14 to the interim report of the Company for 1H2017.

Employees and remuneration policy

As at 30 June 2017, there were 66 (31 December 2016: 73) employees in the Group. The employee wages and salaries, excluding directors' remuneration, amounted to HK$14,376,000 (1H2016: HK$13,135,000) for 1H2017. The Group recognises the importance of good relationship with employees. The Directors believe that the working environment and benefits offered to employees have contributed to building good staff relations and retention. The Group's remuneration policies are formulated based on the performance of individual employees and market conditions and are reviewed regularly. The Group also provides other staff benefits including medical and life insurance, and grants discretionary incentive bonuses and share options to eligible staff based on their performance and contributions to the Group.

FY2016

Overall review

During FY2016, the Group disposed of 浙江東陽金牛針織製衣有限公司 ("Zhejiang Dongyang Jinniu"), a 51%-owned subsidiary, to an independent third party at a cash consideration of

HK$5,650,000. Zhejiang Dongyang Jinniu engaged in the production and distribution of knitting and textile products, knitted fabrics and clothing. The Group decided to dispose of this subsidiary and cease its knitting and textile business because it had been loss-making in recent years. For FY2016, the revenue of this discontinued operation amounted to HK$18,616,000 (FY2015: HK$43,602,000). Together with the gain on disposal of a subsidiary of HK$32,453,000 (FY2015: Nil) recorded, the profit from this discontinued operation was HK$27,362,000 (FY2015: loss of HK$14,056,000).

For FY2016, the Group recorded revenue and gross profit from continuing operations of HK$102,786,000 (FY2015: HK$2,154,988,000) and HK$28,517,000 (FY2015: HK$180,534,000), respectively, which were contributed mainly by the property development and investment business. The Group recorded loss for the year from continuing operations of HK$736,293,000 (FY2015: profit of HK$97,516,000), which arose mainly from the fair value losses on an equity investment at fair value through profit or loss and derivative financial instruments in an aggregate of HK$306,652,000 (FY2015: gain of HK$26,942,000), as well as the share of losses of the joint venture and associates in an aggregate of HK$218,382,000 (FY2015: HK$68,615,000) and the impairment of an available-for-sale investment of HK$134,107,000 (FY2015: HK$311,137,000). Loss attributable to owners of the parent was HK$685,842,000 (FY2015: profit of HK$41,820,000) and basic loss per share was HK¢12.43 (FY2015: basic earnings per share of HK¢0.76). The return on equity, calculated on the basis of profit attributable to owners of the parent as a percentage of equity attributable to owners of the parent, was -35% (FY2015: 2%).

Business review

Property development and investment business

Currently, two projects are in progress for the property development and investment business. One is located at the Southern side of Zhongshan Road of the Shahekou District of the Dalian City (“Dalian Project”), and another is situated in a newly developed residential area with communal facilities in the Liangjiangxin District of Chongqing (“Chongqing Project”). In 2016, influenced by the policies of the Chinese government and the domestic monetary environment, the “930 New Policy” set a demarcation line in the real estate market between a booming one and a cooling one. Before the implementation of the new policy, driven jointly by the supply-side structural reform and the easing monetary environment, the demand in first-tier and some second-tier cities was steadily released, thereby leading to significant de-stocking results. However, due to the serious regional differentiation, no apparent increase in price and volume was observed in the market of Dalian City where Dalian Project is located. Upon adoption of the “930 New Policy”, capital flows of financial institutions were subject to strict policy control, causing capital liquidity to become tightened. In several cities, a series of macro-economic control measures were introduced in succession and restrictions on property purchases and mortgage loans were re-launched. Affected by this external environment, the trading volume in Dalian and Chongqing showed a downward trend.

Dalian Project comprises four parcels of land having a total site area of approximately 46,938 square meter (excluding communal site area). A large-scale development project, the International Square, is being constructed comprising offices, retail shops and residential buildings. The total saleable area of Dalian Project upon completion is approximately 350,488 square meter. Dalian Project is currently in the normal development and construction phase, and pre-sale of certain residential and office space of the International Square has commenced since June 2013. Saleable area of 142,311 square meter has been completed as at 31 December 2016, of which 90,649 square meter was sold, 18,299 square meter was leased out and included in investment properties, and the remaining was included in completed properties held for sale. As at 31 December 2016, the total saleable area of properties under development was approximately 208,177 square meter. Chongqing Project comprises twelve parcels of land with a total site area of approximately 375,252 square meter and is currently in the early development phase. As at 31 December 2016, the properties under development and completed properties held for sale amounted to HK$4,105,317,000 (31 December 2015: HK$4,070,648,000) and investment properties amounted to HK$315,866,000 (31 December 2015: HK$373,425,000). The customer deposits, which represent the proceeds of the pre-sale of properties, amounted to HK$920,238,000 (31 December 2015: HK$248,310,000). Dalian Project recorded revenue of HK$102,786,000 (31 December 2015: HK$2,147,344,000) and gross profit of HK$28,517,000 (31 December 2015: HK$180,303,000) for the year. In 2016, enhanced de-stocking efforts remained prevailing in the market of Dalian City where Dalian Project is located. Under the circumstances, the Group controlled the property development progress in a moderate manner by reasonably allocating sales of completed properties and properties under development to capture the market share. Therefore, revenue for the year decreased as compared to last year. The property development and investment business segment recorded loss of HK$47,058,000 (FY2015: profit of HK$35,065,000) for FY2016.

Trading business

The trading business segment recorded no revenue (FY2015: HK$7,644,000) and no profit or loss (FY2015: profit of HK$175,000) for FY2016.

Financial review

Convertible bonds

The Group held convertible bonds issued by Peace Map Holding Limited ("PMH") and AVIC Joy Holdings (HK) Limited ("AVIC Joy"), respectively, both are listed companies in Hong Kong. These convertible bonds are hybrid instruments that include non-derivative host contracts and the embedded derivatives. The non-derivative host contracts, representing the bond components, have been designated as available-for-sale investments. The embedded derivatives, representing the conversion options, have been designated as derivative financial instruments. The Group's derivative financial instruments are managed and their performance is evaluated on a fair value basis. Any fair value gain or loss is recognised in profit or loss. Fair values are stated based on valuations performed by independent professionally qualified valuers, which are mainly influenced by the prices of the underlying securities and the time value of the derivative financial instruments. The Group's portfolio of derivative financial instruments as at 31 December 2016 consisted of the derivatives at fair values of HK$9,277,000 (31 December 2015: HK$90,444,000) and HK$2,061,000 (31 December 2015: HK$29,452,000) embedded in the convertible bonds issued by PMH and AVIC Joy, respectively. During FY2016, a fair value loss of HK$108,558,000 (FY2015: gain of HK$28,146,000) was recognised in respect of the embedded derivatives, which was mainly due to the drop in the share prices of both PMH and AVIC Joy.

Equity investment at fair value through profit or loss

The Group held shares issued by PMH and classified the investment as an equity investment at fair value through profit or loss. During FY2016, the Group recorded a fair value loss on an equity investment at fair value through profit or loss of HK$198,094,000 (FY2015: HK$1,204,000) due to the drop in the share price of PMH.

Impairment of an available-for-sale investment

The Group held shares issued by AVIC Joy and classified the investment as an available-for-sale investment. Due to the significant decline in the share price of AVIC Joy during FY2016, an impairment of an available-for-sale investment of HK$134,107,000 (FY2015: HK$311,137,000) was recorded.

Joint venture and associates

During FY2016, the Group recorded share of losses of the joint venture and associates in an aggregate of HK$218,382,000 (FY2015: HK$68,615,000) mainly because the joint venture made significant impairment provisions on its certain investments and other assets.

Liquidity, capital structure and financial resources

The Group has consistently maintained sufficient working capital. As at 31 December 2016, the Group had current assets of HK$4,969,966,000 (31 December 2015: HK$5,127,503,000), including cash and bank balances and time deposits in an aggregate of HK$605,925,000 (31 December 2015: HK$473,689,000). The Group's current liabilities as at 31 December 2016 were HK$1,692,802,000 (31 December 2015: HK$763,972,000). As at 31 December 2016, the Group's equity attributable to owners of the parent amounted to HK$1,973,272,000 (31 December 2015: HK$2,737,534,000), comprising issued capital of HK$551,959,000 (31 December 2015: HK$551,959,000) and reserves of HK$1,421,313,000 (31 December 2015: HK$2,185,575,000). The Group's interest-bearing debts, including loans from fellow subsidiaries of HK$1,234,637,000 (31 December 2015: HK$1,864,671,000), interest-bearing bank borrowings of HK$230,134,000 (31 December 2015: HK$37,964,000) and loans from an intermediate holding company of HK$475,419,000 (31 December 2015: HK$509,581,000) are mainly denominated in Renminbi and arranged on a fixed rate basis. The Group's gearing ratio, calculated on the basis of the interest-bearing debts as a percentage of equity attributable to owners of the parent plus the interest-bearing debts, was 50% (31 December 2015: 47%). The Group's banking facilities are mainly utilised for general working capital requirements.

Charges on the Group's assets

Details of the charges on the Group's assets are set out in notes 35(a) and 35(b) to the Company's published annual report for FY2016.

Exposure to foreign currency risk

The Group's foreign currency exposures primarily arise from certain sales or purchases by operating units in currencies other than the units' functional currency. In view of the fact that the Group tries to match its assets and liabilities with the same currency, the Group's exposure to foreign currency risk is minimal.

Material acquisitions and disposals

Save for the transactions described elsewhere in the Company's published annual report for FY2016, the Group had no other material acquisitions or disposals during FY2016.

Contingent liabilities

Details of the significant contingent liabilities of the Group are set out in note 44 to the annual report of the Company for FY2016.

Environmental and regulatory compliance

Environmental protection and the effective use of natural resources have gradually become an important concept in modern economic growth. The Company follows the major trends in environmental protection around the world. Our operations are also in an effort to increasingly integrate this concept. Based on new technology and management approach, the Company strictly controls its environmental impact and resource usage, in an effort to forge cleaner production featuring lower pollution and lower emissions toward sustainable development. The Company strictly follows all applicable laws and regulations released by the relevant authorities which are material to the Company. Throughout the year 2016, there was no incidence of non-compliance with the relevant laws and regulations that have a significant impact on the Company.

Employees and remuneration policy

As at 31 December 2016, there were 73 (31 December 2015: 156) employees in the Group. The employee wages and salaries for the continuing operations, excluding directors' remuneration, amounted to HK$28,586,000 (FY2015: HK$22,179,000) for FY2016. The Group recognises the importance of good relationship with employees. The Directors believe that the working environment and benefits offered to employees have contributed to building good staff relations and retention. The Group's remuneration policies are formulated based on the performance of individual employees and market conditions and are reviewed regularly. The Group also provides other staff benefits including medical and life insurance, and grants discretionary incentive bonuses and share options to eligible staff based on their performance and contributions to the Group.

FY2015 and FY2014

Overall review

For FY2015, the Group recorded turnover of HK$2,198,590,000 (FY2014: HK$70,856,000) and gross profit of HK$182,991,000 (FY2014: HK$5,823,000). The substantial rise in turnover and gross profit was because the property development and investment business segment started to sell and lease out properties during the year and thus turnover was recorded. The Group also recorded a one-off net gain on deemed disposal of associates of HK$433,380,000 (FY2014: HK$679,000). Nevertheless, a provision for impairment of an available-for-sale investment of HK$311,137,000 (FY2014: Nil) was made due to the significant fall in stock market. During FY2015, the profit before tax was HK$191,314,000 (FY2014: HK$6,438,000). After deducting income tax expense, the profit for the year was HK$83,460,000 (FY2014: HK$5,947,000) of which the profit attributable to owners of the parent was HK$41,820,000 (FY2014: HK$27,266,000). Basic earnings per share amounted to HK¢0.76 (FY2014: HK¢0.59). The return on equity, calculated on the basis of profit attributable to owners of the parent as a percentage of equity attributable to owners of the parent, was 2% (FY2014: 1%).

Business review

Property development and investment business

During FY2015, the property development and investment business acquired by the Group on 30 December 2014 became one of the Group's principal activities. Currently, two projects are in progress. One is located at the Southern side of Zhongshan Road of the Shahekou District of Dalian City ("Dalian Project"), and another is situated in a newly developed residential area with communal facilities in the Liangjiangxin District of Chongqing ("Chongqing Project"). In 2015, the overall keynote of the regulation and control policy of the Chinese government for the real estate industry insisted on promoting consumption and destocking, with frequent launch of supply and demand easing policies to push ahead with the steady rally of market volumes and prices. Despite the steady release of demand volume in the second- and third-tier cities as stimulated by such policies, the impetus was inadequate to push up the house prices due to the high inventory of real estate. Remarkably increasing prices and volumes have not yet turned up in the market of Dalian City where the Dalian Project is located. Dalian Project comprises four parcels of land having a total site area of approximately 46,938 square meter (excluding communal site area). A large scale development project, the International Square, is being constructed comprising offices, retail shops and residential buildings. The total saleable area of Dalian Project upon completion is approximately 350,488 square meter. Dalian Project is currently in the normal development and construction phase, and pre-sale of certain residential and office space of the International Square has commenced since June 2013. Saleable area of 142,311 square meter was completed in 2015, of which 86,960 square meter was sold, 18,299 square meter was leased out and included in investment properties, and the remaining was included in completed properties held for sale. As at 31 December 2015, the total saleable area of properties under development was approximately 208,177 square meter.

Chongqing Project comprises twelve parcels of land with a total site area of approximately 375,252 square meter and is currently in the early development phase. As at 31 December 2015, the properties under development and completed properties held for sale amounted to HK$4,070,648,000 (31 December 2014: HK$4,950,000,000) and investment properties amounted to HK$373,425,000 (31 December 2014: Nil). The customer deposits, which represent the proceeds of the pre-sale of properties, decreased from HK$1,757,152,000 as at 31 December 2014 to HK$248,310,000 as at 31 December 2015, because sales was recognised after the completion of properties during the year. Dalian Project recorded turnover of HK$2,147,344,000 and gross profit of HK$180,303,000 for FY2015. The property development and investment business segment contributed profit of HK$35,065,000 for FY2015.

Knitting and textile business

For FY2015, the operating condition of 浙江東陽金牛針織製衣有限公司 (“Zhejiang Dongyang Jinniu”), a 51%-owned subsidiary, was unfavourable. It was mainly attributable to the weak condition of the knitting and textile industry as a result of the influence of macro economy. Its turnover was HK$43,602,000, a drop of 18% from HK$53,413,000 for FY2014. The sales volume was approximately 2,571 tonnes (FY2014: 2,784 tonnes). The gross profit rate was 6% (FY2014: 10%). A provision for impairment of items of property, plant and equipment of HK$6,924,000 (FY2014: Nil) was made due to a reduced future cash inflow estimated. Moreover, a provision for impairment of trade and bills receivables of HK$6,871,000 (FY2014: HK$4,371,000) was made. The knitting and textile business segment recorded loss of HK$14,056,000 (FY2014: HK$43,509,000) for the year.

Trading business

During FY2015, the Group continued to engage in the trading of raw materials and auxiliary materials such as electronic components, electronic products and metal materials in Zhejiang Province. The turnover and gross profit rate for FY2015 was HK$7,644,000 (FY2014: HK$17,443,000) and 3% (FY2014: 2%) respectively. The trading business segment recorded profit of HK$175,000 (FY2014: HK$2,987,000) for FY2015.

Financial review

Joint venture and associates

During FY2015, the Group’s equity interests in two associates, AVIC Joy Holdings (HK) Limited (“AVIC Joy”), a listed company in Hong Kong, and 上海藍沛新材料科技股份有限公司 (“上海藍沛”), were diluted and the Group no longer had significant influence over them. As such, the Group’s investments in these two companies were reclassified from investments in associates to available-for-sale investments, and the Group discontinued to apply the equity method to share the results and other comprehensive income of these two companies. This reclassification was accounted for as disposals of the entire interests in AVIC Joy and 上海藍沛, and re-acquisitions of the retained interests at their fair values. As a result, a net gain on deemed disposal of associates of HK$433,380,000 (FY2014: Nil) was recorded. In addition, the Group recorded share of losses of the joint venture and associates in an aggregate of HK$68,615,000 (FY2014: HK$50,204,000) for FY2015.

Impairment of an available-for-sale investment

Subsequent to the Group's investment in AVIC Joy being reclassified from investment in an associate to an available-for-sale investment during the year, there was a significant fall in the stock market in Hong Kong. As a result, an impairment of an available-for-sale investment of HK$311,137,000 (FY2014: Nil) was recorded for FY2015.

Convertible bonds

The Group held convertible bonds issued by Peace Map Holding Limited ("PMH") and AVIC Joy, respectively, both are listed companies in Hong Kong. These convertible bonds are hybrid instruments that include non-derivative host contracts and the embedded derivatives. The non-derivative host contracts, representing the bond components, have been designated as available-for-sale investments. The embedded derivatives, representing the conversion options, have been designated as derivative financial instruments. During FY2015, the Group converted certain convertible bonds issued by PMH ("PMH Convertible Bonds") with a principal amount of HK$66,000,000 into 264,000,000 shares of PMH at the conversion price of HK$0.25 per share. The number of shares of PMH held by the Group increased from 497,900,000 shares as at 31 December 2014 to 761,900,000 shares as at 31 December 2015, which was included in equity investment at fair value through profit or loss. A loss on derecognition of HK$3,760,000 was calculated which was the difference between the fair value of the shares of PMH received and that of PMH Convertible Bonds converted. At the same time, the corresponding fair value gain of HK$8,573,000 previously recorded in the statement of other comprehensive income was released from the available-for-sale investment revaluation reserve. As a result, a net gain on derecognition of an available-for-sale investment of HK$4,813,000 in respect of PMH Convertible Bonds was recorded in the consolidated statement of profit or loss for FY2015.

Furthermore, during FY2015, the maturity date of the convertible bond issued by AVIC Joy ("AVIC Joy Convertible Bond") was extended from 6 March 2015 to 6 March 2018 as agreed by the Group and AVIC Joy, and the conversion rate was changed from HK$0.235 per share to HK$0.23 per share. A gain on derecognition of the original AVIC Joy Convertible Bond of HK$3,984,000 was calculated which was the difference between the fair values of the original and the new AVIC Joy Convertible Bonds. At the same time, the corresponding fair value gain of HK$10,518,000 previously recorded in the statement of other comprehensive income was released from the available-for-sale investment revaluation reserve. As a result, a net gain on derecognition of an available-for-sale investment of HK$14,502,000 in respect of AVIC Joy Convertible Bond was recorded in the consolidated statement of profit or loss for FY2015. The Group's derivative financial instruments are managed and their performance is evaluated on a fair value basis. Any fair value gain or loss is recognised in profit or loss. Fair values are stated based on valuations performed by independent professionally qualified valuers, which are mainly influenced by the prices of the underlying securities and the time value of the derivative financial instruments. The Group's portfolio of derivative financial instruments as at 31 December 2015 consisted of the derivatives at fair values of HK$90,444,000 (31 December 2014: HK$125,373,000) and HK$29,452,000 (31 December 2014: HK$25,497,000) embedded in PMH Convertible Bonds and AVIC Joy Convertible Bond, respectively. During FY2015, a fair value gain of HK$28,146,000 (FY2014: loss of HK$8,565,000) was recognised in respect of the embedded derivatives, which was mainly due to the rise in the share price of PMH.

Liquidity, capital structure and financial resource

The Group has consistently maintained sufficient working capital. As at 31 December 2015, the Group had current assets of HK$5,127,503,000 (31 December 2014: HK$7,810,267,000), including cash and bank balances and time deposits in an aggregate of HK$473,689,000 (31 December 2014: HK$1,249,324,000). The Group's current liabilities as at 31 December 2015 were HK$763,972,000 (31 December 2014: HK$4,176,488,000). As at 31 December 2015, the Group's equity attributable to owners of the parent amounted to HK$2,737,534,000 (31 December 2014: HK$2,783,371,000), comprising issued capital of HK$551,959,000 (31 December 2014: HK$551,959,000) and reserves of HK$2,185,575,000 (31 December 2014: HK$2,231,412,000). The Group's interest-bearing debts, including loans from fellow subsidiaries of HK$1,864,671,000 (31 December 2014: HK2,361,837,000), interest-bearing bank borrowings of HK$37,964,000 (31 December 2014: HK$704,686,000) and loans from an intermediate holding company of HK$509,581,000 (31 December 2014: Nil) are mainly denominated in Renminbi and arranged on a fixed rate basis. The Group's gearing ratio, calculated on the basis of the interest-bearing debts as a percentage of equity attributable to owners of the parent plus the interest-bearing debts, was 47% (31 December 2014: 52%). The Group's banking facilities are mainly utilised for general working capital requirements.

Charges on the Group's assets

Details of the charges on the Group's assets are set out in note 34(a) to the Company's published annual report for FY2015.

Exposure to foreign currency risk

The Group's foreign currency exposures primarily arise from certain sales or purchases by operating units in currencies other than the units' functional currency. In view of the fact that the Group tries to match its assets and liabilities with the same currency, the Group's exposure to foreign currency risk is minimal.

Material acquisitions and disposals

Save for the transactions described elsewhere in the Company's published annual report for FY2015, the Group had no other material acquisitions or disposals during FY2015.

Contingent liabilities

Details of the significant contingent liabilities of the Group are set out in note 43 to the Company's published annual report for FY2015.

Employees and remuneration policy

As at 31 December 2015, there were 156 (31 December 2014: 179) employees in the Group. The employee wages and salaries, excluding directors' remuneration, amounted to HK$30,269,000 (FY2014: HK$17,096,000) for FY2015. The Group recognises the importance of good relationship with employees. The Directors believe that the working environment and benefits offered to employees have contributed to building good staff relations and retention. The Group's remuneration policies are formulated based on the performance of individual employees and market conditions and are reviewed regularly. The Group also provides other staff benefits including medical and life insurance, and grants discretionary incentive bonuses and share options to eligible staff based on their performance and contributions to the Group.

III. AUDITED FINANCIAL STATEMENTS FOR FY2016

The following information is extracted from the audited financial statements of the Group as set out in the annual report of the Company for FY2016.

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

Year ended 31 December 2016

	Notes	2016 HK$'000	2015 HK$'000 (Restated)
CONTINUING OPERATIONS			
REVENUE	5	102,786	2,154,988
Cost of sales		(74,269)	(1,974,454)
Gross profit		28,517	180,534
Other income and gains	5	12,765	34,550
Selling and distribution expenses		(31,694)	(22,998)
Administrative expenses		(41,611)	(54,059)
Other operating income/(expenses), net	6	(54,633)	15,299
Finance costs	7	(77)	(47,638)
Net gain on deemed disposal of associates	18	3,386	433,380
Share of profits and losses of:			
Joint venture		(215,369)	(27,278)
Associates		(3,013)	(41,337)
Impairment of an available-for-sale investment (transfer from available-for-sale investment revaluation reserve)	20(d)	(134,107)	(311,137)
Gain on derecognition of available-for-sale investments	20(a), (b)	—	224
Fair value gain/(loss) of available-for-sale investments (transfer from equity on derecognition)	20(a), (b), (c)	(490)	19,091
Fair value gain/(loss) on derivative financial instruments, net	21	(108,558)	28,146
Fair value loss on an equity investment at fair value through profit or loss		(198,094)	(1,204)
PROFIT/(LOSS) BEFORE TAX FROM CONTINUING OPERATIONS	6	(742,978)	205,573
Income tax credit/(expense)	10	6,685	(108,057)

	Notes	2016 HK$'000	2015 HK$'000 (Restated)
PROFIT/(LOSS) FOR THE YEAR FROM CONTINUING OPERATIONS		(736,293)	97,516
DISCONTINUED OPERATION			
Profit/(loss) for the year from a discontinued operation	11	27,362	(14,056)
PROFIT/(LOSS) FOR THE YEAR		(708,931)	83,460
Attributable to:			
Owners of the parent		(685,842)	41,820
Non-controlling interests		(23,089)	41,640
		(708,931)	83,460
EARNINGS/(LOSS) PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT	12		
Basic and diluted			
– For profit/(loss) for the year		(HK12.43 cents)	HK0.76 cent
– For profit/(loss) from continuing operations		(HK12.97 cents)	HK0.89 cent

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December 2016

	Notes	2016 HK$'000	2015 HK$'000
PROFIT/(LOSS) FOR THE YEAR		(708,931)	83,460
OTHER COMPREHENSIVE INCOME			
Other comprehensive income to be reclassified to profit or loss in subsequent periods:			
Available-for-sale investments:			
Changes in fair value	20	(119,876)	(307,190)
Reclassification adjustments for losses/(gains) included in the consolidated statement of profit or loss			
– Loss/(gain) on derecognition	20	490	(19,091)
– Impairment loss	20	134,107	311,137
		14,721	(15,144)
Exchange differences:			
Exchange differences on translation of foreign operations		(125,145)	(76,206)
Reclassification adjustment for a foreign operation disposed of during the year	41	(1,223)	—
		(126,368)	(76,206)
Share of other comprehensive income of a joint venture		(8,905)	—
Share of other comprehensive income of associates		—	16,028
Release of share of an associate's other comprehensive income upon deemed disposal of the associate		—	(38,241)
NET OTHER COMPREHENSIVE INCOME TO BE RECLASSIFIED TO PROFIT OR LOSS IN SUBSEQUENT PERIODS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR, NET OF TAX		(120,552)	(113,563)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		(829,483)	(30,103)
Attributable to:			
Owners of the parent		(764,262)	(45,837)
Non-controlling interests		(65,221)	15,734
		(829,483)	(30,103)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

31 December 2016

	Notes	2016 HK$'000	2015 HK$'000
NON-CURRENT ASSETS			
Property, plant and equipment	13	24,975	31,595
Investment properties	14	315,866	373,425
Prepaid land lease payments	15	—	2,814
Intangible asset	16	—	380
Investment in a joint venture	17	58,602	290,621
Investments in associates	18	13,378	24,146
Financial asset under Project EC120	19	—	—
Available-for-sale investments	20	278,745	400,421
Derivative financial instruments	21	11,338	119,896
Trade receivable	24	20,178	21,628
Due from a fellow subsidiary	32	—	3,178
Loan to a related company	25	—	11,976
Prepayments	26	—	278
Deferred tax assets	36	10,025	9,685
Total non-current assets		733,107	1,290,043
CURRENT ASSETS			
Properties under development and completed properties held for sale	22	4,105,317	4,070,648
Inventories	23	—	4,564
Trade and bills receivables	24	69,442	155,450
Due from fellow subsidiaries	32	10,960	46,016
Due from a non-controlling shareholder of a subsidiary	30	—	323
Due from an intermediate holding company	31	5,282	—
Loans to associates	18	9,497	—
Loans to related companies	25	16,760	17,230
Prepayments, deposits and other receivables	26	42,978	61,714
Equity investment at fair value through profit or loss	27	87,619	285,713
Prepaid taxes	28	16,186	12,156
Pledged time deposits	29	—	359
Cash and cash equivalents	29	605,925	473,330
Total current assets		4,969,966	5,127,503

	Notes	2016 HK$'000	2015 HK$'000
CURRENT LIABILITIES			
Due to non-controlling shareholders of subsidiaries	30	88,444	64,301
Due to an intermediate holding company	31	—	14,164
Due to fellow subsidiaries	32	1,643	4
Loans from fellow subsidiaries	32	586,592	205,988
Trade and bills payables	33	41,213	92,358
Other payables and accruals	34	17,223	32,744
Customer deposits		920,238	248,310
Interest-bearing bank borrowings	35	—	37,964
Tax payable		37,449	68,139
Total current liabilities		1,692,802	763,972
NET CURRENT ASSETS		3,277,164	4,363,531
TOTAL ASSETS LESS CURRENT LIABILITIES		4,010,271	5,653,574
NON-CURRENT LIABILITIES			
Loans from an intermediate holding company	31	475,419	509,581
Loans from a fellow subsidiary	32	648,045	1,658,683
Interest-bearing bank borrowings	35	230,134	—
Deferred tax liabilities	36	129,920	153,652
Total non-current liabilities		1,483,518	2,321,916
Net assets		2,526,753	3,331,658
EQUITY			
Equity attributable to owners of the parent			
Issued capital	37	551,959	551,959
Reserves	39	1,421,313	2,185,575
		1,973,272	2,737,534
Non-controlling interests		553,481	594,124
Total equity		2,526,753	3,331,658

Pan Linwu
Director

Lai Weixuan
Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2016

	Attributable to owners of the parent									
	Issued capital HK$'000	Share premium account HK$'000	Share option reserve HK$'000	Available-for-sale investment revaluation reserve HK$'000	Reserve fund HK$'000 (note 39)	Exchange fluctuation reserve HK$'000	Retained profits HK$'000	Total HK$'000	Non-controlling interests HK$'000	Total equity HK$'000
At 1 January 2015	551,959	609,080	5,193	31,546	7,882	38,384	1,539,327	2,783,371	578,390	3,361,761
Profit for the year	—	—	—	—	—	—	41,820	41,820	41,640	83,460
Other comprehensive income for the year:										
Changes in fair value of available-for-sale investments, net of tax	—	—	—	(15,144)	—	—	—	(15,144)	—	(15,144)
Share of other comprehensive income of associates	—	—	—	17,211	—	(1,183)	—	16,028	—	16,028
Release of share of an associate's other comprehensive income upon deemed disposal of the associate	—	—	(5,193)	(22,948)	—	(10,100)	—	(38,241)	—	(38,241)
Exchange differences related to foreign operations	—	—	—	—	—	(50,300)	—	(50,300)	(25,906)	(76,206)
Total comprehensive income for the year	—	—	(5,193)	(20,881)	—	(61,583)	41,820	(45,837)	15,734	(30,103)
Transfer to reserve fund	—	—	—	—	10,595	—	(10,595)	—	—	—
At 31 December 2015	551,959	609,080*	—*	10,665*	18,477*	(23,199)*	1,570,552*	2,737,534	594,124	3,331,658

		Attributable to owners of the parent								
	Note	Issued capital HK$'000	Share premium account HK$'000	Available-for-sale investment revaluation reserve HK$'000	Reserve fund HK$'000 (note 39)	Exchange fluctuation reserve HK$'000	Retained profits HK$'000	Total HK$'000	Non-controlling interests HK$'000	Total equity HK$'000
At 1 January 2016		551,959	609,080	10,665	18,477	(23,199)	1,570,552	2,737,534	594,124	3,331,658
Loss for the year		—	—	—	—	—	(685,842)	(685,842)	(23,089)	(708,931)
Other comprehensive income for the year:										
Changes in fair value of available-for-sale investments, net of tax		—	—	14,721	—	—	—	14,721	—	14,721
Share of other comprehensive income of a joint venture		—	—	—	—	(8,905)	—	(8,905)	—	(8,905)
Exchange differences related to foreign operations		—	—	—	—	(84,236)	—	(84,236)	(42,132)	(126,368)
Total comprehensive income for the year		—	—	14,721	—	(93,141)	(685,842)	(764,262)	(65,221)	(829,483)
Transfer to reserve fund		—	—	—	121	—	(121)	—	—	—
Disposal of a subsidiary	41	—	—	—	(93)	—	93	—	24,578	24,578
At 31 December 2016		551,959	609,080*	25,386*	18,505*	(116,340)*	884,682*	1,973,272	553,481	2,526,753

* These reserve accounts comprise the consolidated reserves of HK$1,421,313,000 (2015: HK$2,185,575,000) in the consolidated statement of financial position.

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December 2016

	Notes	2016 HK$'000	2015 HK$'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit/(loss) before tax:			
From continuing operations		(742,978)	205,573
From a discontinued operation	11	(5,075)	(14,259)
Adjustments for:			
Finance costs		1,265	50,353
Share of profits and losses of a joint venture and associates		218,382	68,615
Bank interest income		(2,176)	(11,907)
Interest income on a convertible bond	5	(1,036)	(518)
Interest income on loans to associates	5	(577)	(1,229)
Interest income on loans to related companies	5	(1,076)	(1,994)
Net gain on deemed disposal of associates	18	(3,386)	(433,380)
Depreciation	13	2,487	3,969
Amortisation of customer relationship	16	95	190
Recognition of prepaid land lease payments	15	13	73
Provision for impairment of a loan to a related company	6	12,608	—
Provision for impairment of trade and bills receivables		—	6,871
Provision for impairment/(recovery) of prepayments and other receivables		4,345	(6,152)
Loss/(gain) on disposal of items of property, plant and equipment	5, 6	(222)	105
Provision of impairment of items of property, plant and equipment		—	6,924
Fair value losses/(gains) on investment properties	5, 6	34,047	(757)
Reversal of impairment of loans to associates	6	—	(11,677)
Impairment of an investment in a joint venture	6	7,745	—
Fair value loss on an equity investment at fair value through profit or loss		198,094	1,204
Gain on derecognition of available-for-sale investments	20(a), (b)	—	(224)
Fair value loss/(gain) of available-for-sale investments (transfer from equity on derecognition)	20(a), (b),(c)	490	(19,091)
Impairment of an available-for-sale investment	20(d)	134,107	311,137
Fair value loss/(gain) on derivative financial instruments, net	21	108,558	(28,146)
		(34,290)	125,680

	Notes	2016 HK$'000	2015 HK$'000
Decrease/(increase) in properties under development and completed properties held for sale		(172,696)	1,594,911
Decrease/(increase) in inventories		502	(1,797)
Decrease/(increase) in trade and bills receivables		83,708	(164,791)
Decrease in prepayments, deposits and other receivables		12,108	84,455
Decrease/(increase) in amounts due from fellow subsidiaries		34,671	(49,194)
Decrease/(increase) in an amount due from a non-controlling shareholder of a subsidiary		323	(323)
Increase/(decrease) in trade and bills payables		(31,988)	84,127
Increase/(decrease) in other payables and accruals		6,696	(21,514)
Increase/(decrease) in customer deposits		689,909	(1,454,289)
Cash generated from operations		588,943	197,265
Overseas tax paid		(41,544)	(40,756)
Net cash flows from operating activities		547,399	156,509
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of items of property, plant and equipment	13	(96)	(1,926)
Proceeds from disposal of items of property, plant and equipment		746	—
Proceeds from disposal of available-for-sale investments		1,800	3,090
Additional investment in an associate		—	(4,500)
Repayment of a loan from an associate		—	1,078
Repayment of loans to related companies		22	19,656
Advance of a loan to a related company		—	(11,976)
Disposal of a subsidiary	41	3,716	—
Bank interest received		2,072	14,836
Interest received on a convertible bond		1,036	518
Interest received on loans to associates		427	975
Interest received on other receivables		—	2,528
Interest received on loans to related companies		790	4,445
Decrease/(increase) in pledged time deposits		(2,815)	4
Decrease in a time deposit with original maturity of more than three months when acquired		—	155,588
Net cash flows from investing activities		7,698	184,316

	Notes	2016 HK$'000	2015 HK$'000
CASH FLOWS FROM FINANCING ACTIVITIES			
New bank loans		230,134	37,964
Repayment of bank loans		—	(675,148)
New loans from an intermediate holding company		—	509,581
Repayment of loans from fellow subsidiaries		(495,008)	(443,090)
Increase in amounts due to non-controlling shareholders of subsidiaries		28,817	16,111
Increase/(decrease) in an amount due to an intermediate holding company		(15,189)	14,164
Increase in amounts due to fellow subsidiaries		713	360
Interest paid		(162,359)	(392,434)
Net cash flows used in financing activities		(412,892)	(932,492)
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS		142,205	(591,667)
Cash and cash equivalents at beginning of year		473,330	1,093,361
Effect of foreign exchange rate changes, net		(9,610)	(28,364)
CASH AND CASH EQUIVALENTS AT END OF YEAR		605,925	473,330
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balances	29	307,215	461,354
Non-pledged time deposits with original maturity of less than three months when acquired	29	298,710	11,976
		605,925	473,330

NOTES TO FINANCIAL STATEMENTS

31 December 2016

1. CORPORATE AND GROUP INFORMATION

AVIC International Holding (HK) Limited is a limited liability company incorporated in Bermuda. The registered office of the Company is located at Canon's Court, 22 Victoria Street, Hamilton, HM 12, Bermuda.

During the year, the Group was mainly involved in the following activities:

(i) the property development and investment business;

(ii) the trading business; and

(iii) the knitting and textile business*.

* The Group disposed of the knitting and textile business during the year. Details of the disposal are included in note 41 to the financial statements.

In the opinion of the directors, the ultimate holding company of the Company is Aviation Industry Corporation of China, which is incorporated in the People's Republic of China (the "PRC").

Information about subsidiaries

Particulars of the Company's principal subsidiaries are as follows:

Name	Place of incorporation/ registration and business	Issued ordinary/ registered share capital	Percentage of equity attributable to the Company		Principal activities
			Direct	Indirect	
CATIC Helicopter Development (Shenzhen) Limited ("CATIC Helicopter SZ")*#	PRC/Mainland China	HK$42,000,000	—	100	Investment holding
Billirich Investment Limited#	British Virgin Islands/Hong Kong	US$1,000	100	—	Investment holding
Ease Triumph International Limited	Hong Kong/Hong Kong	HK$250,000,002	100	—	Investment holding
重慶航龍置業有限公司 (「重慶航龍」)**#	PRC/Mainland China	US$62,530,000	—	99	Property developer of residential and commercial projects

Name	Place of incorporation/ registration and business	Issued ordinary/ registered share capital	Percentage of equity attributable to the Company		Principal activities
			Direct	Indirect	
大連航華置業有限公司 (「大連航華」)**#	PRC/Mainland China	US$96,000,000	—	52.08	Property developer of residential and commercial projects
CATIC General Aviation Holdings Limited#	British Virgin Islands/Hong Kong	US$2	100	—	Investment holding
Wahman Investment Limited#	British Virgin Islands/Hong Kong	US$1	100	—	Investment holding
Smartcon Investment Limited#	British Virgin Islands/Hong Kong	US$1	100	—	Investment holding
Sanba Investment Limited#	British Virgin Islands/Hong Kong	US$1	100	—	Investment holding
Welly Investment Limited#	British Virgin Islands/Hong Kong	US$1	100	—	Investment holding
Sumber Investment Limited#	British Virgin Islands/Hong Kong	US$1	100	—	Investment holding
Kingspot Investment Limited#	British Virgin Islands/Hong Kong	HK$1	100	—	Investment holding
Sino-Aviation Investments Limited ("Sino-Aviation Investments")#	British Virgin Islands/Hong Kong	US$1	100	—	Investment holding
Yipon Investment Limited#	British Virgin Islands/Hong Kong	US$1	100	—	Investment holding
CATIC Helicopter (H.K.) Limited#	British Virgin Islands/Hong Kong	US$2	100	—	Investment holding

* CATIC Helicopter SZ is registered as a wholly-foreign-owned enterprise under PRC law.

** 重慶航龍 and 大連航華 are registered as sino-foreign co-operative joint ventures under PRC law.

\# None of the statutory financial statements of these subsidiaries was audited by Ernst & Young, Hong Kong or another member firm of the Ernst & Young global network.

The above tables list the subsidiaries of the Company which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

During the year, the Group disposed of its 51% equity interest in 浙江東陽金牛針織製衣有限公司 ("Zhejiang Dongyang Jinniu"). Further details of the above disposal are included in note 41 to the financial statements.

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which include all Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for investment properties, an equity investment at fair value through profit or loss, certain available-for-sale investments, and derivative financial instruments which have been measured at fair value. These financial statements are presented in Hong Kong dollars and all values are rounded to the nearest thousand except when otherwise indicated.

Basis of consolidation

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

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

(a) the contractual arrangement with the other vote holders of the investee;

(b) rights arising from other contractual arrangements; and

(c) the Group's voting rights and potential voting rights.

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

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

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

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

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES

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

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

Other than as explained below regarding the impact of amendments to HKAS 1 and certain amendments included in the *Annual Improvements 2012-2014 Cycle*, the adoption of the above new and revised standards has had no significant financial effect on these financial statements.

(a) Amendments to HKAS 1 include narrow-focus improvements in respect of the presentation and disclosure in financial statements. The amendments clarify:

(i) the materiality requirements in HKAS 1;

(ii) that specific line items in the statement of profit or loss and the statement of financial position may be disaggregated;

(iii) that entities have flexibility as to the order in which they present the notes to financial statements; and

(iv) that the share of other comprehensive income of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

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

(b) *Annual Improvements to HKFRSs 2012-2014 Cycle* issued in October 2014 sets out amendments to a number of HKFRSs. Details of the amendments are as follows:

- HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*: Clarifies that changes to a plan of sale or a plan of distribution to owners should not be considered to be a new plan of disposal, rather it is a continuation of the original plan. Accordingly, there is no change in the application of the requirements in HKFRS 5. The amendments also clarify that changing the disposal method does not change the date of classification of the non-current assets or disposal group held for sale. The amendments are to be applied prospectively. The amendments have had no impact on the Group as the Group did not have any change in the plan of sale or disposal method in respect of the disposal group held for sale during the year.

2.3 ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

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

Amendments to HKFRS 2	*Classification and Measurement of Share-based Payment Transactions*[2]
Amendments to HKFRS 4	*Applying HKFRS 9 Financial Instruments with HKFRS 4 Insurance Contracts*[2]

HKFRS 9	*Financial Instruments*[2]
Amendments to HKFRS 10 and HKAS 28 (2011)	*Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*[4]
HKFRS 15	*Revenue from Contracts with Customers*[2]
Amendments to HKFRS 15	*Clarifications to HKFRS 15 Revenue from Contracts with Customers*[2]
HKFRS 16	*Leases*[3]
Amendments to HKAS 7	*Disclosure Initiative*[1]
Amendments to HKAS 12	*Recognition of Deferred Tax Assets for Unrealised Losses*[1]

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

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

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

4 No mandatory effective date yet determined but available for adoption

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

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

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

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

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

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

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

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

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments in associates and a joint venture

An associate is an entity in which the Group has a long term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

The Group's investments in associates and a joint venture are stated in the consolidated statement of financial position at the Group's share of net assets under the equity method of accounting, less any impairment losses. Adjustments are made to bring into line any dissimilar accounting policies that may exist. The Group's share of the post-acquisition results and other comprehensive income of associates and the joint venture is included in the consolidated statement of profit or loss and consolidated other comprehensive income, respectively. In addition, when there has been a change recognised directly in the equity of the associate or joint venture, the Group recognises its share of any changes, when applicable, in the consolidated statement of changes in equity. Unrealised gains and losses resulting from transactions between the Group and its associates or joint venture are eliminated to the extent of the Group's investments in the associates or joint venture, except where unrealised losses provide evidence of an impairment of the assets transferred. Goodwill arising from the acquisition of associates or the joint venture is included as part of the Group's investments in associates or the joint venture.

If an investment in an associate becomes an investment in a joint venture or vice versa, the retained interest is not remeasured. Instead, the investment continues to be accounted for under the equity method. In all other cases, upon loss of significant influence over the associate or joint control over the joint venture, the Group measures and recognises any retained investment at its fair value. Any difference between the carrying amount of the associate or joint venture upon loss of significant influence or joint control and the fair value of the retained investment and proceeds from disposal is recognised in profit or loss.

Business combinations and goodwill

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

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

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

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

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

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

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

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

Fair value measurement

The Group measures its investment properties, derivative financial instruments and certain equity investments at fair value at the end of each reporting period. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either in the principal market for the asset or liability, or in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or the most advantageous market must be accessible by the Group. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

Level 1 — based on quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2 — based on valuation techniques for which the lowest level input that is significant to the fair value measurement is observable, either directly or indirectly

Level 3 — based on valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by reassessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

Impairment of non-financial assets

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

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

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

Related parties

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

(a) the party is a person or a close member of that person's family and that person

(i) has control or joint control over the Group;

(ii) has significant influence over the Group; or

(iii) is a member of the key management personnel of the Group or of a parent of the Group;

or

(b) the party is an entity where any of the following conditions applies:

(i) the entity and the Group are members of the same group;

(ii) one entity is an associate or joint venture of the other entity (or of a parent, subsidiary or fellow subsidiary of the other entity);

(iii) the entity and the Group are joint ventures of the same third party;

(iv) one entity is a joint venture of a third entity and the other entity is an associate of the third entity;

(v) the entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group;

(vi) the entity is controlled or jointly controlled by a person identified in (a);

(vii) a person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity); and

(viii) the entity, or any member of a group of which it is a part, provides key management personnel services to the Group or to the parent of the Group.

Property, plant and equipment and depreciation

Property, plant and equipment are stated at cost less accumulated depreciation and any impairment losses. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

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

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

Land and buildings	Over the lease terms
Plant and machinery	10%-20%
Furniture, fixtures and equipment	20%-33%
Motor vehicles	20%-25%

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

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

Investment properties

Investment properties are interests in land and buildings (including the leasehold interest under an operating lease for a property which would otherwise meet the definition of an investment property) held to earn rental income and/or for capital appreciation, rather than for use in the production or supply of goods or services or for administrative purposes; or for sale in the ordinary course of business. Such properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the end of the reporting period.

Gains or losses arising from changes in the fair values of investment properties are included in the statement of profit or loss in the year in which they arise.

Any gains or losses on the retirement or disposal of an investment property are recognised in the statement of profit or loss in the year of the retirement or disposal.

For a transfer from investment properties to owner-occupied properties or inventories, the deemed cost of a property for subsequent accounting is its fair value at the date of change in use. For a transfer from inventories to investment properties, any difference between the fair value of the property at that date and its previous carrying amount is recognised in the statement of profit or loss.

Properties under development

Properties under development are stated at cost less any impairment losses. Cost of properties under development comprises cost of acquisition, land cost, construction costs, development costs, capitalised borrowing costs and other direct costs attributable to the development. The land cost is recognised on the straight-line basis over the lease term. Impairment is assessed by the directors based on prevailing market prices, on an individual property basis.

Properties held for sale

Properties held for sale are stated at the lower of cost and net realisable value. Cost is determined by apportionment of total development cost, including capitalised borrowing cost, attributable to the unsold units. Net realisable value is determined on the basis of anticipated sales proceeds, or estimated by management based on the prevailing market conditions, less all estimated costs to completion and selling expenses, on an individual property basis.

Intangible assets (other than goodwill)

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

Customer relationship

Customer relationship is stated at cost less any impairment losses and is amortised on the straight-line basis over its estimated useful life of 6 years.

Leases

Leases that transfer substantially all the rewards and risks of ownership of assets to the Group, other than legal title, are accounted for as finance leases. At the inception of a finance lease, the cost of the leased asset is capitalised at the present value of the minimum lease payments and recorded together with the obligation, excluding the interest element, to reflect the purchase and financing. Assets held under capitalised finance leases, including prepaid land lease payments under finance leases, are included in property, plant and equipment, and depreciated over the shorter of the lease terms and the estimated useful lives of the assets. The finance costs of such leases are charged to the statement of profit or loss so as to provide a constant periodic rate of charge over the lease terms.

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

Prepaid land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms. When the lease payments cannot be allocated reliably between the land and buildings elements, the entire lease payments are included in the cost of the land and buildings as a finance lease in property, plant and equipment.

Investments and other financial assets

Initial recognition and measurement

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

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

Subsequent measurement

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

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include the financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit or loss. Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments as defined by HKAS 39.

Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with net changes in fair value recognised in the statement of profit or loss. These net fair value changes do not include any dividends or interest earned on these financial assets, which are recognised in accordance with the policies set out for “Revenue recognition” below.

Financial assets designated upon initial recognition as at fair value through profit or loss are designated at the date of initial recognition and only if the criteria in HKAS 39 are satisfied.

Derivatives embedded in host contracts are accounted for as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contracts and the host contracts are not held for trading or designated as at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the statement of profit or loss. Reassessment only occurs if there is either a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required or a reclassification of a financial asset out of the fair value through profit or loss category.

Loans and receivables

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

Available-for-sale financial investments

Available-for-sale financial investments are non-derivative financial assets in listed and unlisted equity investments and debt securities and a financial asset under Project EC120 as set out in notes 20 and 19, respectively, to the financial statements. Equity investments classified as available for sale are those which are neither classified as held for trading nor designated as at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in market conditions.

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

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

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

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

Derecognition of financial assets

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

- the rights to receive cash flows from the asset have expired; or

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

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

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

Impairment of financial assets

The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. An impairment exists if one or more events that occurred after the initial recognition of the asset have an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that a debtor or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial assets carried at amortised cost

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

The amount of any impairment loss identified is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not yet been incurred). The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition).

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

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

Available-for-sale financial investments

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

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

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

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

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

Financial liabilities

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, or as loans and borrowings, as appropriate.

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

The Group’s financial liabilities include amounts due to fellow subsidiaries and non-controlling shareholders of subsidiaries, loans from fellow subsidiaries and an intermediate holding company, trade and bills payables, other payables and accruals and interest-bearing bank borrowings.

Subsequent measurement of loans and borrowings

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

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

Derecognition of financial liabilities

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

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

Offsetting of financial instruments

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

Inventories

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

Cash and cash equivalents

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

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

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the end of the reporting period of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the statement of profit or loss.

Income tax

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

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

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

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

- when the deferred tax liability arises from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with investments in subsidiaries, associates and a joint venture, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

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

- when the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with investments in subsidiaries, associates and a joint venture, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

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

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

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

Government grants

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

Revenue recognition

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

(a) from the sale of properties, when the significant risks and rewards of the properties are passed to the purchasers when (i) an irrevocable sale and purchase contract has been entered into by both buyer and seller; (ii) the seller has received or retained the right to receive all the consideration of the sale; (iii) the construction has been completed, and its quality has been inspected and accepted by the relevant government authorities; (iv) the ready-for-delivery conditions under the sale and purchase contract have been fulfilled; and (v) the notices of property delivery have been sent to the buyer;

(b) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;

(c) rental income, on a time proportion basis over the lease terms;

(d) interest income, on an accrual basis using the effective interest method by applying the rate that exactly discounts the estimated future cash receipts over the expected life of the financial instrument or a shorter period, when appropriate, to the net carrying amount of the financial asset;

(e) dividend income, when the shareholders' right to receive payment has been established; and

(f) from the development, manufacture and distribution of helicopters, when the Group's right to receive its share of profit from Project EC120 has been established *(note 19)*.

Share-based payments

The Company operates a share option scheme for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Employees (including directors) of the Group receive remuneration in the form of share-based payments, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

The cost of equity-settled transactions with employees for grants after 7 November 2002 is measured by reference to the fair value at the date at which they are granted.

The cost of equity-settled transactions is recognised in employee benefit expense, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled. The cumulative expense recognised for equity-settled transactions at the end of each reporting period until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The charge or credit to the statement of profit or loss for a period represents the movement in the cumulative expense recognised as at the beginning and end of that period.

Service and non-market performance conditions are not taken into account when determining the grant date fair value of awards, but the likelihood of the conditions being met is assessed as part of the Group's best estimate of the number of equity instruments that will ultimately vest. Market performance conditions are reflected within the grant date fair value. Any other conditions attached to an award, but without an associated service requirement, are considered to be non-vesting conditions. Non-vesting conditions are reflected in the fair value of an award and lead to an immediate expensing of an award unless there are also service and/or performance conditions.

For awards that do not ultimately vest because non-market performance and/or service conditions have not been met, no expense is recognised. Where awards include a market or non-vesting condition, the transactions are treated as vesting irrespective of whether the market or non-vesting condition is satisfied, provided that all other performance and/or service conditions are satisfied.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified, if the original terms of the award are met. In addition, an expense is recognised for any modification that increases the total fair value of the share-based payments, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. This includes any award where non-vesting conditions within the control of either the Group or the employee are not met. However, if a new award is substituted for the cancelled award, and is designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect of outstanding options, if any, is reflected as additional share dilution in the computation of earnings per share.

The cost of cash-settled transactions is measured initially at fair value at the grant date taking into account the terms and conditions upon which the instruments were granted. The fair value is expensed over the period until the vesting date with recognition of a corresponding liability. The liability is measured at the end of each reporting period up to and including the settlement date, with changes in fair value recognised in the Group's statement of profit or loss.

Other employee benefits

Pension schemes

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

The employees of the Group's subsidiaries which operate in Mainland China are required to participate in a central pension scheme operated by the local municipal government. These subsidiaries are required to contribute a certain percentage of their payroll costs to the central pension scheme. The contributions are charged to the statement of profit or loss as they become payable in accordance with the rules of the central pension scheme.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e., 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. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised. All other borrowing costs are expensed in the period in which they are incurred. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

Foreign currencies

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

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

The functional currencies of certain overseas subsidiaries, joint venture and associates are currencies other than the Hong Kong dollar. As at the end of the reporting period, the assets and liabilities of these entities are translated into Hong Kong dollars at the exchange rates prevailing at the end of the reporting period and their statements of profit or loss are translated into Hong Kong dollars at the weighted average exchange rates for the year.

The resulting exchange differences are recognised in other comprehensive income and accumulated in the exchange fluctuation reserve. On disposal of a foreign operation, the component of other comprehensive income relating to that particular foreign operation is recognised in the statement of profit or loss.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on acquisition are treated as assets and liabilities of the foreign operation and translated at the closing rate.

For the purpose of the consolidated statement of cash flows, the cash flows of overseas subsidiaries are translated into Hong Kong dollars at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of the overseas subsidiaries which arise throughout the year are translated into Hong Kong dollars at the weighted average exchange rates for the year.

3. SIGNIFICANT ACCOUNTING JUDGEMENT AND ESTIMATES

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

Judgement

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

Classification of equity investments among investments in subsidiaries, investments in associates and an investment in a joint venture

In determining whether an equity investment is classified as investments in subsidiaries, investments in associates or an investment in a joint venture, the Group considers a number of factors including (1) whether the Group has the power to exercise control; (2) whether the Group can exercise significant influence; and (3) whether the unanimous consent of the parties sharing control is required for the relevant activities of the investee company.

Estimation uncertainty

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

Deferred tax assets

Deferred tax assets are recognised for unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies. The carrying value of deferred tax assets relating to recognised tax losses at 31 December 2016 was HK$38,056,000 (2015: HK$37,448,000). Further details are included in note 36 to the financial statements.

Estimation of fair value of investment properties

In the absence of current prices in an active market for similar properties, the Group considers information from a variety of sources, including:

(a) current prices in an active market for properties of a different nature, condition or location, adjusted to reflect those differences;

(b) recent prices of similar properties on less active markets, with adjustments to reflect any changes in economic conditions since the date of the transactions that occurred at those prices; and

(c) discounted cash flow projections based on reliable estimates of future cash flows, supported by the terms of any existing lease and other contracts and (when possible) by external evidence such as current market rents for similar properties in the same location and condition, and using discount rates that reflect current market assessments of the uncertainty in the amount and timing of the cash flows.

The aggregate carrying amount of investment properties at 31 December 2016 was HK$315,866,000 (2015: HK$373,425,000). Further details, including the key assumptions used for fair value measurement and a sensitivity analysis, are included in note 14 to the financial statements.

Impairment of non-financial assets (other than goodwill)

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

Impairment of trade and bills receivables and deposits and other receivables

The Group maintains an allowance for estimated losses arising from the inability of the customers or borrowers to make the required payments. The Group makes the estimates based on the ageing of trade and bills receivables and deposits and other receivable balances, customers' creditworthiness, and historical write-off experience. If the financial condition of the customers or borrowers was to deteriorate so that the actual impairment loss might be higher than expected, the Group would be required to revise the basis of making the allowance and the future results would be affected. The carrying amounts of trade and bills receivables and deposits and other receivables as at 31 December 2016 were HK$89,620,000 (2015: HK$177,078,000) and HK$15,407,000 (2015: HK$45,064,000), respectively. Further details are included in notes 24 and 26 to the financial statements.

Estimation of recoverable amounts of properties under development

The Group considers information from a variety of sources, including recent prices of similar properties in the same location and condition, with adjustments to reflect any changes in economic conditions since the date of transactions that occurred at those prices.

Estimation of total budgeted costs and costs of completion for properties under development

Total budgeted costs for properties under development comprise (i) prepaid land lease payments; (ii) building costs; and (iii) any other direct costs attributable to the development of the properties. In estimating the total budgeted costs for properties under development, management makes reference to information such as (i) current offers from contractors and suppliers; (ii) recent offers agreed with contractors and suppliers; and (iii) professional estimation on construction and material costs.

Land appreciation tax

Under the Detailed Rules for the Implementation of Provisional Regulations on Land Appreciation Tax ("LAT") implemented upon the issuance of the Provisional Regulations of the PRC on 27 January 1995, all gains arising from the transfer of real estate properties in Mainland China with effect from 1 January 1994 are subject to LAT at progressive rates ranging from 30% to 60% on the appreciation of land value, being the proceeds from sales of properties less deductible expenditures including amortisation of land use rights, borrowing costs and all property development expenditures.

The subsidiaries of the Group engaging in the property development business in Mainland China are subject to LAT. However, the implementation of LAT varies amongst various Mainland China cities and the Group has not finalised certain of its LAT returns with various tax authorities. Accordingly, significant judgement is required in determining the amount of land appreciation and its related taxes. The ultimate tax determination is uncertain during the ordinary course of business. The Group recognises these liabilities based on management's best estimates. When the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact on the income tax and provisions of LAT in the period in which such determination is made.

4. OPERATING SEGMENT INFORMATION

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

(a) the property development and investment business segment engages in the property development of residential and commercial projects; and

(b) the trading business segment engages in the trading of raw materials and auxiliary materials.

During the year, the Group disposed of the knitting and textile business. Accordingly, the comparative segment information related to the knitting and textile business is reclassified as "profit/(loss) for the year from a discontinued operation" in the consolidated statement of profit or loss. Details of which are set out in note 11 to the financial statements.

Management monitors the results of the Group's operating segments separately for the purpose of making decisions about resources allocation and performance assessment. Segment performance is evaluated based on reportable segment profit/(loss), which is a measure of adjusted profit/(loss) for the year from continuing operations. The adjusted profit/(loss) for the year from continuing operations is measured consistently with the Group's profit/(loss) for the year from continuing operations except that certain income and gains or losses relating to investments in a joint venture and associates and financial instruments, as well as head office and corporate expenses (including reversal of impairments/impairments of loans to associates and related companies and an investment in a joint venture, and recovery/impairment of other receivables) and unallocated income tax are excluded from such measurement.

The following is an analysis of the Group's revenue and results from continuing operations by reportable operating segments.

Year ended 31 December 2016

	Property development and investment business	**Trading business**	**Total**
	HK$'000	*HK$'000*	*HK$'000*
Segment revenue:			
Sales to external customers	85,987	—	85,987
Gross rental income	16,799	—	16,799
Revenue from continuing operations	102,786	—	102,786
Segment results	(47,058)	—	(47,058)
Reconciliation:			
Unallocated other income			5,985
Corporate and other unallocated expenses			(38,592)
Net gain on deemed disposal of associates			3,386
Share of profits and losses of:			
Joint venture			(215,369)
Associates			(3,013)
Impairment of an available-for-sale investment			(134,107)
Fair value loss of available-for-sale investments			(490)
Fair value loss on derivative financial instruments, net			(108,558)
Fair value loss on an equity investment at fair value through profit or loss			(198,094)
Unallocated income tax expense			(383)
Loss for the year from continuing operations			(736,293)
Other segment information:			
Bank interest income	1,789	—	1,789
Unallocated bank interest income			385
			2,174
Depreciation	—	—	—
Unallocated depreciation			(2,174)
			(2,174)
Finance costs	(77)	—	(77)

Year ended 31 December 2015

	Property development and investment business *HK$'000*	Trading business *HK$'000*	Total *HK$'000* *(Restated)*
Segment revenue:			
Sales to external customers	2,137,619	7,644	2,145,263
Gross rental income	9,725	—	9,725
Revenue from continuing operations	2,147,344	7,644	2,154,988
Segment results	35,065	175	35,240
Reconciliation:			
Unallocated other income			4,461
Corporate and other unallocated expenses			(15,957)
Net gain on deemed disposal of associates			433,380
Share of profits and losses of:			
Joint venture			(27,278)
Associates			(41,337)
Impairment of an available-for-sale investment			(311,137)
Gain on derecognition of available-for-sale investments			224
Fair value gain of available-for-sale investments			19,091
Fair value gain on derivative financial instruments, net			28,146
Fair value loss on an equity investment at fair value through profit or loss			(1,204)
Unallocated income tax expense			(26,113)
Profit for the year from continuing operations			97,516
Other segment information:			
Bank interest income	769	9,010	9,779
Unallocated bank interest income			2,114
			11,893
Depreciation	(1)	(1,225)	(1,226)
Unallocated depreciation			(1,294)
			(2,520)
Finance costs	(47,638)	—	(47,638)

Geographical information

(a) Revenue from external customers

	2016	2015
	HK$'000	*HK$'000*
		(Restated)
Mainland China	102,786	2,154,988

The revenue information of continuing operations above is based on the location of the customers.

(b) Non-current assets

	2016	2015
	HK$'000	*HK$'000*
Hong Kong	23,211	24,411
Mainland China	389,610	688,668
	412,821	713,079

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

Information about major customers

Revenue from continuing operations of approximately HK$44,390,000 (2015: Nil) was derived from sales by the property development and investment business segment to two customers of HK$31,100,000 and HK$13,290,000, respectively.

5. REVENUE, OTHER INCOME AND GAINS

Revenue represents the sale of properties; the net invoiced value of goods sold, after allowances for returns and trade discounts; and gross rental income received and receivable from investment properties during the year.

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

	2016	2015
	HK$'000	*HK$'000*
		(Restated)
Revenue		
Sale of properties	85,987	2,137,619
Sale of raw materials and auxiliary materials	—	7,644
Gross rental income	16,799	9,725
	102,786	2,154,988
Other income		
Bank interest income	2,174	11,893
Interest income on a convertible bond	1,036	518
Interest income on loans to associates	577	1,229
Interest income on loans to related companies	1,076	1,994
Government grant*	7,534	17,800
Others	146	359
	12,543	33,793
Gains		
Fair value gains on investment properties *(note 14)*	—	757
Gain on disposal of items of property, plant and equipment	222	—
	12,765	34,550

* This represents subsidies from municipal government in Mainland China. There are no unfulfilled conditions or contingencies relating to these subsidies.

6. PROFIT/(LOSS) BEFORE TAX

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

	Notes	2016 HK$'000	2015 HK$'000 (Restated)
Cost of properties sold*		74,269	1,967,041
Cost of goods sold*		—	7,413
Depreciation		2,174	2,520
Minimum lease payments under operating leases		2,511	5,080
Employee benefit expense (excluding directors' remuneration *(note 8)*):			
Wages and salaries		26,204	21,562
Pension scheme contributions**		2,382	617
		28,586	22,179
Other operating expenses/(income), net:			
Loss on disposal of items of property, plant and equipment		—	105
Fair value losses on investment properties	14	34,047	—
Impairment of an investment in a joint venture	17	7,745	—
Reversal of impairment of loans to associates	18	—	(11,677)
Provision for impairment of loans to related companies	25	12,608	—
Provision for impairment/(recovery) of prepayments and other receivables		233	(3,727)
		54,633	(15,299)
Auditor's remuneration		1,500	2,380
Foreign exchange differences, net		(51)	10,716
Direct operating expenses (including repairs and maintenance) arising on rental-earning investment properties		790	479

* Included in "cost of sales" in the consolidated statement of profit or loss.

** At 31 December 2016, the Group had no forfeited contributions available to reduce its contributions to the pension scheme in future years (2015: Nil).

7. FINANCE COSTS

An analysis of finance costs from continuing operations is as follows:

	2016 *HK$'000*	2015 *HK$'000* *(Restated)*
Interest on bank loans and other loans	156,816	266,319
Less: Interest capitalised	(156,739)	(218,681)
	77	47,638

8. DIRECTORS' AND CHIEF EXECUTIVE'S REMUNERATION

Directors' remuneration for the year, disclosed pursuant to the Listing Rules, section 383(1)(a), (b), (c) and (f) of the Hong Kong Companies Ordinance and Part 2 of the Companies (Disclosure of Information about Benefits of Directors) Regulation, is as follows:

	2016 *HK$'000*	2015 *HK$'000*
Fees	840	836
Other emoluments:		
Salaries, allowances and benefits in kind	—	1,993
Pension scheme contributions	—	119
	—	2,112
	840	2,948

(a) Independent Non-executive Directors

The fees paid to Independent Non-executive Directors during the year were as follows:

	2016 *HK$'000*	2015 *HK$'000*
Chu Yu Lin, David	240	240
Li Ka Fai, David	240	240
Li Zhaoxi	60	60
	540	540

There were no other emoluments payable to the Independent Non-executive Directors during the year (2015: Nil).

(b) Executive Directors and Non-executive Directors

	Fees	Salaries, allowances and benefits in kind	Pension Scheme contributions	Total remuneration
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
2016				
Executive Directors:				
Liu Hongde (appointed on 30 December 2016)	—	—	—	—
Pan Linwu	36	—	—	36
Lai Weixuan	36	—	—	36
Zhou Chunhua (appointed on 30 December 2016)	—	—	—	—
Xu Hongge*	36	—	—	36
Wu Guangquan (resigned on 30 December 2016)	36	—	—	36
Xiao Nan (resigned on 30 December 2016)	36	—	—	36
	180	—	—	180
Non-executive Director:				
Chow Wai Kam	120	—	—	120
	300	—	—	300

* Xu Hongge is also the chief executive officer of the Group.

	Fees	Salaries, allowances and benefits in kind	Pension Scheme contributions	Total remuneration
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
2015				
Executive Directors:				
Wu Guangquan	36	—	—	36
Pan Linwu	36	—	—	36
Lai Weixuan	19	—	—	19
Xu Hongge	19	—	—	19
Xiao Nan	19	—	—	19
You Lei (resigned on 23 June 2015)	17	—	—	17
Ji Guirong (resigned on 23 June 2015)	15	1,613	91	1,719
Zhang Chuanjun (resigned on 23 June 2015)	15	380	28	423
	176	1,993	119	2,288
Non-executive Directors:				
Chow Wai Kam	63	—	—	63
Ip Tak Chuen, Edmond	57	—	—	57
	296	1,993	119	2,408

There was no arrangement under which a director waived or agreed to waive any remuneration during the year (2015: Nil).

9. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees did not include executive directors (2015: two). Details of the remuneration for the year of the five (2015: three) highest paid employees who are not a director of the Company are as follows:

	2016	**2015**
	HK$'000	*HK$'000*
Basic salaries, allowances and benefits in kind	2,333	3,743
Pension scheme contributions	79	87
Performance related bonuses	610	220
	3,022	4,050

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

	Number of employees	
	2016	**2015**
Nil to HK$1,000,000	4	2
HK$1,000,001 to HK$1,500,000	1	—
HK$2,000,001 to HK$2,500,000	—	1
	5	3

10. INCOME TAX

No provision for Hong Kong profits tax has been made as the Group did not generate any assessable profits arising in Hong Kong during the year (2015: Nil). Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries/jurisdictions in which the Group operates.

The provision of LAT has been estimated according to the requirements set forth in the relevant PRC laws and regulations. LAT has been provided at ranges of progressive rates of the appreciation value, with certain allowable deductions.

	2016	2015
	HK$'000	*HK$'000*
		(Restated)
Current-Elsewhere:		
Charge for the year	1,155	100,216
Deferred	(15,225)	(67,024)
LAT in Mainland China	7,385	74,865
Total tax charge/(credit) for the year	(6,685)	108,057

A reconciliation of the tax expense/(credit) applicable to profit/(loss) before tax from continuing operations at the statutory rates for the countries/jurisdictions in which the Company and the majority of its subsidiaries are domiciled to the tax charge/(credit) at the effective rate for the year is as follows:

	2016	2015
	HK$'000	*HK$'000*
		(Restated)
Profit/(loss) before tax from continuing operations	(742,978)	205,573
Tax at the statutory tax rates	(148,280)	29,434
Effect of withholding tax at 5% on the distributable profits of the Group's PRC subsidiary	—	26,113
Profits and losses attributable to the joint venture and associates	54,596	13,403
Income not subject to tax	(1,385)	(83,435)
Expenses not deductible for tax	80,999	47,677
LAT in Mainland China	7,385	74,865
Tax charge/(credit) at the Group's effective rate of 0.9% (2015: 52.6%)	(6,685)	108,057

Share of tax charge attributable to associates of HK$67,000 (2015: HK$1,399,000) is included in "Share of profits and losses of associates" in the consolidated statement of profit or loss.

There was no tax charge attributable to the joint venture shared by the Group during the year (2015: Nil).

11. DISCONTINUED OPERATION

During the year, the Group disposed of Zhejiang Dongyang Jinniu, a 51%-owned subsidiary, to an independent third party. Zhejiang Dongyang Jinniu engaged in the production and distribution of knitting and textile products, knitted fabrics and clothing. The Group decided to dispose of this subsidiary and cease its knitting and textile business because it had been loss-making in recent years.

The results of Zhejiang Dongyang Jinniu included in the Group's consolidated statement of profit or loss as a discontinued operation are presented below:

	2016	**2015**
	HK$'000	*HK$'000*
REVENUE	18,616	43,602
Cost of sales	(17,621)	(41,145)
Gross profit	995	2,457
Other income	112	479
Administrative expenses	(882)	(3,110)
Other operating expenses, net	(4,112)	(11,370)
Finance costs	(1,188)	(2,715)
Loss before tax from the discontinued operation	(5,075)	(14,259)
Income tax credit/(expense)	(16)	203
Loss after tax from the discontinued operation	(5,091)	(14,056)
Pre-tax gain on disposal of a subsidiary *(note 41)*	32,453	—
Tax expense	—	—
After-tax gain on disposal of a subsidiary	32,453	—
Profit/(loss) for the year from the discontinued operation	27,362	(14,056)
Attributable to:		
Owners of the parent	29,857	(7,169)
Non-controlling interests	(2,495)	(6,887)
	27,362	(14,056)
Earnings/(loss) per share:		
Basic and diluted, from the discontinued operation	HK0.54 cent	(HK0.13 cent)

The calculation of basic and diluted earnings/(loss) per share from the discontinued operation is based on:

	2016	2015
Profit/(loss) attributable to ordinary equity holders of the parent from the discontinued operation	HK$29,857,000	(HK$7,169,000)
Weighted average number of ordinary shares in issue during the year	5,519,591,000	5,519,591,000

The net cash flows incurred by Zhejiang Dongyang Jinniu are as follows:

	2016	2015
	HK$'000	*HK$'000*
Operating activities	5,354	3,070
Investing activities	(2,814)	16
Financing activities	(962)	(3,052)
Net cash inflow	1,578	34

12. EARNINGS/(LOSS) PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The calculation of the basic earnings/(loss) per share amounts is based on the profit/(loss) for the year attributable to ordinary equity holders of the parent, and the weighted average number of ordinary shares of 5,519,591,000 (2015: 5,519,591,000) in issue during the year.

No adjustment has been made to the basic earnings/(loss) per share amounts presented for the years ended 31 December 2016 and 2015 in respect of a dilution as the Group had no potentially dilutive ordinary shares in issue during those years.

The calculation of basic and diluted earnings/(loss) per share is based on:

	2016	2015
	HK$'000	*HK$'000*
Profit/(loss) attributable to ordinary equity holders of the parent:		
From continuing operations	(715,699)	48,989
From a discontinued operation	29,857	(7,169)
	(685,842)	41,820

	Number of shares 2016	2015
Weighted average number of ordinary shares in issue during the year	5,519,591,000	5,519,591,000

13. PROPERTY, PLANT AND EQUIPMENT

	Land and buildings *HK$'000*	Plant and machinery *HK$'000*	Furniture, fixtures and equipment *HK$'000*	Motor vehicles *HK$'000*	Total *HK$'000*
31 December 2016					
At 31 December 2015 and 1 January 2016:					
Cost	34,565	11,493	5,223	10,385	61,666
Accumulated depreciation and impairment	(7,567)	(11,493)	(3,879)	(7,132)	(30,071)
Net carrying amount	26,998	—	1,344	3,253	31,595
At 1 January 2016, net of accumulated depreciation and impairment	26,998	—	1,344	3,253	31,595
Additions	—	—	96	—	96
Disposals	—	—	—	(524)	(524)
Disposal of a subsidiary *(note 41)*	(3,004)	—	(36)	(488)	(3,528)
Depreciation provided during the year	(901)	—	(490)	(1,096)	(2,487)
Exchange realignment	—	—	(57)	(120)	(177)
At 31 December 2016, net of accumulated depreciation	23,093	—	857	1,025	24,975
At 31 December 2016:					
Cost	30,350	—	4,958	4,214	39,522
Accumulated depreciation	(7,257)	—	(4,101)	(3,189)	(14,547)
Net carrying amount	23,093	—	857	1,025	24,975

	Land and buildings *HK$'000*	Plant and machinery *HK$'000*	Furniture, fixtures and equipment *HK$'000*	Motor vehicles *HK$'000*	Total *HK$'000*
31 December 2015					
At 1 January 2015:					
Cost	34,782	12,228	5,160	11,696	63,866
Accumulated depreciation	(6,633)	(4,496)	(3,435)	(8,005)	(22,569)
Net carrying amount	28,149	7,732	1,725	3,691	41,297
At 1 January 2015, net of accumulated depreciation	28,149	7,732	1,725	3,691	41,297
Additions	—	—	165	1,761	1,926
Disposals	—	—	—	(515)	(515)
Depreciation provided during the year	(1,049)	(802)	(496)	(1,622)	(3,969)
Impairment	—	(6,924)	—	—	(6,924)
Exchange realignment	(102)	(6)	(50)	(62)	(220)
At 31 December 2015, net of accumulated depreciation and impairment	26,998	—	1,344	3,253	31,595
At 31 December 2015:					
Cost	34,565	11,493	5,223	10,385	61,666
Accumulated depreciation and impairment	(7,567)	(11,493)	(3,879)	(7,132)	(30,071)
Net carrying amount	26,998	—	1,344	3,253	31,595

During the year ended 31 December 2015, impairment of HK$6,924,000 had been recognised for plant and machinery because the knitting and textile business had been loss-making in recent years. The impairment had been determined based on a value in use calculation using cash flow projections based on financial budgets approved by senior management covering a five-year period. The discount rate applied to cash flow projections was 15%.

Assumptions used in the cash flow projections to undertake impairment testing of plant and machinery are as follows:

Budgeted gross margins — The basis used to determine the value assigned to the budgeted gross margins was the average gross margins achieved in the year immediately before the budget year, increased for expected efficiency improvements.

Discount rate — The discount rate used was before tax and reflected specific risks relating to the relevant unit.

The values assigned to key assumptions were consistent with external information sources.

As at 31 December 2015, the Group's building located in Mainland China with net book value of HK$3,148,000 had been pledged to secure general banking facilities granted to the Group *(note 35(b)(i))*.

14. INVESTMENT PROPERTIES

	2016	2015
	HK$'000	*HK$'000*
Carrying amount at 1 January	373,425	—
Transfer from properties under development	—	374,445
Net gain/(loss) from a fair value adjustment *(notes 5 and 6)*	(34,047)	757
Exchange realignment	(23,512)	(1,777)
Carrying amount at 31 December	315,866	373,425

The Group's investment properties consist of commercial properties in Mainland China. The Group's investment properties were revalued on 31 December 2016 based on valuations performed by LCH (Asia-Pacific) Surveyors Limited, independent professionally qualified valuers, at HK$315,866,000. Each year, the Group's chief financial officer decides to appoint which external valuer to be responsible for the external valuations of the Group's properties. Selection criteria include market knowledge, reputation, independence and whether professional standards are maintained. The Group's chief financial officer has discussions with the valuer on the valuation assumptions and valuation results twice a year when the valuation is performed for interim and annual financial reporting.

The investment properties are leased to third parties under operating leases, further summary details of which are included in note 42(a) to the financial statements.

Further particulars of the Group's investment properties are included on page 225.

Fair value hierarchy

The following table illustrates the fair value measurement hierarchy of the Group's investment properties:

	Fair value measurement as at 31 December 2016 using			
	Quoted prices in active markets (Level 1)	**Significant observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Recurring fair value measurement for:				
Commercial properties	—	—	315,866	315,866

	Fair value measurement as at 31 December 2015 using			
	Quoted prices in active markets (Level 1)	**Significant observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Recurring fair value measurement for:				
Commercial properties	—	—	373,425	373,425

During the year, there were no transfers of fair value measurements between Level 1 and Level 2 and no transfers into or out of Level 3 (2015: Nil).

Below is a summary of the valuation techniques used and the key inputs to the valuation of investment properties:

	Valuation techniques	Significant unobservable inputs	Range or weighted average 2016	2015
Commercial properties	Term and reversion method	Term yield	6%	N/A
		Reversionary yield	6.5%	N/A
		Market rent (per sq.m. and per month)	HK$102 to HK$108	N/A
Commercial properties	Discounted cash flow method	Estimated rental value (per sq.m. and per month)	N/A	HK$108 to HK$120
		Rent growth (p.a.)	N/A	2.5%
		Long term vacancy rate	N/A	2%
		Discount rate	N/A	5.6%

The term and reversion method measures the fair value of the property by taking into account the rental income derived from the existing leases with due allowance for the reversionary income potential of the leases, which are then capitalised into the value at appropriate rates.

A significant increase (decrease) in the term yield and the reversionary yield in isolation would result in a significant decrease (increase) in the fair value of the investment properties. A significant increase (decrease) in the market rent would result in a significant increase (decrease) in the fair value of the investment properties.

Under the discounted cash flow method, fair value is estimated using assumptions regarding the benefits and liabilities of ownership over the asset's life including an exit or terminal value. This method involves the projection of a series of cash flows on a property interest. A market-derived discount rate is applied to the projected cash flow in order to establish the present value of the income stream associated with the asset. The exit yield is normally separately determined and differs from the discount rate.

The duration of the cash flows and the specific timing of inflows and outflows are determined by events such as rent reviews, lease renewal and related reletting, redevelopment or refurbishment. The appropriate duration is driven by market behaviour that is a characteristic of the class of property. The periodic cash flow is estimated as gross income less vacancy, non-recoverable expenses, collection losses, lease incentives, maintenance costs, agent and commission costs and other operating and management expenses. The series of periodic net operating income, along with an estimate of the terminal value anticipated at the end of the projection period, is then discounted.

A significant increase (decrease) in the estimated rental value and the market rent growth rate per annum in isolation would result in a significant increase (decrease) in the fair value of the investment properties. A significant increase (decrease) in the long term vacancy rate and the discount rate in isolation would result in a significant decrease (increase) in the fair value of the investment properties. Generally, a change in the assumption made for the estimated rental value is accompanied by a directionally similar change in the rent growth per annum and the discount rate and an opposite change in the long term vacancy rate.

As at 31 December 2016, the Group has adopted the term and reversion method (2015: the discounted cash flow method) to value the investment properties as in the opinion of the directors, the term and reversion method is a more appropriate valuation technique for the Group's investment properties.

15. PREPAID LAND LEASE PAYMENTS

	2016	**2015**
	HK\$'000	*HK\$'000*
Carrying amount at 1 January	2,885	3,032
Disposal of a subsidiary *(note 41)*	(2,872)	—
Exchange realignment	—	(74)
Recognised during the year	(13)	(73)
Carrying amount at 31 December	—	2,885
Current portion included in prepayments, deposits and other receivables	—	(71)
Non-current portion	—	2,814

As at 31 December 2015, the Group's leasehold land located in Mainland China with net book value of HK$2,885,000 had been pledged to secure general banking facilities granted to the Group *(note 35(b)(ii))*.

16. INTANGIBLE ASSET

	Customer relationship
	HK$'000
31 December 2016	
Cost at 1 January 2016, net of accumulated amortisation	380
Amortisation provided during the year	(95)
Disposal of a subsidiary *(note 41)*	(285)
At 31 December 2016	—
At 31 December 2016:	
Cost	—
Accumulated amortisation	—
Net carrying amount	—
31 December 2015	
Cost at 1 January 2015, net of accumulated amortisation	570
Amortisation provided during the year	(190)
At 31 December 2015	380
At 31 December 2015:	
Cost	1,141
Accumulated amortisation	(761)
Net carrying amount	380

17. INVESTMENT IN A JOINT VENTURE

	2016	2015
	HK$'000	*HK$'000*
Share of net assets	58,602	282,876
Goodwill on acquisition	7,745	7,745
	66,347	290,621
Provision for impairment	(7,745)	—
	58,602	290,621

The investment in a joint venture represents the Group's right to enjoy certain economic benefits derived from a 69.4% (2015: 69.4%) equity interest in CATIC Siwei Co., Ltd. ("CATIC Siwei") held by third parties through trust arrangements. CATIC Siwei is registered as a co-operative joint venture under PRC law and is holding an investment in China which operates in aero-technology business and in investment holding.

In the opinion of the directors, notwithstanding that the Group has the right to enjoy certain economic benefits from the 69.4% equity interest in CATIC Siwei, none of the shareholders of CATIC Siwei has unilateral control over the economic activity of CATIC Siwei pursuant to the provisions in the articles and association of CATIC Siwei. Since the Group does not have any power to control the financial and operating activities of CATIC Siwei, the directors consider it is appropriate to account for this right as an investment in a joint venture using the equity method of accounting as at 31 December 2016 and 2015.

The above entity was not audited by Ernst & Young, Hong Kong or another member firm of the Ernst & Young global network.

During the year, impairment of HK$7,745,000 *(note 6)* has been recognised for investment in the joint venture because the joint venture has been loss-making in recent years. The impairment has been determined based on value in use calculation using cash flow projections based on financial budgets. The discount rate applied to cash flow projections was 16%.

The following table illustrates the summarised financial information of CATIC Siwei adjusted for any differences in accounting policies, and reconciled to the carrying amount in the consolidated financial statements:

	2016	**2015**
	HK$'000	*HK$'000*
Cash and cash equivalents	7,140	15,058
Other current assets	49,494	163,000
Current assets	56,634	178,058
Non-current assets	149,490	353,185
Current liabilities	(115,380)	(116,062)
Non-current liabilities	(828)	(1,293)
Net assets	89,916	413,888
Less: Net assets attributable to non-controlling interests	(5,475)	(6,286)
	84,441	407,602
Reconciliation to the Group's interest in the joint venture:		
Proportion of the Group's ownership	69.4%	69.4%
Group's share of net assets of the joint venture	58,602	282,876
Goodwill on acquisition	7,745	7,745
Provision for impairment	(7,745)	—
Carrying amount of the investment	58,602	290,621
Revenue	17,756	17,833
Interest income	2,900	1,091
Depreciation and amortisation	(17,380)	(18,683)
Impairment provision*	(224,155)	(78,295)
Interest expenses	—	—
Tax	—	—
Loss for the year	(311,141)	(39,330)
Other comprehensive income	(12,831)	—
Total comprehensive income for the year	(323,972)	(39,330)

* The impairment has been determined based on a value in use calculation using cash flow projections based on financial budgets approved by senior management covering a five-year period. The discount rate applied to cash flow projections is 16%.

Assumptions used in the cash flow projections to undertake impairment testing are as follows:

Budgeted gross margins — The basis used to determine the value assigned to the budgeted gross margins is the average gross margins achieved in the year immediately before the budget year, increased for expected efficiency improvements.

Discount rate — The discount rate used is before tax and reflects specific risks relating to the relevant unit.

The values assigned to key assumptions are consistent with external information sources.

18. INVESTMENTS IN ASSOCIATES

	2016	**2015**
	HK$'000	*HK$'000*
Share of net assets	13,204	13,792
Goodwill on acquisition	7,500	8,265
	20,704	22,057
Less: Provision for impairment	(7,326)	(8,091)
	13,378	13,966
Loans to associates-non-current	—	40,120
Less: Impairment of loans to associates	—	(29,940)
	—	10,180
	13,378	24,146
Loans to associates included in the Group's current assets:		
Loans to associates current	37,430	—
Less: Impairment of loans to associates	(27,933)	—
	9,497	—

The loans to associates are unsecured and bear interest at 4.5% to 6% (2015: 4.5% to 6%) per annum. Included in the loans to associates are loans of HK$27,933,000 (2015: HK$29,940,000) which have convertible options allowing the Group to convert the loans into ordinary shares of the associates at an established conversion rate (i.e. RMB1 per share). In the opinion of the directors, the fair values of the convertible options do not have significant financial effect and were therefore not recognised in these financial statements.

The loans to associates which are not repayable within one year were classified as non-current and were included in the investments in associates. The loans to associates which are repayable within one year were classified as current and were included in the Group's current assets.

As at 31 December 2016, impairment losses of HK$27,933,000 (2015: HK$29,940,000) have been recognised for the loans to associates. Impairment has been recognised for loans to associates because the associates have been loss-making in recent years.

The movements in the provision for impairment of the loans to associates are as follows:

	2016	**2015**
	HK$'000	*HK$'000*
At 1 January	29,940	86,750
Exchange realignment	(2,007)	(3,217)
Reversal of impairment loss *(note 6)*	—	(11,677)
Reclassified to other receivables *(note 26)*	—	(41,916)
At 31 December	27,933	29,940

Particulars of the material associate are as follows:

Name	**Particulars of issued shares held**	**Place of incorporation/ registration and business**	**Percentage of ownership interest attributable to the Group**	**Principal activities**
北京華信泰科技有限公司（「北京華信泰」）*	Registered capital of RMB1 each	PRC/Mainland China	35.6 (2015: 45)	Research and development of engineering technology and electronics communication technology

* Not audited by Ernst & Young, Hong Kong or another member firm of the Ernst & Young global network.

The above table lists the associates of the Group which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other associates would, in the opinion of the directors, result in particulars of excessive length.

The Group has discontinued the recognition of its share of losses of an associate, 星聯商務航空有限公司, because the share of losses of the associate exceeded the Group's interest in the associate and the Group has no obligation to take up further losses. The amounts of the Group's unrecognised share of losses of this associate for the current year and cumulatively were HK$10,574,000 (2015: HK$15,051,000) and HK$54,995,000 (2015: HK$44,421,000), respectively.

During the year, the Group's equity interest in 北京華信泰 has been diluted subsequent to the capital contribution by other shareholders of 北京華信泰. A gain on deemed disposal of an associate of HK$3,386,000 was recognised in the consolidated statement of profit or loss for the year.

During the year ended 31 December 2015, the Group's equity interests in two associates, AVIC Joy Holdings (HK) Limited ("AVIC Joy") and 上海藍沛新材料科技股份有限公司 ("上海藍沛"), had been diluted and the Group no longer had any significant influence over them. As such, the Group's investments in these two companies had been reclassified from investments in associates to available-for-sale investments, and the Group had discontinued to apply the equity method to share the results and other comprehensive income of these two companies. The reclassifications had been accounted for as disposals of the entire interests in AVIC Joy and 上海藍沛 and re-acquisitions of the retained interests at their fair values. As a result, an aggregate net gain on deemed disposal of associates of HK$433,380,000 had been recognised in the consolidated statement of profit or loss for the year ended 31 December 2015. Since then, the fully-impaired loans to 上海藍沛 were reclassified to other receivables.

The following table illustrates the aggregate financial information of the Group's associates that are not individually material:

	2016 *HK$'000*	2015 *HK$'000*
Share of the associates' losses for the year	(3,013)	(41,337)
Share of the associates' other comprehensive income	—	16,028
Share of the associates' total comprehensive income	(3,013)	(25,309)
Aggregate carrying amount of the Group's investments in the associates	13,378	24,146

19. FINANCIAL ASSET UNDER PROJECT EC120

The balance represents the carrying value of the Group's interest in 80% of the interest of AVIC International Holding Corporation ("AVIC International"), a substantial shareholder of the Company, in the net income in relation to Project EC120, a jointly-controlled operation established by AVIC International and certain independent third parties, to develop, manufacture and globally distribute the multi-purpose EC120 helicopters.

AVIC International's net income derived from Project EC120 is limited to AVIC International's share of income, net of all expenses, to be derived from its interest in Project EC120.

The investment represents a contractual right to receive cash in the future from another enterprise and has been classified as a non-current available-for-sale financial asset and stated at cost less any impairment losses because the range of reasonable fair value estimates is so significant that the directors are of the opinion that its fair value could not be measured reliably.

As at 31 December 2016, the directors has made a full provision for impairment of the value of the financial asset and the cost less accumulated impairment losses of the financial asset is analysed as follows:

	HK$'000
At 1 January 2015, 31 December 2015, 1 January 2016 and 31 December 2016:	
Cost	39,759
Accumulated impairment	(39,759)
Carrying amount	—

20. AVAILABLE-FOR-SALE INVESTMENTS

	2016 *HK$'000*	**2015** *HK$'000*
Non-current:		
Unlisted investments, at fair value:		
PMH Bonds *(note (a))*	83,420	70,998
AVIC Joy Bond *(note (b))*	45,744	43,445
Club debentures *(note (c))*	—	2,290
	129,164	116,733
Listed equity investment, at fair value *(note (d))*	149,581	283,688
Unlisted equity investment, at cost *(note (e))*	—	—
	278,745	400,421

Notes:

(a) Peace Map Holding Limited ("PMH") is a company whose shares are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). The convertible bonds issued by PMH ("PMH Convertible Bonds") held by the Group are non-interest-bearing, convertible into 400,000,000 ordinary shares of PMH at HK$0.25 per share (subject to adjustment upon the change in the capital structure of PMH) and will mature in five years from the date of the issuance.

PMH Convertible Bonds are hybrid instruments that include non-derivative host contracts and embedded derivatives. The non-derivative host contracts, representing the bond components ("PMH Bonds"), have been designated as available-for-sale investments. The embedded derivatives, representing the conversion options which allow the Group to convert PMH Convertible Bonds into ordinary shares of PMH at an established conversion rate (i.e., HK$0.25 per share), have been designated as derivative financial instruments ("PMH Derivatives") as detailed in note 21(a) to the financial statements.

During the year ended 31 December 2015, the Group had converted certain PMH Convertible Bonds ("PMH Converted CB") with a principal amount of HK$66,000,000 into 264,000,000 shares of PMH at the conversion price of HK$0.25 per share. On the date of the conversion, the market value of the shares of PMH received was HK$120,120,000 while the fair value of the PMH Converted CB was stated at HK$123,880,000 based on a valuation performed by an independent professionally qualified valuer. A loss on derecognition of HK$3,760,000 was resulted. At the same time, the corresponding fair value gain of HK$8,573,000 previously recorded in the statement of comprehensive income was released from the available-for-sale investment revaluation reserve. As a result, a net gain on derecognition of an available-for-sale investment of HK$4,813,000 was recognised in the consolidated statement of profit or loss for the year ended 31 December 2015.

As at 31 December 2016, the fair value of PMH Bonds was stated at HK$83,420,000 (2015: HK$70,998,000) based on a valuation performed by an independent professionally qualified valuer, and a fair value gain of HK$12,422,000 (2015: HK$2,381,000) in respect of PMH Bonds was recognised as other comprehensive income for the year ended 31 December 2016.

(b) AVIC Joy is a company whose shares are listed on the Stock Exchange. The convertible bond issued by AVIC Joy ("AVIC Joy Convertible Bond") bears interest at 2% per annum, is convertible into 225,112,487 ordinary shares of AVIC Joy at HK$0.23 per share (subject to adjustment upon the change in the capital structure of AVIC Joy) and will mature in three years from the date of the issuance.

AVIC Joy Convertible Bond is a hybrid instrument that includes a non-derivative host contract and an embedded derivative. The non-derivative host contract, representing the bond component ("AVIC Joy Bond"), has been designated as an available-for-sale investment. The embedded derivative, representing the conversion option which allows the Group to convert AVIC Joy Convertible Bond into ordinary shares of AVIC Joy at an established conversion rate (i.e., HK$0.23 per share) before the maturity date of AVIC Joy Convertible Bond, has been designated as a derivative financial instrument ("AVIC Joy Derivative") as detailed in note 21(b) to the financial statements.

During the year ended 31 December 2015, the maturity date of AVIC Joy Convertible Bond was extended from 6 March 2015 to 6 March 2018 as agreed by the Group and AVIC Joy, and the conversion rate was changed from HK$0.235 per share to HK$0.23 per share. On the date of the extension, the market value of the new AVIC Joy Convertible Bond was HK$76,691,000 while the fair value of the original AVIC Joy Convertible Bond was stated at HK$72,707,000 based on a valuation performed by an independent professionally qualified valuer. A gain on derecognition of the original AVIC Joy Convertible Bond of HK$3,984,000 was resulted. At the same time, the corresponding fair value gain of HK$10,518,000 previously recorded in the statement of other comprehensive income was released from the available-for-sale investment revaluation reserve. As a result, an aggregate net gain on derecognition of an available-for-sale investment of HK$14,502,000 was recognised in the consolidated statement of profit or loss for the year ended 31 December 2015.

As at 31 December 2016, the fair value of AVIC Joy Bond was stated at HK$45,744,000 (2015: HK$43,445,000) based on a valuation performed by an independent professionally qualified valuer, and a fair value gain of HK$2,299,000 (2015: HK$1,566,000) in respect of AVIC Joy Bond was recognised as other comprehensive income for the year ended 31 December 2016.

(c) During the year, the Group disposed of club debentures for cash consideration of HK$1,800,000. As a result, a fair value loss of HK$490,000 was recognised as other comprehensive income and the same fair value loss was then released from the available-for-sale investment revaluation reserve to the consolidated statement of profit or loss for the year.

(d) As detailed in note 18 to the financial statements, the Group's equity interest in AVIC Joy was diluted during the year ended 31 December 2015 and the Group's investment in AVIC Joy was reclassified to available-for-sale investment. This investment was designated as an available-for-sale financial asset and has no fixed maturity date or coupon rate.

During the year, a fair value loss of HK$134,107,000 (2015: HK$311,137,000) in respect of the Group's investment in AVIC Joy was recognised as other comprehensive income for the year.

There has been a significant decline in the market value of AVIC Joy shares during the year. The directors consider that such a decline indicates that the investment in AVIC Joy has been impaired and an impairment loss of HK$134,107,000 (2015: HK$311,137,000), which included a reclassification from other comprehensive income of HK$134,107,000 (2015: HK$311,137,000), has been recognised in the consolidated statement of profit or loss for the year.

(e) As detailed in note 18 to the financial statements, the Group's equity interest in 上海藍沛 was diluted during the year ended 31 December 2015 and the Group no longer had any significant influence over it. The Group's investment in 上海藍沛 was reclassified to available-for-sale investment. This investment was designated as an available-for-sale financial asset and has no fixed maturity date or coupon rate.

As at 31 December 2016, the investment in 上海藍沛 was stated at cost less impairment because the range of reasonable fair value estimates is so significant that the directors are of the opinion that its fair value cannot be measured reliably. The investment has been fully impaired in the prior year. The Group does not intend to dispose of it in the near future.

During the year, net fair value loss of HK$119,876,000 (2015: HK$307,190,000), in aggregate, in respect of the Group's available-for-sale investments was recognised as other comprehensive income for the year, of which fair value loss of HK$490,000 (2015: gain of HK$19,091,000) and HK$134,107,000 (2015: HK$311,137,000) were reclassified from other comprehensive income to the consolidated statement of profit or loss for the year on derecognition and impairment, respectively.

The fair values of certain of the unlisted available-for-sale investments have been estimated using valuation techniques based on assumptions that are supported by observable market prices or rates. The valuation requires the directors to make estimates about the expected future cash flows including expected future dividends, the risk-free rate and the credit spread of the underlying shares. The directors believe that the estimated fair values resulting from the valuation techniques, which are recorded in the consolidated statement of financial position, and the related changes in fair value, which are recorded in other comprehensive income, are reasonable, and that they were the most appropriate values at the end of the reporting period.

21. DERIVATIVE FINANCIAL INSTRUMENTS

	2016	2015
	HK$'000	*HK$'000*
Non-current assets:		
PMH Derivatives *(note (a))*	9,277	90,444
AVIC Joy Derivative *(note (b))*	2,061	29,452
	11,338	119,896

The Group's derivative financial instruments are managed and their performance is evaluated on a fair value basis. Any fair value gain or loss is recognised in the consolidated statement of profit or loss.

The fair values of the derivative financial instruments have been estimated using valuation techniques based on assumptions that are supported by observable market prices or rates. The valuations require the directors to make estimates, including expected cash flows and volatility of the underlying securities. The directors believe that the estimated fair values resulting from the valuation technique, which are recorded in the consolidated statement of financial position, and the related changes in fair value, which are recorded in the consolidated statement of profit or loss, are reasonable, and that they are the most appropriate values at the end of the reporting period.

Notes:

(a) The PMH Derivatives represent the derivatives embedded in PMH Convertible Bonds as detailed in note 20(a) to the financial statements.

As at 31 December 2016, the fair value of PMH Derivatives was stated at HK$9,277,000 (2015: HK$90,444,000) based on a valuation performed by an independent professionally qualified valuer, and a fair value loss of HK$81,167,000 (2015: gain of HK$40,868,000) in respect of PMH Derivatives was recognised in the consolidated statement of profit or loss for the year.

(b) AVIC Joy Derivative represents the derivative embedded in AVIC Joy Convertible Bond as detailed in note 20(b) to the financial statements. As at 31 December 2016, the fair value of AVIC Joy Derivative was stated at HK$2,061,000 (2015: HK$29,452,000) based on a valuation performed by an independent professionally qualified valuer, and a fair value loss of HK$27,391,000 (2015: HK$12,722,000) was recognised in the consolidated statement of profit or loss for the year.

During the year, aggregate fair value loss of HK$108,558,000 (2015: gain of HK$28,146,000) in respect of the Group's derivative financial instruments was recognised in the consolidated statement of profit or loss for the year.

22. PROPERTIES UNDER DEVELOPMENT AND COMPLETED PROPERTIES HELD FOR SALE

The analysis of the costs of the Group's properties under development and completed properties held for sale situated in the PRC is as follows:

	2016	**2015**
	HK$'000	*HK$'000*
Properties under development expected to be recovered:		
Within one year	1,239,303	—
After one year	2,150,603	3,334,352
	3,389,906	3,334,352
Properties held for sale	715,411	736,296
	4,105,317	4,070,648

At 31 December 2016, certain of the Group's properties under development with an aggregate carrying amount of approximately HK$1,658,082,000 were pledged to secure the banking facilities granted to the Group *(note 35(a))*.

23. INVENTORIES

	2016	**2015**
	HK$'000	*HK$'000*
Raw materials	—	930
Finished goods	—	3,634
	—	4,564

24. TRADE AND BILLS RECEIVABLES

	2016	2015
	HK$'000	*HK$'000*
Trade and bills receivables	89,620	188,763
Impairment	—	(11,685)
	89,620	177,078
Less: Trade receivable, non-current portion	(20,178)	(21,628)
Current portion	69,442	155,450

The Group has different credit policies for different business operations depending on the requirements of the markets and businesses in which the subsidiaries operate. Trade receivables from sale of properties in respect of the property development and investment business are payable pursuant to the terms of sale and purchase agreements. The Group's trading terms with its customers for the knitting and textile business and for the trading business are mainly on credit, except for new customers, where payment in advance is normally required. The credit period is generally one month, extending up to three months for major customers. Each customer has a maximum credit limit.

The Group seeks to maintain strict control over its outstanding receivables. Overdue balances are reviewed regularly by senior management. In view of the aforementioned and the fact that the Group's trade and bills receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. The Group does not hold any collateral or other credit enhancements over its trade receivable balances. Trade receivables are non-interest-bearing.

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

	2016	2015
	HK$'000	*HK$'000*
Within 1 month	2,089	168,800
1 to 2 months	—	1,184
2 to 3 months	—	2,858
Over 3 months	87,531	4,236
	89,620	177,078

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

	2016	2015
	HK$'000	*HK$'000*
At beginning of year	11,685	5,361
Disposal of a subsidiary	(11,685)	—
Impairment losses recognised	—	6,871
Exchange realignment	—	(547)
At end of year	—	11,685

Included in the above provision for impairment of trade and bills receivables as at 31 December 2015 was a provision for individually impaired trade and bills receivables of HK$11,685,000 with the same carrying amount before provision. The individually impaired trade and bills receivables related to customers that were in financial difficulties or were in default in principal payments and were not expected to be recovered.

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

	2016	2015
	HK$'000	*HK$'000*
Neither past due nor impaired	22,266	169,984
Less than 1 month past due	21,940	2,858
1 to 3 months past due	45,414	4,236
	89,620	177,078

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

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

25. LOANS TO RELATED COMPANIES

The loan to a related company represents the loan to 易拍全球(北京)科貿有限公司("易拍全球"), an associate of an intermediate holding company, which is unsecured, bears interest at 6.15% per annum and is repayable within one year.

As at 31 December 2015, the loans to related companies also included the loan to 北京勝和幢科技有限責任公司 ("北京勝和幢"), a subsidiary of the joint venture of the Group, which was unsecured, bore interest at 6.15% per annum and was repayable within one year; and the loan to 上海匯聯皆景信息技術有限公司("上海匯聯皆景"), an associate of the joint venture of the Group, which was unsecured, bore interest at 5.25% per annum and was repayable within one year. During the year, impairment losses of HK$12,608,000 *(note 6)* have been recognised for the loans to 北京勝和幢 and 上海匯聯皆景 because 北京勝和幢 has been loss-making in recent years and 上海匯聯皆景 was liquidated during the year ended 31 December 2016, and the related loans have then been written off.

Particulars of loans to related companies, disclosed pursuant to 383(1)(d) of the Hong Kong Companies Ordinance and Part 3 of the Companies (Disclosure of Information about Benefits of Directors) Regulation, are as follows:

	At 31 December 2016	Maximum amount outstanding during the year	At 31 December 2015 and 1 January 2016	Maximum amount outstanding during prior year	At 1 January 2015
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
易拍全球	16,760	16,760	16,272	18,750	18,750
北京勝和幢	—	958	958	1,000	1,000
上海匯聯皆景	—	11,976	11,976	11,976	—
	16,760		29,206		19,750
Less: Non-current portion	—		(11,976)		(18,750)
Current portion	16,760		17,230		1,000

26. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

	2016	2015
	HK$'000	*HK$'000*
Prepayments	27,571	50,530
Deposits and other receivables	52,516	85,376
Impairment	(37,109)	(73,914)
	42,978	61,992
Less: Prepayments, non-current portion	—	(278)
Current portion	42,978	61,714

Deposits and other receivables that were not impaired relate to receivables for which there is no recent history of default.

The movements in the provision for impairment of prepayments and other receivables are as follows:

	2016	2015
	HK$'000	*HK$'000*
At beginning of year	73,914	38,880
Disposal of a subsidiary	(38,501)	—
Reclassified from loans to an associate *(note 18)*	—	41,916
Impairment losses recognised/(reversed)	4,345	(6,152)
Exchange realignment	(2,649)	(730)
At end of year	37,109	73,914

Included in the above provision for impairment is a provision for individually impaired other receivables of HK$37,109,000 (2015: HK$40,312,000), with the same carrying amounts before provision. As at 31 December 2015, the provision for impairment of prepayments and other receivables also included full provision for impaired prepayments to suppliers of HK$15,331,000 and prepayments for an investment project of HK$18,271,000. Both the impaired prepayments to suppliers and for the investment project arose from the knitting and textile business. The impaired prepayments to suppliers related to suppliers that were in financial difficulties and were not expected to be recovered. The prepayment for the investment project was impaired as, in the opinion of the directors, its cost exceeded its recoverable amount.

27. EQUITY INVESTMENT AT FAIR VALUE THROUGH PROFIT OR LOSS

	2016	2015
	HK$'000	*HK$'000*
Listed equity investment, at market value	87,619	285,713

The above equity investment is managed and its performance is evaluated on a fair value basis. The Group designated this investment as a financial asset at fair value through profit or loss upon initial recognition.

28. PREPAID TAXES

Balance represents taxes and surcharges prepaid for the sales deposits received from pre-sales of properties in the PRC.

29. CASH AND CASH EQUIVALENTS AND PLEDGED DEPOSITS

	2016	2015
	HK$'000	*HK$'000*
Time deposits	298,710	12,335
Less: Pledged short term time deposits for short term banking facilities *(note 35(b)(iii))*	—	(359)
	298,710	11,976
Cash and bank balances	307,215	461,354
Cash and cash equivalents	605,925	473,330

At the end of the reporting period, the cash and bank balances and time deposits of the Group denominated in Renminbi amounted to HK$253,965,000 (2015: HK$120,275,000). The RMB is not freely convertible into other currencies, however, under Mainland China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.

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

30. BALANCES WITH NON-CONTROLLING SHAREHOLDERS OF SUBSIDIARIES

The balances are unsecured, non-interest-bearing and have no fixed terms of repayment.

31. BALANCES WITH AN INTERMEDIATE HOLDING COMPANY

The loans from an intermediate holding company are unsecured, bear interest at 6% (2015: 10%) per annum and are not repayable within one year.

The amount due from/to an intermediate holding company is unsecured, non-interest-bearing and has no fixed terms of repayment.

32. BALANCES WITH FELLOW SUBSIDIARIES

All amounts due from fellow subsidiaries are unsecured, non-interest-bearing and repayable within one year except that an amount due from a fellow subsidiary of HK$3,178,000 as at 31 December 2015 was repayable on 31 January 2017 and had been included in non-current assets as at 31 December 2015.

The amounts due to fellow subsidiaries are unsecured, non-interest-bearing and have no fixed terms of repayment.

The loans from fellow subsidiaries are unsecured and bear interest at 6% (2015: 10%) per annum.

The loans from a fellow subsidiary which are not repayable within one year were included in the Group's non-current liabilities. The loans from fellow subsidiaries which are repayable within one year were included in the Group's current liabilities.

33. TRADE AND BILLS PAYABLES

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

	2016	**2015**
	HK$'000	*HK$'000*
Within 1 month	10,249	80,197
1 to 2 months	28,005	2,307
2 to 3 months	—	1,841
Over 3 months	2,959	8,013
	41,213	92,358

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

34. OTHER PAYABLES AND ACCRUALS

	2016	2015
	HK$'000	*HK$'000*
Other payables	10,918	18,416
Accruals	6,305	14,328
	17,223	32,744

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

35. INTEREST-BEARING BANK BORROWINGS

	2016			2015		
	Effective interest rate (%)	**Maturity**	**HK$'000**	**Effective interest rate (%)**	**Maturity**	**HK$'000**
Current:						
Bank loans-secured	—	—	—	5.88-7.275	2016	37,964
Non-current:						
Bank loans-secured	5.4625	2018	230,134	—	—	—

Notes:

(a) As at 31 December 2016, the Group's banking facilities were secured by pledges of certain of the Group's properties under development with an aggregate carrying value of HK$1,658,082,000 (2015: Nil) *(note 22)*.

(b) As at 31 December 2015, the Group's banking facilities had also been secured by:

(i) a pledge of the Group's building in Mainland China with net book value of HK$3,148,000 *(note 13)*;

(ii) a pledge of the Group's leasehold land in Mainland China with net book value of HK$2,885,000 *(note 15)*;

(iii) pledges of certain of the Group's short term time deposits amounting to HK$359,000 *(note 29)*; and

(iv) pledges of certain properties owned by a director of a subsidiary, his spouse, his spouse's family member and his acquaintance.

As at 31 December 2015, a director of a subsidiary, the spouse of the director, the spouse's acquaintances and the companies controlled by the acquaintances had guaranteed repayment of certain of the Group's bank borrowings amounting to HK$23,952,000.

(c) All bank borrowings are denominated in RMB.

36. DEFERRED TAX

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

Deferred tax liabilities

	Revaluation of investment properties	**Fair value adjustments arising from acquisition of subsidiaries**	**Total**
	HK$'000	*HK$'000*	*HK$'000*
At 1 January 2015	—	262,583	262,583
Deferred tax charged/(credited) to the statement of profit or loss during the year	189	(66,385)	(66,196)
Exchange realignment	(7)	(9,179)	(9,186)
At 31 December 2015 and 1 January 2016	182	187,019	187,201
Disposal of a subsidiary *(note 41)*	—	(548)	(548)
Deferred tax credited to the statement of profit or loss during the year	(182)	(3,026)	(3,208)
Exchange realignment	—	(11,686)	(11,686)
Gross deferred tax liabilities at 31 December 2016	—	171,759	171,759

Deferred tax assets

	Revaluation of investment properties	Provision for LAT	Losses available for offsetting against future taxable profits	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January 2015	—	—	44,030	44,030
Deferred tax credited/(charged) to the statement of profit or loss during the year	—	6,002	(4,914)	1,088
Exchange realignment	—	(216)	(1,668)	(1,884)
At 31 December 2015 and 1 January 2016	—	5,786	37,448	43,234
Deferred tax credited to the statement of profit or loss during the year	8,330	473	3,264	12,067
Exchange realignment	(372)	(409)	(2,656)	(3,437)
Gross deferred tax assets at 31 December 2016	7,958	5,850	38,056	51,864

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

	2016	2015
	HK$'000	*HK$'000*
Net deferred tax assets recognised in the consolidated statement of financial position	10,025	9,685
Net deferred tax liabilities recognised in the consolidated statement of financial position	(129,920)	(153,652)
	(119,895)	(143,967)

At 31 December 2016, the Group had aggregate tax losses arising in Hong Kong of approximately HK$15,456,000 (2015: HK$15,456,000) that are available indefinitely for offsetting against future taxable profits of the companies in which the losses arose and tax losses arising in Mainland China of HK$14,934,000 (2015: HK$528,000) that will expire in one to five years for offsetting against future taxable profits. Deferred tax assets have not been recognised in respect of these losses as they have arisen in the companies that have been loss-making for some time and it is not considered probable that taxable profits will be available against which the tax losses can be utilised.

Pursuant to the PRC Corporate Income Tax Law, a 10% withholding tax is levied on dividends declared to foreign investors from the foreign investment enterprises established in Mainland China. The requirement is effective from 1 January 2008 and applies to earnings after 31 December 2007. A lower withholding tax rate may be applied if there is a tax treaty between Mainland China and the jurisdiction of the foreign investors. For the Group, the applicable rates range from 5% to 10%. The Group is therefore liable for withholding taxes on dividends distributed by those subsidiaries established in Mainland China in respect of earnings generated from 1 January 2008.

At 31 December 2016, no deferred tax has been recognised for withholding taxes that would be payable on the unremitted earnings that are subject to withholding taxes of the Group's subsidiaries, joint venture and associates established in Mainland China. In the opinion of the directors, it is not probable that these subsidiaries, joint venture and associates will distribute such earnings in the foreseeable future. As at 31 December 2016, the aggregate amount of temporary differences of approximately HK$117,573,000 (2015: HK$346,729,000) is associated with investments in subsidiaries in Mainland China for which deferred tax liabilities have not been recognised.

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

37. SHARE CAPITAL

Shares

	2016	**2015**
	HK$'000	*HK$'000*
Authorised:		
10,000,000,000 ordinary shares of HK$0.10 each	1,000,000	1,000,000
Issued and fully paid:		
5,519,591,000 ordinary shares of HK$0.10 each	551,959	551,959

38. SHARE OPTION SCHEME

At the annual general meeting held on 28 May 2014, the Company adopted a share option scheme (the "Scheme") for the purpose of providing incentives and rewards to eligible participants to contribute to the business development and growth of the Group and to enable the Group to recruit high-calibre employees and attract or retain human resources that are valuable to the Group. Since the adoption of the Scheme, no options have been granted, exercised, lapsed, cancelled or outstanding thereunder as at 31 December 2016.

Major terms of the Scheme include:

1. The purpose of the Scheme is to provide incentives to the participants.

2. The participants of the Scheme are any individual being employees, officers or consultants of the Company or any of its subsidiaries including any executive or non-executive directors thereof whether employed in Hong Kong or any part of the world.

3. The total number of shares of the Company (the "Shares") which may be issued upon exercise of all options to be granted under the Scheme, together with all options to be granted under any other share option schemes of any member of the Group, must not in aggregate represent more than 10% of the total number of the Shares in issue as at the date of adoption of the Scheme. The Company may refresh this 10% limit at any time subject to prior approval given by its shareholders at a general meeting. The overall limit on the total number of Shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the Scheme, together with all outstanding options granted and yet to be exercised under any other share option schemes of any member of the Group, must not exceed 30% of the total number of the Shares in issue from time to time. No options may be granted under the Scheme and any other share option schemes of any member of the Group if such grant will result in the said 30% limit being exceeded. As at the date of this annual report, the total number of securities available for issue under the Scheme is 461,959,100 Shares, representing approximately 8.37% of the total number of the Shares in issue as at the date of this annual report.

4. The total number of Shares issued and to be issued upon exercise of the options (whether exercised, cancelled or outstanding) granted or to be granted under the Scheme and any other share option schemes of the Company to each eligible participant under the Scheme in any 12-month period shall not exceed 1% of the total number of the Shares in issue as at the proposed grant date.

5. An option may be exercised in accordance with the terms of the Scheme at any time during a period of 10 years commencing on the date which the Board may determine at its discretion but such date shall not be earlier than three months after the date of the grant of such option is made.

6. An option granted shall remain open for acceptance by eligible participants for a period of 28 days from the date of the grant of such option together with a non-refundable payment of HK$1.00.

7. The exercise price of an option shall be the highest of:

   (a) the closing price of the Shares as stated in the Stock Exchange's daily quotation sheet on the date of the grant of the option, which must be a business day;

   (b) the average of the closing prices of the Shares as stated in the Stock Exchange's daily quotation sheets for the five business days immediately preceding the date of the grant (subject to acceptance) of the option; and

   (c) the nominal value of the Shares.

8. The Scheme shall be valid and effective for a period of 10 years commencing on 28 May 2014 and thereafter for as long as there are outstanding options granted and accepted pursuant thereto prior to the expiration of the said 10-year period and in order to give effect to the exercise of any such options.

Share options did not confer rights on the holders to dividends or to vote at shareholders' meetings.

At the end of the reporting period and at the date of approval of these financial statements, there were no share options outstanding (2015: Nil).

39. RESERVES

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity on pages 68 to 71 of this annual report.

Pursuant to the articles of association of certain subsidiaries operating as foreign-owned enterprises in Mainland China and the relevant PRC Company Law, the subsidiaries shall make an allocation from their profit after tax at the rate of 10% to the statutory surplus reserve fund, until such reserve reaches 50% of the registered capital of the subsidiaries. Part of the statutory surplus reserve may be capitalised as the subsidiaries' registered capital, provided that the remaining balance after the capitalisation is not less than 25% of the registered capital of the subsidiaries. The statutory reserve will be reclassified to retained profits upon the disposal of the subsidiaries.

40. PARTLY-OWNED SUBSIDIARY WITH MATERIAL NON-CONTROLLING INTERESTS

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

	2016	2015
Percentage of equity interest held by non-controlling interests of 大連航華	47.92%	47.92%

	2016 *HK$'000*	2015 *HK$'000*
Profit/(loss) for the year allocated to non-controlling interests of 大連航華	(20,560)	48,775
Dividend paid to non-controlling interests of 大連航華	—	—
Accumulated balances of non-controlling interests of 大連航華 at the reporting date	548,868	611,218

The following table illustrates the summarised financial information of the above subsidiary. The amounts disclosed are before any inter-company eliminations:

大連航華

	2016 *HK$'000*	2015 *HK$'000*
Revenue	102,786	2,147,344
Cost of sales and total expenses	(145,691)	(2,045,561)
Profit/(loss) for the year	(42,905)	101,783
Total comprehensive income for the year	(130,113)	45,969
Current assets	3,424,363	3,314,071
Non-current assets	368,913	430,767
Current liabilities	(1,606,924)	(625,068)
Non-current liabilities	(1,040,968)	(1,844,273)
Net cash flows from operating activities	553,053	159,470
Net cash flows from investing activities	—	—
Net cash flows from financing activities	(414,003)	(152,375)
Net increase in cash and cash equivalents	139,050	7,095

41. DISPOSAL OF A SUBSIDIARY

During the year, the Group disposed of its 51% equity interest in Zhejiang Dongyang Jinniu. An analysis of the disposal is as follows:

	Notes	2016 HK$'000	2015 HK$'000
Net assets disposed of:			
Property, plant and equipment	13	3,528	—
Prepaid land lease payments	15	2,872	—
Intangible asset	16	285	—
Inventories		4,062	—
Trade receivables		3,151	—
Prepayments, deposits and other receivables		2,174	—
Pledged time deposits		3,174	—
Cash and cash equivalents		1,934	—
Due to a non-controlling shareholder of a subsidiary		(18)	—
Trade and bills payables		(13,420)	—
Other payables and accruals		(19,017)	—
Interest-bearing bank borrowings		(37,964)	—
Tax payable	36	(371)	—
Deferred tax liabilities		(548)	—
Non-controlling interests		24,578	—
		(25,580)	—
Exchange fluctuation reserve		(1,223)	—
		(26,803)	—
Gain on disposal of a subsidiary	11	32,453	—
		5,650	—
Satisfied by:			
Cash		5,650	—

An analysis of the net inflow of cash and cash equivalents in respect of the disposal of a subsidiary is as follows:

	2016	2015
	HK$'000	*HK$'000*
Cash consideration	5,650	—
Cash and bank balances disposed of	(1,934)	—
Net inflow of cash and cash equivalents in respect of the disposal of a subsidiary	3,716	—

42. OPERATING LEASE ARRANGEMENTS

(a) As lessor

The Group leases its investment properties (note 14 to the financial statements) under operating lease arrangements, with leases negotiated for terms ranging from 1 to 10 years. The terms of the leases generally also require the tenants to pay security deposits and provide for periodic rent adjustments according to the then prevailing market conditions.

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

	2016	2015
	HK$'000	*HK$'000*
Within one year	19,441	11,908
In the second to fifth years, inclusive	39,724	19,483
After five years	7,385	9,757
	66,550	41,148

(b) As lessee

The Group leases certain of its office premises under non-cancellable operating lease arrangements with terms ranging from one to three years.

At the end of the reporting period, the Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	2016	2015
	HK$'000	*HK$'000*
Within one year	—	3,677
In the second to fifth years, inclusive	—	1,367
	—	5,044

43. COMMITMENTS

In addition to the operating lease commitments in note 42(b) above, the Group had the following commitments at the end of the reporting period:

	2016	2015
	HK$'000	*HK$'000*
Contracted, but not provided for:		
Establishment of a joint venture *(note)*	—	47,904
Property development expenditure	328,655	338,402
	328,655	386,306

Note:

On 4 January 2006, Sino-Aviation Investments, a wholly-owned subsidiary of the Company, entered into a joint venture agreement (the "JV Agreement") with AVIC International, a substantial shareholder of the Company, and Chengdu Aircraft Industry (Group) Corporation Ltd. ("Chengdu Aircraft"), for the establishment of a joint venture to engage in the research and development, design and manufacture of parts and components for commercial aircraft, and provision of related technical services. According to the JV Agreement, the total registered capital of the joint venture was RMB100 million (equivalent to approximately HK$120 million), of which 40%, 15% and 45% respectively, would be contributed by Sino-Aviation Investments, AVIC International and Chengdu Aircraft. The JV Agreement was conditional upon (i) the internal approval obtained by each of the three parties; and (ii) the approval from the relevant PRC authorities. As at 31 December 2015, the JV Agreement had not become effective as the conditions stated above had not been fulfilled.

During the year, all parties entered into a termination agreement to terminate the JV Agreement, details of which have been disclosed in the Company's announcement dated 30 September 2016.

44. CONTINGENT LIABILITIES

At the end of the reporting period, contingent liabilities not provided for in the financial statements were as follows:

	2016	2015
	HK$'000	*HK$'000*
Guarantee given to banks for housing loans extended by the banks to the purchasers of the Group's properties for a period from the date of loans being granted to the purchasers up to the date of issuance of property title certificates to the purchasers	76,085	36,489

The fair value of the guarantees is not significant and the directors consider that in case of default in payments by the purchasers, the net realisable value of the related properties will be sufficient to cover the repayment of the outstanding loan principals together with the accrued interests and penalties and therefore no provision for the guarantees has been made in the financial statements for the year ended 31 December 2016 (2015: Nil).

45. RELATED PARTY TRANSACTIONS

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

		2016	2015
	Notes	*HK$'000*	*HK$'000*
Interest income on loans to related companies	(i)	1,076	1,994
Interest income on loans to associates	(ii)	577	1,229
Fellow subsidiaries:			
Interest expense on loans from fellow subsidiaries	(iii)	(130,038)	(225,058)
Management fee paid to a fellow subsidiary	(iv)	(6,619)	(6,178)
Agency fee paid to a fellow subsidiary	(iv)	(177)	—
Purchases of materials	(v)	(8,035)	—
Interest expenses on loans from an intermediate holding company	(vi)	(7,548)	(14,691)

Notes:

(i) Details of the loans to related companies are set out in note 25 to the financial statements.

(ii) Details of the loans to associates are set out in note 18 to the financial statements.

(iii) Details of the loans from fellow subsidiaries are set out in note 32 to the financial statements.

(iv) The management fee and agency fee paid to fellow subsidiaries are determined between the Group and the fellow subsidiary.

(v) The cost of purchases from a fellow subsidiary was made at pre-determined prices agreed between the parties.

(vi) Details of the loans from an intermediate holding company are set out in note 31 to the financial statements.

(b) Outstanding balances with related parties:

(i) Details of the Group's loans to associates are disclosed in note 18 to the financial statements.

(ii) Details of the Group's loans to related companies are disclosed in note 25 to the financial statements.

(iii) Details of the Group's balances with non-controlling shareholders of subsidiaries are disclosed in note 30 to the financial statements.

(iv) Details of the Group's balances with an intermediate holding company are disclosed in note 31 to the financial statements.

(v) Details of the Group's balances with fellow subsidiaries are disclosed in note 32 to the financial statements.

(c) Compensation of key management personnel of the Group:

	2016	**2015**
	HK$'000	*HK$'000*
Short term employee benefits	370	3,262
Post-employment benefits	14	183
Total compensation paid to key management personnel	384	3,445

Further details of directors' emoluments are included in note 8 to the financial statements.

The related party transactions in respect of item (a)(iv) above also constitute continuing connected transactions as defined in Chapter 14A of the Listing Rules.

46. FINANCIAL INSTRUMENTS BY CATEGORY

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

2016

Financial assets

	Financial assets at fair value through profit or loss-held for trading	Loans and receivables	Available-for-sale financial assets	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Loans to associates	—	9,497	—	9,497
Available-for-sale investments	—	—	278,745	278,745
Derivative financial instruments	11,338	—	—	11,338
Trade and bills receivables	—	89,620	—	89,620
Due from fellow subsidiaries	—	10,960	—	10,960
Loans to related companies	—	16,760	—	16,760
Due from an intermediate holding company	—	5,282	—	5,282
Financial assets included in prepayments, deposits and other receivables	—	15,407	—	15,407
Equity investment at fair value through profit or loss	87,619	—	—	87,619
Cash and cash equivalents	—	605,925	—	605,925
	98,957	753,451	278,745	1,131,153

Financial liabilities

	Financial liabilities at amortised cost
	HK$'000
Due to non-controlling shareholders of subsidiaries	88,444
Due to fellow subsidiaries	1,643
Loans from fellow subsidiaries	1,234,637
Trade and bills payables	41,213
Other payables and accruals	17,223
Interest-bearing bank borrowings	230,134
Loans from an intermediate holding company	475,419
	2,088,713

2015

Financial assets

	Financial assets at fair value through profit or loss-held for trading	**Loans and receivables**	**Available-for-sale financial assets**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Loans to associates	—	10,180	—	10,180
Available-for-sale investments	—	—	400,421	400,421
Derivative financial instruments	119,896	—	—	119,896
Trade and bills receivables	—	177,078	—	177,078
Due from fellow subsidiaries	—	49,194	—	49,194
Loans to related companies	—	29,206	—	29,206
Due from non-controlling shareholder of a subsidiary	—	323	—	323
Financial assets included in prepayments, deposits and other receivables	—	45,064	—	45,064
Equity investment at fair value through profit or loss	285,713	—	—	285,713
Pledged time deposits	—	359	—	359
Cash and cash equivalents	—	473,330	—	473,330
	405,609	784,734	400,421	1,590,764

Financial liabilities

	Financial liabilities at amortised cost
	HK$'000
Due to non-controlling shareholders of subsidiaries	64,301
Due to an intermediate holding company	14,164
Due to fellow subsidiaries	4
Loans from fellow subsidiaries	1,864,671
Trade and bills payables	92,358
Other payables and accruals	31,892
Interest-bearing bank borrowings	37,964
Loans from an intermediate holding company	509,581
	2,614,935

47. FAIR VALUE AND FAIR VALUE HIERARCHY OF FINANCIAL INSTRUMENTS

The carrying amounts and fair values of the Group's financial instruments, other than those with carrying amounts that reasonably approximate to fair values, are as follows:

	Carrying amounts		Fair values	
	2016	**2015**	**2016**	**2015**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Financial assets				
Trade receivable (non-current portion)	20,178	21,628	18,862	19,356
Due from a fellow subsidiary (non-current portion)	—	3,178	—	3,022
Loans to associates (non-current portion)	—	10,180	—	10,373
Loans to related companies (non-current portion)	—	11,976	—	12,065
Available-for-sale investments	278,745	400,421	278,745	400,421
Equity investment at fair value through profit or loss	87,619	285,713	87,619	285,713
Derivative financial instruments	11,338	119,896	11,338	119,896
	397,880	852,992	396,564	850,846
Financial liabilities				
Loans from a fellow subsidiary (non-current portion)	648,045	1,658,683	646,682	1,791,586
Interest-bearing bank borrowings (non-current portion)	230,134	—	227,430	—
Loans from an intermediate holding company	475,419	509,581	473,114	607,026
	1,353,598	2,168,264	1,347,226	2,398,612

Management has assessed that the fair values of trade and bills receivables (current portion), balances with fellow subsidiaries (current portion), an intermediate holding company, non-controlling shareholders of subsidiaries, associates (current portion) and related companies (current portion), financial assets included in prepayments, deposits and other receivables, pledged time deposits, cash and cash equivalents, trade and bills payables, other payables and accruals and interest-bearing bank borrowings (current portion) approximate to their carrying amounts largely due to the short term maturities of these instruments.

The Group's finance department headed by the chief financial officer is responsible for determining the policies and procedures for the fair value measurement of financial instruments. At each reporting date, the finance department analyses the movements in the values of financial instruments and determines the major inputs applied in the valuation. The valuation is reviewed and approved by the chief financial officer and then reported to the chief executive officer. The valuation process and results are discussed with the audit committee twice a year for interim and annual financial reporting.

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

The following methods and assumptions were used to estimate the fair values:

The fair values of the non-current portion of trade receivables, loans to related companies, loans from a fellow subsidiary, interest-bearing bank borrowings and loans from an intermediate holding company have been calculated by discounting the expected future cash flows using rates currently available for instruments with similar terms, credit risk and remaining maturities. The Group's own non-performance risk for loans from a fellow subsidiary, interest-bearing bank borrowings and loans from an intermediate holding company as at 31 December 2016 was assessed to be insignificant.

The fair values of listed equity investments are based on quoted market prices. The fair values of unlisted available-for-sale investments and derivative financial instruments, including PMH Derivatives and AVIC Joy Derivative, have been estimated using a valuation technique based on assumptions that are supported by observable market prices or rates. The directors believe that the estimated fair values resulting from the valuation technique, which are recorded in the consolidated statement of financial position, and the related changes in fair values, which are recorded in other comprehensive income and consolidated statement of profit or loss, are reasonable, and that they were the most appropriate values at the end of the reporting period.

The Group enters into derivative financial instruments with various counterparties. Derivative financial instruments were measured using valuation models which incorporate various market observable inputs including the credit quality of counterparties and interest rate curves. The carrying amounts of derivative financial instruments were the same as their fair values. As at 31 December 2016, the marked to market value of the above derivative asset position was net of a credit valuation adjustment attributable to derivative counterparty default risk.

Fair value hierarchy

The following tables illustrate the fair value measurement hierarchy of the Group's financial instruments:

Assets measured at fair value:

	Fair value measurement using			
	Quoted prices in active markets (Level 1)	**Significant observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
As at 31 December 2016				
Available-for-sale investments:				
Equity investments	149,581	—	—	149,581
Debt investments	—	129,164	—	129,164
Equity investment at fair value through profit or loss	87,619	—	—	87,619
Derivative financial instruments	—	11,338	—	11,338
	237,200	140,502	—	377,702
As at 31 December 2015				
Available-for-sale investments:				
Equity investments	283,688	—	—	283,688
Debt investments	2,290	114,443	—	116,733
Equity investment at fair value through profit or loss	285,713	—	—	285,713
Derivative financial instruments	—	119,896	—	119,896
	571,691	234,339	—	806,030

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

During the year, there were no transfers of fair value measurements between Level 1 and Level 2 and no transfers into or out of Level 3 for both financial assets and financial liabilities (2015: Nil).

Assets for which fair values are disclosed:

	Fair value measurement using			
	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
As at 31 December 2016				
Trade receivable (non-current portion)	—	18,862	—	18,862
As at 31 December 2015				
Trade receivable (non-current portion)	—	19,356	—	19,356
Due from a fellow subsidiary (non-current portion)	—	3,022	—	3,022
Loans to associates	—	10,373	—	10,373
Loans to related companies (non-current portion)	—	12,065	—	12,065
	—	44,816	—	44,816

Liabilities for which fair values are disclosed:

	Fair value measurement using			
	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
As at 31 December 2016				
Loans from a fellow subsidiary (non-current portion)	—	646,682	—	646,682
Interest-bearing bank borrowings (non-current portion)	—	227,430	—	227,430
Loans from an intermediate holding company	—	473,114	—	473,114
	—	1,347,226	—	1,347,226
As at 31 December 2015				
Loans from a fellow subsidiary (non-current portion)	—	1,791,586	—	1,791,586
Loans from an intermediate holding company	—	607,026	—	607,026
	—	2,398,612	—	2,398,612

48. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

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

The main risks arising from the Group's financial instruments are foreign currency risk, interest rate risk, credit risk, liquidity risk and equity price risk. The board of directors reviews and agrees policies for managing each of these risks and they are summarised below.

Foreign currency risk

The Group's foreign currency exposures primarily arise from certain sales or purchases by operating units in currencies other than the units' functional currencies. In view of the fact that the Group tries to match its assets and liabilities with the same currency, the Group's exposure to foreign currency risk is minimal.

Interest rate risk

The Group has no significant interest rate risk because the Group's interest-bearing debts, including loans from fellow subsidiaries and an intermediate holding company and interest-bearing bank borrowings, are arranged on a fixed rate basis. During the Track Record Period, the Group has not used any financial instruments to hedge its exposure to interest-rate risk.

Credit risk

The Group trades only with recognised and creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis and the Group's exposure to bad debts is not significant.

The credit risk of the Group's other financial assets, which comprise cash and cash equivalents, time deposit with original maturity of more than three months, pledged time deposits, available-for-sale investments, derivative financial instruments, deposits and other receivables, an amount due from non-controlling shareholder of a subsidiary, and loans to associates and related companies, arises from default of the counterparty, with a maximum exposure equal to the carrying amounts of these instruments.

Since the Group trades only with recognised and creditworthy third parties, there is no requirement for collateral. Concentrations of credit risk are managed by customer/counterparty, by geographical region and by industry sector. There are no significant concentrations of credit risk within the Group as the customer bases of the Group's trade and bills receivables are widely dispersed in different sectors and industries.

Further quantitative data in respect of the Group's exposure to credit risk arising from trade and bills receivables are disclosed in note 24 to the financial statements.

Liquidity risk

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

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank loans and loans from fellow subsidiaries and an intermediate holding company. The Group's policy is to minimise borrowings.

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

	2016				
	On demand	**Less than 3 months**	**3 to less than 12 months**	**1-5 years**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Due to non-controlling shareholders of subsidiaries	88,444	—	—	—	88,444
Due to fellow subsidiaries	717	—	926	—	1,643
Loans from fellow subsidiaries	—	566,006	30,922	707,765	1,304,693
Trade and bills payables	—	41,213	—	—	41,213
Other payables and accruals	—	17,223	—	—	17,223
Interest-bearing bank borrowings	—	3,143	12,571	242,705	258,419
Loans from an intermediate holding company	—	7,131	21,394	553,863	582,388
Guarantee given to banks *(note 44)*	76,085	—	—	—	76,085
	165,246	634,716	65,813	1,504,333	2,370,108

	2015				
	On demand	Less than 3 months	3 to less than 12 months	1-5 years	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Due to non-controlling shareholders of subsidiaries	64,301	—	—	—	64,301
Due to an intermediate holding company	14,164	—	—	—	14,164
Due to fellow subsidiaries	4	—	—	—	4
Loans from fellow subsidiaries	—	46,617	335,539	1,807,322	2,189,478
Trade and bills payables	—	84,345	8,013	—	92,358
Other payables and accruals	—	31,892	—	—	31,892
Interest-bearing bank borrowings	—	609	39,238	—	39,847
Loans from an intermediate holding company	—	12,739	38,219	700,674	751,632
Guarantee given to banks *(note 44)*	36,489	—	—	—	36,489
	114,958	176,202	421,009	2,507,996	3,220,165

Equity price risk

Equity price risk is the risk that the fair values of financial instruments decrease as a result of changes in the levels of equity indices and the value of individual securities. The Group is exposed to equity price risk arising from a listed equity investment classified as trading equity investment *(note 27)* as at 31 December 2016. The Group's listed equity investment is listed on the Stock Exchange and is valued at quoted market price at the end of the reporting period.

The market equity index for the following stock exchange, at the close of business of the nearest trading day in the year to the end of the reporting period, and its respective highest and lowest points during the year was as follows:

	31 December 2016	High/low 2016	31 December 2015	High/low 2015
Hong Kong-Hang Seng Index	22,001	22,070/21,819	21,914	21,970/21,864

The following table demonstrates the sensitivity to every 1% change in the fair values of the listed equity investments and the underlying equity investments of the derivative financial instruments, with all other variables held constant and before any impact on tax, based on their carrying amounts at the end of the reporting period.

	Carrying amount of financial instruments	**Increase/ (decrease) in profit before tax**	**Increase/ (decrease) in equity***
	HK$'000	*HK$'000*	*HK$'000*
2016			
Investment listed in Hong Kong			
— Available-for-sale investment	149,581	—	1,496/(1,496)
— Equity investment at fair value through profit or loss	87,619	877/(877)	—
PMH Derivatives	9,277	176/(176)	—
AVIC Joy Derivative	2,061	70/(155)	—
2015			
Investment listed in Hong Kong			
— Available-for-sale investment	283,688	—	2,837/(2,837)
— Equity investment at fair value through profit or loss	285,713	2,857/(2,857)	—
PMH Derivatives	90,444	1,130/(1,130)	—
AVIC Joy Derivative	29,452	342/(3)	—

* Excluding retained profits

Capital management

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

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

The Group monitors capital using a gearing ratio, which is the interest-bearing debts divided by equity attributable to owners of the parent plus the interest-bearing debt. Interest-bearing debts include loans from fellow subsidiaries, interest-bearing bank borrowings and loans from an intermediate holding company.

The gearing ratios as at the end of the reporting periods were as follows:

	2016	**2015**
	HK$'000	*HK$'000*
Loans from fellow subsidiaries	1,234,637	1,864,671
Interest-bearing bank borrowings	230,134	37,964
Loans from an intermediate holding company	475,419	509,581
Interest-bearing debts	1,940,190	2,412,216
Equity attributable to owners of the parent	1,973,272	2,737,534
Equity attributable to owners of the parent plus the interest-bearing debts	3,913,462	5,149,750
Gearing ratio	50%	47%

49. STATEMENT OF FINANCIAL POSITION OF THE COMPANY

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

	2016	2015
	HK$'000	*HK$'000*
NON-CURRENT ASSETS		
Property, plant and equipment	23,211	24,411
Investments in subsidiaries	1,726,465	849,550
Total non-current assets	1,749,676	873,961
CURRENT ASSETS		
Prepayments, deposits and other receivables	840	4,016
Due from a subsidiary	955	954
Cash and cash equivalents	346,020	320,589
Total current assets	347,815	325,559
CURRENT LIABILITIES		
Other payables and accruals	2,358	3,302
NET CURRENT ASSETS	345,457	322,257
Net assets	2,095,133	1,196,218
EQUITY		
Issued capital	551,959	551,959
Reserves *(Note)*	1,543,174	644,259
Total equity	2,095,133	1,196,218

Note:

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

	Share premium account	Contributed surplus	Retained profits	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January 2015	609,080	5,243	96,944	711,267
Total comprehensive income for the year	—	—	(67,008)	(67,008)
At 31 December 2015 and 1 January 2016	609,080	5,243	29,936	644,259
Total comprehensive income for the year	—	—	898,915	898,915
At 31 December 2016	609,080	5,243	928,851	1,543,174

The contributed surplus of the Company represents the excess of the consolidated net asset value of Far East Aluminium (B.V.I.) Limited on 20 November 1991, when its entire issued share capital was acquired by the Company pursuant to a group reorganisation, over the nominal amount of the Company's shares issued in consideration for such acquisition, net of accumulated losses of the Company set off in the prior years. Under the Companies Act of 1981 of Bermuda, the contributed surplus of the Company is distributable to shareholders under certain circumstances.

The Company's share premium account of HK$609,080,000 (2015: HK$609,080,000) as at 31 December 2016 may be distributed in the form of fully paid bonus shares.

50. COMPARATIVE AMOUNTS

The comparative consolidated statement of profit or loss has been re-presented as if the operation discontinued during the current year had been discontinued at the beginning of the comparative period *(note 11)*.

51. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 14 March 2017.

IV. UNAUDITED FINANCIAL STATEMENTS FOR 1H2017

The following information is extracted from the unaudited financial statements of the Group as set out in the interim report of the Company for 1H2017.

INTERIM FINANCIAL INFORMATION

CONDENSED CONSOLIDATED STATEMENT OF PROFIT OR LOSS

		For the six months ended 30 June	
		2017	**2016**
		(Unaudited)	*(Unaudited)*
	Notes	*HK$'000*	*HK$'000*
CONTINUING OPERATIONS			
Revenue	3	29,740	64,587
Cost of sales		(20,980)	(36,028)
Gross profit		8,760	28,559
Other income	4	4,570	9,846
Selling and distribution expenses		(14,716)	(8,927)
Administrative expenses		(31,511)	(24,106)
Other operating expenses	6	(347)	(934)
Finance costs	5	(22,089)	(38)
Gain on disposal of convertible loans		87,151	—
Gain on deemed disposal of interest in an associate		—	3,386
Share of profits and losses of:			
Joint venture		(9,934)	(43,232)
Associates		(1,113)	(2,623)
Impairment of an available-for-sale investment (transfer from available-for- sale investment revaluation reserve)		(48,485)	(94,907)
Fair value loss on derivative financial instruments		(11,086)	(72,027)
Fair value loss on equity investment at fair value through profit or loss		(25,905)	(137,904)
Loss before tax from continuing operations	6	(64,705)	(342,907)
Income tax expense	7	(2,302)	(5,761)
Loss for the period from continuing operations		(67,007)	(348,668)

	Notes	For the six months ended 30 June 2017 (Unaudited) HK$'000	2016 (Unaudited) HK$'000
DISCONTINUED OPERATION			
Loss for the period from a discontinued operation	8	—	(5,091)
LOSS FOR THE PERIOD		(67,007)	(353,759)
Attributable to:			
Owners of the parent		(57,374)	(353,498)
Non-controlling interests		(9,633)	(261)
		(67,007)	(353,759)
LOSS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT	9		
Basic and diluted			
— For loss for the period		(HK1.04 cents)	(HK6.40 cents)
— For loss from continuing operations		(HK1.04 cents)	(HK6.36 cents)

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	For the six months ended 30 June	
	2017	2016
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
LOSS FOR THE PERIOD	(67,007)	(353,759)
OTHER COMPREHENSIVE INCOME		
Other comprehensive income to be reclassified to profit or loss in subsequent periods:		
Available-for-sale investments:		
Changes in fair value	(37,212)	(89,224)
Reclassification adjustment for losses included in the condensed consolidated statement of profit or loss		
— Impairment loss	48,485	94,907
	11,273	5,683
Share of other comprehensive income of a joint venture	1,468	—
Exchange differences on translation of foreign operations	59,570	(33,077)
NET OTHER COMPREHENSIVE INCOME TO BE RECLASSIFIED TO PROFIT OR LOSS IN SUBSEQUENT PERIODS AND OTHER COMPREHENSIVE INCOME FOR THE PERIOD, NET OF TAX	72,311	(27,394)
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD	5,304	(381,153)
Attributable to:		
Owners of the parent	(5,040)	(370,392)
Non-controlling interests	10,344	(10,761)
	5,304	(381,153)

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Note	30 June 2017 (Unaudited) HK$'000	31 December 2016 (Audited) HK$'000
NON-CURRENT ASSETS			
Property, plant and equipment		23,425	24,975
Investment properties		325,391	315,866
Investment in a joint venture		50,137	58,602
Investments in associates		12,265	13,378
Financial asset under Project EC120		—	—
Available-for-sale investments		192,897	278,745
Derivative financial instruments		68	11,338
Trade receivable	11	—	20,178
Deferred tax assets		10,327	10,025
Total non-current assets		614,510	733,107
CURRENT ASSETS			
Properties under development and completed properties held for sale		4,326,947	4,105,317
Trade receivables	11	88,307	69,442
Due from fellow subsidiaries		2,646	10,960
Due from an intermediate holding company		—	5,282
Loans to associates		9,783	9,497
Loan to a related company		17,265	16,760
Prepayments, deposits and other receivables		45,575	42,978
Available-for-sale investments		48,636	—
Derivative financial instruments		184	—
Equity investment at fair value through profit or loss		61,714	87,619
Prepaid taxes		23,078	16,186
Cash and cash equivalents		670,377	605,925
Total current assets		5,294,512	4,969,966

	Note	30 June 2017 (Unaudited) HK$'000	31 December 2016 (Audited) HK$'000
CURRENT LIABILITIES			
Due to non-controlling shareholders of subsidiaries		117,783	88,444
Due to an intermediate holding company		7,535	—
Due to fellow subsidiaries		2,969	1,643
Loans from a fellow subsidiary		621,547	586,592
Trade payables	12	35,178	41,213
Other payables and accruals		22,217	17,223
Customer deposits		1,367,722	920,238
Tax payable		36,954	37,449
Total current liabilities		2,211,905	1,692,802
NET CURRENT ASSETS		3,082,607	3,277,164
TOTAL ASSETS LESS CURRENT LIABILITIES		3,697,117	4,010,271
NON-CURRENT LIABILITIES			
Loans from an intermediate holding company		489,756	475,419
Loans from a fellow subsidiary		540,976	648,045
Interest-bearing bank borrowings		—	230,134
Deferred tax liabilities		134,328	129,920
Total non-current liabilities		1,165,060	1,483,518
Net assets		2,532,057	2,526,753
EQUITY			
Equity attributable to owners of the parent			
Issued capital		551,959	551,959
Reserves		1,416,273	1,421,313
		1,968,232	1,973,272
Non-controlling interests		563,825	553,481
Total equity		2,532,057	2,526,753

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Attributable to owners of the parent								
	Issued capital	Share premium account	Available-for-sale investment revaluation reserve	Reserve fund	Exchange fluctuation reserve	Retained profits	Total	Non-controlling interests	Total equity
	(Unaudited)	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January 2017	551,959	609,080	25,386	18,505	(116,340)	884,682	1,973,272	553,481	2,526,753
Loss for the period	—	—	—	—	—	(57,374)	(57,374)	(9,633)	(67,007)
Other comprehensive income for the period:									
Changes in fair value of available-for-sale investments, net of tax	—	—	11,273	—	—	—	11,273	—	11,273
Share of other comprehensive income of a joint venture	—	—	—	—	1,468	—	1,468	—	1,468
Exchange differences on translation of foreign operations	—	—	—	—	39,593	—	39,593	19,977	59,570
Total comprehensive income for the period	—	—	11,273	—	41,061	(57,374)	(5,040)	10,344	5,304
At 30 June 2017	551,959	609,080*	36,659*	18,505*	(75,279)*	827,308*	1,968,232	563,825	2,532,057

* These reserve accounts comprise the consolidated reserves of HK$1,416,273,000 in the condensed consolidated statement of financial position as at 30 June 2017.

	Attributable to owners of the parent								
	Issued capital	**Share premium account**	**Available-for-sale investment revaluation reserve**	**Reserve fund**	**Exchange fluctuation reserve**	**Retained profits**	**Total**	**Non-controlling interests**	**Total equity**
	(Unaudited)	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*	*(Unaudited)*
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January 2016	551,959	609,080	10,665	18,477	(23,199)	1,570,552	2,737,534	594,124	3,331,658
Loss for the period	—	—	—	—	—	(353,498)	(353,498)	(261)	(353,759)
Other comprehensive income for the period:									
Changes in fair value of available-for-sale investments, net of tax	—	—	5,683	—	—	—	5,683	—	5,683
Exchange differences on translation of foreign operations	—	—	—	—	(22,577)	—	(22,577)	(10,500)	(33,077)
Total comprehensive income for the period	—	—	5,683	—	(22,577)	(353,498)	(370,392)	(10,761)	(381,153)
At 30 June 2016	551,959	609,080	16,348	18,477	(45,776)	1,217,054	2,367,142	583,363	2,950,505

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

		For the six months ended 30 June	
		2017	**2016**
		(Unaudited)	*(Unaudited)*
	Notes	*HK$'000*	*HK$'000*
CASH FLOWS FROM OPERATING ACTIVITIES			
Loss before tax:			
From continuing operations		(64,705)	(342,907)
From a discontinued operation	8	—	(5,075)
Adjustments for:			
Finance costs	5, 8	22,089	1,226
Share of profits and losses of a joint venture and associates		11,047	45,855
Bank interest income		(3,091)	(818)
Interest income on a convertible bond		(518)	(518)
Interest income on loans to associates		(282)	(284)
Interest income on loans to related companies		(511)	(833)
Gain on disposal of convertible loans		(87,151)	—
Gain on deemed disposal of interest in an associate		—	(3,386)
Depreciation		681	1,462
Amortisation of customer relationship		—	95
Recognition of prepaid land lease payments		—	13
Provision for impairment of a loan to a related company		—	934
Provision for impairment of prepayments and other receivables		—	4,112
Loss on disposal of items of property, plant and equipment		347	—
Impairment of an available-for-sale investment		48,485	94,907
Fair value loss on derivative financial instruments		11,086	72,027
Fair value loss on equity investment at fair value through profit or loss		25,905	137,904
		(36,618)	4,714
Increase in properties under development and completed properties held for sale		(50,019)	(98,302)
Decrease in inventories		—	501
Decrease in trade receivables		3,898	27,472
Decrease in amounts due from fellow subsidiaries		8,314	5,806

	For the six months ended 30 June	
	2017	**2016**
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Decrease/(increase) in prepayments, deposits and other receivables	(2,467)	13,693
Decrease in an amount due from a non-controlling shareholder of a subsidiary	—	323
Decrease in trade payables	(7,065)	(22,974)
Increase/(decrease) in other payables and accruals	4,344	(12,480)
Increase in customer deposits	407,446	276,530
Cash generated from operations	327,833	195,283
Overseas tax paid	(8,898)	(33,222)
Net cash flows from operating activities	318,935	162,061
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of items of property, plant and equipment	(26)	(102)
Proceeds from disposal of items of property, plant and equipment	548	—
Proceeds from disposal of convertible loans	87,151	—
Repayment of a loan from a related company	—	24
Bank interest received	3,094	818
Interest received on a convertible bond	518	518
Interest received on loans to associates	570	344
Interest received on loans to related companies	1,065	—
Increase in pledged time deposits	—	(2,815)
Net cash flows from/(used in) investing activities	92,920	(1,213)

	For the six months ended 30 June	
	2017	2016
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
CASH FLOWS FROM FINANCING ACTIVITIES		
New bank loans	—	354,455
Repayment of bank loans	(230,134)	—
Repayment of loans from a fellow subsidiary	(106,145)	(265,792)
Increase in amounts due to non-controlling shareholders of subsidiaries	25,891	58,216
Increase/(decrease) in an amount due to an intermediate holding company	7,535	(14,163)
Increase in amounts due to fellow subsidiaries	1,830	—
Interest paid	(56,083)	(93,535)
Net cash flows from/(used in) financing activities	(357,106)	39,181
NET INCREASE IN CASH AND CASH EQUIVALENTS	54,749	200,029
Cash and cash equivalents at 1 January	605,925	473,330
Effect of foreign exchange rate changes, net	9,703	(7,164)
CASH AND CASH EQUIVALENTS AT 30 JUNE	670,377	666,195
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS		
Cash and bank balances	370,086	643,902
Non-pledged time deposit with original maturity of less than three months when acquired	300,291	20,359
Cash and cash equivalents as stated in the statement of financial position	670,377	664,261
Cash and bank balances attributable to a discontinued operation	—	1,934
Cash and cash equivalents as stated in the statement of cash flows	670,377	666,195

NOTES TO INTERIM FINANCIAL STATEMENTS

1. **Accounting policies and basis of preparation**

The condensed consolidated interim financial statements are prepared in accordance with the applicable disclosure requirements of Appendix 16 of the Listing Rules and are in compliance with the Hong Kong Accounting Standard ("HKAS") 34 "Interim Financial Reporting" issued by the HKICPA.

The accounting policies and basis of preparation adopted in the preparation of the condensed consolidated interim financial statements are the same as those used in the annual financial statements for the year ended 31 December 2016, except for the adoption of certain revised Hong Kong Financial Reporting Standards ("HKFRSs") (which also include HKASs and Interpretations) for the first time in the current period as disclosed in note 2 below.

2. **Changes in accounting policies and disclosures**

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

Amendments to HKAS 7	*Disclosure Initiative*
Amendments to HKAS 12	*Recognition of Deferred Tax Assets for Unrealised Losses*
Annual Improvements 2014-2016 Cycle	Amendments to HKFRS 12 *Clarification of the scope of disclosure requirements in HKFRS 12*

The adoption of the revised HKFRSs has had no significant financial effect on these condensed consolidated interim financial statements.

3. **Operating segment information**

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

(a) the property development and investment business segment engages in the property development of residential and commercial projects; and

(b) the trading business segment engages in the trading of raw materials and auxiliary materials.

Management monitors the results of the Group's operating segments separately for the purpose of making decisions about resources allocation and performance assessment. Segment performance is evaluated based on reportable segment profit/(loss), which is a measure of adjusted profit/(loss) for the period from continuing operations. The adjusted profit/(loss) for the period from continuing operations is measured consistently with the Group's profit/(loss) for the period from continuing operations except that certain income and gains or losses relating to investments in a joint venture and associates and financial instruments, the gain on disposal of convertible loans, as well as head office and corporate expenses and unallocated income tax are excluded from such measurement.

The following is an analysis of the Group's revenue and results from continuing operations by reportable operating segments.

For the six months ended 30 June 2017

	Property development and investment business	**Trading business**	**Total**
	(Unaudited)	*(Unaudited)*	*(Unaudited)*
	HK$'000	*HK$'000*	*HK$'000*
Segment revenue:			
Sales to external customers	19,760	—	19,760
Gross rental income	9,980	—	9,980
Revenue from continuing operations	29,740	—	29,740
Segment results	(46,841)	—	(46,841)
Reconciliation:			
Unallocated other income			3,311
Corporate and other unallocated expenses			(14,105)
Gain on disposal of convertible loans			87,151
Share of profits and losses of:			
Joint venture			(9,934)
Associates			(1,113)
Impairment of an available-for-sale investment			(48,485)
Fair value loss on derivative financial instruments			(11,086)
Fair value loss on equity investment at fair value through profit or loss			(25,905)
Loss for the period from continuing operations			(67,007)

For the six months ended 30 June 2016

	Property development and investment business *(Unaudited)* *HK$'000*	**Trading business** *(Unaudited)* *HK$'000*	**Total** *(Unaudited)* *HK$'000*
Segment revenue:			
Sales to external customers	56,431	—	56,431
Gross rental income	8,156	—	8,156
Revenue from continuing operations	64,587	—	64,587
Segment results	2,288	—	2,288
Reconciliation:			
Unallocated other income			4,551
Corporate and other unallocated expenses			(8,195)
Gain on deemed disposal of interest in an associate			3,386
Share of profits and losses of:			
Joint venture			(43,232)
Associates			(2,623)
Impairment of an available-for-sale investment			(94,907)
Fair value loss on derivative financial instruments			(72,027)
Fair value loss on equity investment at fair value through profit or loss			(137,904)
Unallocated income tax expense			(5)
Loss for the period from continuing operations			(348,668)

4. **Other income**

An analysis of other income from continuing operations is as follows:

	For the six months ended 30 June	
	2017	**2016**
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Bank interest income	3,091	816
Interest income on a convertible bond	518	518
Interest income on loans to associates	282	284
Interest income on loans to related companies	511	833
Government grant*	168	7,245
Others	—	150
	4,570	9,846

* This represents subsidies from municipal government in Mainland China. There are no unfulfilled conditions or contingencies relating to these subsidies.

5. **Finance costs**

An analysis of finance costs from continuing operations is as follows:

	For the six months ended 30 June	
	2017	**2016**
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Interest on bank loans and other loans	60,772	97,139
Less: Interest capitalised	(38,683)	(97,101)
	22,089	38

6. **Loss before tax**

The Group's loss before tax from continuing operations is arrived at after charging:

	For the six months ended 30 June	
	2017	**2016**
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Cost of properties sold*	20,980	36,028
Depreciation	681	1,150
Other operating expenses:		
Loss on disposal of items of property, plant and equipment	347	—
Provision for impairment of a loan to a related company	—	934
	347	934

* Included in "cost of sales" in the condensed consolidated statement of profit or loss.

7. **Income tax**

No provision for Hong Kong profits tax has been made for the six months ended 30 June 2017 and 2016 as the Group did not generate any assessable profits arising in Hong Kong during those periods. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries/jurisdictions in which the Group operates.

	For the six months ended 30 June	
	2017	**2016**
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Current — Elsewhere	1,714	1,471
Deferred	(25)	(989)
Land Appreciation Tax in Mainland China	613	5,279
Total tax charge for the period	2,302	5,761

8. **Discontinued operation**

On 29 June 2016, the Group signed an agreement with an independent third party to dispose of 浙江東陽金牛針織製衣有限公司 ("Zhejiang Dongyang Jinniu"), a 51%-owned subsidiary. Zhejiang Dongyang Jinniu engaged in the production and distribution of knitting and textile products, knitted fabrics and clothing. The Group decided to dispose of this subsidiary and cease its knitting and textile business because it had been loss-making in recent years.

The results of Zhejiang Dongyang Jinniu included in the Group's condensed consolidated statement of profit or loss as a discontinued operation are presented below:

	For the six months ended 30 June	
	2017	**2016**
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Revenue	—	18,616
Cost of sales	—	(17,621)
Gross profit	—	995
Other income	—	112
Administrative expenses	—	(882)
Other operating expenses, net	—	(4,112)
Finance costs	—	(1,188)
Loss before tax from the discontinued operation	—	(5,075)
Income tax expense	—	(16)
Loss after tax from the discontinued operation	—	(5,091)
Attributable to:		
Owners of the parent	—	(2,596)
Non-controlling interests	—	(2,495)
	—	(5,091)
Loss per share:		
Basic and diluted, from the discontinued operation	—	(HK0.04 cent)

The calculation of basic and diluted loss per share from the discontinued operation is based on:

	For the six months ended 30 June	
	2017	**2016**
	(Unaudited)	*(Unaudited)*
Loss attributable to ordinary equity holders of the parent from the discontinued operation	—	(HK$2,596,000)
Weighted average number of ordinary shares in issue during the period	5,519,591,000	5,519,591,000

The net cash flows incurred by Zhejiang Dongyang Jinniu are as follows:

	For the six months ended 30 June	
	2017	**2016**
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Operating activities	—	5,354
Investing activities	—	(2,814)
Financing activities	—	(962)
Net cash inflow	—	1,578

9. **Loss per share attributable to ordinary equity holders of the parent**

The calculation of the basic loss per share amounts is based on the loss for the period attributable to ordinary equity holders of the parent, and the weighted average number of ordinary shares of 5,519,591,000 (2016: 5,519,591,000) in issue during the period.

No adjustment has been made to the basic loss per share amounts presented for the six months ended 30 June 2017 and 2016 in respect of a dilution as the Group had no potentially dilutive ordinary shares in issue during those periods.

The calculation of basic and diluted loss per share is based on:

	For the six months ended 30 June 2017	2016
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Loss attributable to ordinary equity holders of the parent		
From continuing operations	(57,374)	(350,902)
From a discontinued operation	—	(2,596)
	(57,374)	(353,498)

	For the six months ended 30 June 2017	2016
	(Unaudited)	*(Unaudited)*
Shares		
Weighted average number of ordinary shares in issue during the period	5,519,591,000	5,519,591,000

10. Dividend

The Directors do not declare an interim dividend for the six months ended 30 June 2017 (2016: Nil).

11. Trade receivables

	30 June 2017	31 December 2016
	(Unaudited)	*(Audited)*
	HK$'000	*HK$'000*
Trade receivables	88,307	89,620
Less: Non-current portion	—	(20,178)
Current portion	88,307	69,442

The Group has different credit policies for different business operations depending on the requirements of the markets and businesses in which the subsidiaries operate. Trade receivables from sale of properties in respect of the property development and investment business are payable pursuant to the terms of sale and purchase agreements. The Group's trading terms with its customers in the trading business are mainly on credit, except for new customers, where payment in advance is normally required. The credit period is generally one month, extending up to three months for major customers. Each customer has a maximum credit limit.

The Group seeks to maintain strict control over its outstanding receivables. Overdue balances are reviewed regularly by senior management. In view of the aforementioned and the fact that the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. The Group does not hold any collateral or other credit enhancements over its trade receivable balances. Trade receivables are non-interest-bearing.

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

	30 June 2017	**31 December 2016**
	(Unaudited)	*(Audited)*
	HK$'000	*HK$'000*
Within 1 month	1,713	2,089
1 to 2 months	—	—
2 to 3 months	—	—
Over 3 months	86,594	87,531
	88,307	89,620

12. **Trade payables**

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

	30 June 2017	**31 December 2016**
	(Unaudited)	*(Audited)*
	HK$'000	*HK$'000*
Within 1 month	5,167	10,249
1 to 2 months	—	28,005
2 to 3 months	—	—
Over 3 months	30,011	2,959
	35,178	41,213

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

13. **Commitments**

	30 June 2017	**31 December 2016**
	(Unaudited)	*(Audited)*
	HK$'000	*HK$'000*
Contracted, but not provided for:		
Property development expenditure	309,435	328,655

14. **Contingent liabilities**

As at 30 June 2017, the Group has given guarantees of HK$73,081,000 (31 December 2016: HK$76,085,000) to banks for housing loans extended by the banks to the purchasers of the Group's properties for a period from the date of loans being granted to the purchasers up to the date of issuance of property title certificates to the purchasers.

15. **Related party transactions**

(a) In addition to the transactions described elsewhere in the interim report, the Group had the following material transactions with related parties during the period:

	For the six months ended 30 June	
	2017	**2016**
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Interest income on loans to related companies	511	833
Interest income on loans to associates	282	284
Fellow subsidiaries:		
Interest expense on loans from fellow subsidiaries	(34,726)	(87,622)
Management fee paid to a fellow subsidiary	(1,148)	(4,566)
Agency fee paid to a fellow subsidiary	(56)	(93)
Interest expenses on loans from an intermediate holding company	(21,956)	(5,449)

These related party transactions were conducted in accordance with the terms as disclosed in the last annual report.

(b) Outstanding balances with related parties:

(i) The loans to associates are unsecured and bear interest at 6% (31 December 2016: 4.5% to 6%) per annum.

(ii) The loan to a related company is unsecured, bears interest at 6.15% (31 December 2016: 6.15%) per annum and is repayable within one year.

(iii) The balances with non-controlling shareholders of subsidiaries are unsecured, non-interest-bearing and have no fixed terms of repayment.

(iv) The amounts due from and to an intermediate holding company are unsecured, non-interest-bearing and have no fixed terms of repayment. The loans from an intermediate holding company are unsecured, bear interest at 6% (31 December 2016: 6%) per annum and are not repayable within one year.

(v) The amounts due from and to fellow subsidiaries are unsecured and non-interest-bearing. The loans from a fellow subsidiary are unsecured and bear interest at 6% (31 December 2016: 6%) per annum.

(c) Compensation of key management personnel of the Group:

	For the six months ended 30 June	
	2017	2016
	(Unaudited)	*(Unaudited)*
	HK$'000	*HK$'000*
Short term employee benefits	785	280
Post-employment benefits	18	14
Total compensation paid to key management personnel	803	294

16. Fair value and fair value hierarchy of financial instruments

The carrying amounts and fair values of the Group's financial instruments, other than those with carrying amounts that reasonably approximate to fair values, are as follows:

	Carrying amounts		Fair values	
	30 June 2017	31 December 2016	30 June 2017	31 December 2016
	(Unaudited)	*(Audited)*	*(Unaudited)*	*(Audited)*
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Financial assets				
Trade receivable (non-current portion)	—	20,178	—	18,862
Available-for-sale investments	241,533	278,745	241,533	278,745
Equity investment at fair value through profit or loss	61,714	87,619	61,714	87,619
Derivative financial instruments	252	11,338	252	11,338
	303,499	397,880	303,499	396,564
Financial liabilities				
Loans from an intermediate holding company	489,756	475,419	487,645	473,114
Loans from a fellow subsidiary (non-current portion)	540,976	648,045	537,796	646,682
Interest-bearing bank borrowings	—	230,134	—	227,430
	1,030,732	1,353,598	1,025,441	1,347,226

Management has assessed that the fair values of trade receivables (current portion), balances with fellow subsidiaries, an intermediate holding company, non-controlling shareholders of subsidiaries, associates and a related company, financial assets included in prepayments, deposits and other receivables, cash and cash equivalents, trade payables, and other payables and accruals approximate to their carrying amounts largely due to the short term maturities of these instruments.

The Group's finance department headed by the chief financial officer is responsible for determining the policies and procedures for the fair value measurement of financial instruments. At each reporting date, the finance department analyses the movements in the values of financial instruments and determines the major inputs applied in the valuation. The valuation is reviewed and approved by the chief financial officer and then reported to the chief executive officer. The valuation process and results are discussed with the audit committee twice a year for interim and annual financial reporting.

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

The following methods and assumptions were used to estimate the fair values:

The fair values of trade receivable (non-current portion), loans from an intermediate holding company, loans from a fellow subsidiary (non-current portion) and interest-bearing bank borrowings have been calculated by discounting the expected future cash flows using rates currently available for instruments with similar terms, credit risk and remaining maturities. The Group's own non-performance risk for loans from an intermediate holding company and loans from a fellow subsidiary as at 30 June 2017 was assessed to be insignificant.

The fair values of listed equity investments are based on quoted market prices. The fair values of unlisted available-for-sale investments and derivative financial instruments have been estimated using a valuation technique based on assumptions that are supported by observable market prices or rates. The directors believe that the estimated fair values resulting from the valuation technique, which are recorded in the condensed consolidated statement of financial position, and the related changes in fair values, which are recorded in other comprehensive income and the condensed consolidated statement of profit or loss, are reasonable, and that they were the most appropriate values at the end of the reporting period.

The Group enters into derivative financial instruments with various counterparties. Derivative financial instruments were measured using valuation models which incorporate various market observable inputs including the credit quality of counterparties and interest rate curves. The carrying amounts of derivative financial instruments were the same as their fair values. As at 30 June 2017, the marked to market value of the above derivative asset position was net of a credit valuation adjustment attributable to derivative counterparty default risk.

Fair value hierarchy

The following tables illustrate the fair value measurement hierarchy of the Group's financial instruments:

Assets measured at fair value:

	Fair value measurement using			
	Quoted prices in active markets (Level 1)	**Significant observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
As at 30 June 2017 (Unaudited)				
Available-for-sale investments:				
Equity investments	149,732	—	—	149,732
Debt investments	—	91,801	—	91,801
Equity investment at fair value through profit or loss	61,714	—	—	61,714
Derivative financial instruments	—	252	—	252
	211,446	92,053	—	303,499
As at 31 December 2016 (Audited)				
Available-for-sale investments:				
Equity investments	149,581	—	—	149,581
Debt investments	—	129,164	—	129,164
Equity investment at fair value through profit or loss	87,619	—	—	87,619
Derivative financial instruments	—	11,338	—	11,338
	237,200	140,502	—	377,702

The Group did not have any financial liabilities measured at fair value as at 30 June 2017 and 31 December 2016.

During the period, there were no transfers of fair value measurements between Level 1 and Level 2 and no transfers into or out of Level 3 for both financial assets and financial liabilities (2016: Nil).

Assets for which fair values are disclosed:

	Fair value measurement using			
	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
As at 31 December 2016 (Audited)				
Trade receivable (non-current portion)	—	18,862	—	18,862

Liabilities for which fair values are disclosed:

	Fair value measurement using			
	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
As at 30 June 2017 (Unaudited)				
Loans from an intermediate holding company	—	487,645	—	487,645
Loans from a fellow subsidiary (non-current portion)	—	537,796	—	537,796
	—	1,025,441	—	1,025,441
As at 31 December 2016 (Audited)				
Loans from an intermediate holding company	—	473,114	—	473,114
Loans from a fellow subsidiary (non-current portion)	—	646,682	—	646,682
Interest-bearing bank borrowings	—	227,430	—	227,430
	—	1,347,226	—	1,347,226

IV. INDEBTEDNESS STATEMENT OF THE ENLARGED GROUP

Borrowings

As at the close of business on 31 October 2017, being the latest practicable date for the purpose of this indebtedness statement prior to the printing of this circular, the Enlarged Group had (i) guaranteed and unguaranteed bank borrowings of approximately HK$1,752,205,000 and HK$28,082,000; (ii) unsecured loans from an intermediate holding company of the Enlarged Group of approximately HK$499,205,000; and (iii) unsecured loans from fellow subsidiaries of the Enlarged Group of approximately HK$1,486,431,000.

As at the close of business on 31 October 2017, the Enlarged Group had total available and unutilised banking facilities of approximately HK$234,332,000.

Certain bank borrowings of the Enlarged Group were guaranteed as follows:

Details of guarantees:	*HK$'000*
Guaranteed by the ultimate holding company and an intermediate holding company of the Enlarged Group	1,326,109
Guaranteed by an intermediate holding company of the Enlarged Group	426,096
	1,752,205

Contingent liabilities

As at the close of business on 31 October 2017, the Enlarged Group had guarantee given to banks for housing loans extended by the banks to the purchasers of the Enlarged Group's properties for a period from the date of loans being granted to the purchasers up to the date of issuance of property title certificates to the purchasers of approximately HK$118,105,000.

Save as disclosed above, the Enlarged Group did not have any other outstanding mortgages, charges, debentures or other loan capital, bank overdrafts or loan, other similar indebtedness, liabilities under acceptance or acceptance credits, guarantees or other material contingent liabilities as at the close of business on 31 October 2017.

V. WORKING CAPITAL OF THE ENLARGED GROUP

The Directors, after due and careful enquiry, are of the opinion that, after taking into consideration the financial resources available to the Enlarged Group, the Enlarged Group will have sufficient working capital to meet its present requirements for at least 12 months from the date of this Circular in the absence of unforeseen circumstances.

VI. ADJUSTED NAV

	HK$ million
Unaudited consolidated NAV of the Group attributable to owners of the Company as at 30 June 2017	1,968
Adjustment:	
• Unaudited total comprehensive loss for July to October 2017 attributable to owners of the Company	(21)
• Revaluation deficit arising from the valuation of property interests attributable to the owners of the Company as at 31 October 2017 *(Note 1)*	(109)
Adjusted NAV	1,838
Adjusted NAV per Share *(Note 2)*	**HK$0.33**

Notes:

1. This represents revaluation deficit arising from the excess of the book values of the property interests held by the Group as at 31 October 2017 over their corresponding market value as valued by Jones Lang LaSalle Corporate Appraisal & Advisory Limited as at the same date, after taking into account the relevant tax impact and adjusting for relevant interests not attributable to the owners of the Company.

2. Based on 5,519,591,000 Shares in issue as at the Latest Practicable Date.

The following is the text of a report prepared for the sole purpose of inclusion in this circular, received from the independent reporting accountants, Ernst & Young, Certified Public Accountants, Hong Kong. Terms defined herein apply to this report only.

The Board of Directors
AVIC International Holding (HK) Limited

Dear Sirs,

We report on the historical financial information of Motto Investment Limited (the "Target Company") and its subsidiaries (together, the "Target Group") set out on pages III-4 to III-73, which comprises the consolidated statements of profit or loss and other comprehensive income, consolidated statements of changes in equity and consolidated statements of cash flows of the Target Group for each of the years ended 31 December 2014, 2015 and 2016, and the six months ended 30 June 2017 (the "Relevant Periods"), and the consolidated statements of financial position of the Target Group and the statements of financial position of the Target Company as at 31 December 2014, 2015 and 2016 and 30 June 2017 and a summary of significant accounting policies and other explanatory information (together, the "Historical Financial Information"). The Historical Financial Information set out on pages III-4 to III-73 forms an integral part of this report, which has been prepared for inclusion in the circular of AVIC International Holding (HK) Limited (the "Company") dated 29 December 2017 (the "Circular") in connection with the proposed acquisition of the entire equity interest of the Target Company.

Directors' responsibility for the Historical Financial Information

The directors of the Target Company (the "Directors") are responsible for the preparation of the Historical Financial Information that gives a true and fair view in accordance with the basis of presentation and the basis of preparation set out in notes 2.1 and 2.2 to the Historical Financial Information, respectively, and for such internal control as the Directors determine is necessary to enable the preparation of the Historical Financial Information that is free from material misstatement, whether due to fraud or error.

Reporting accountants' responsibility

Our responsibility is to express an opinion on the Historical Financial Information and to report our opinion to you. We conducted our work in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 200 *Accountants' Reports on Historical Financial Information in Investment Circulars* issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"). This standard requires that we comply with ethical standards and plan and perform our work to obtain reasonable assurance about whether the Historical Financial Information is free from material misstatement.

Our work involved performing procedures to obtain evidence about the amounts and disclosures in the Historical Financial Information. The procedures selected depend on the reporting accountants' judgement, including the assessment of risks of material misstatement of the Historical Financial Information, whether due to fraud or error. In making those risk assessments, the reporting accountants consider internal control relevant to the entity's preparation of the Historical Financial Information that gives a true and fair view in accordance with the basis of presentation and the basis of preparation set out in notes 2.1 and 2.2 to the Historical Financial Information, respectively, in order to design procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Our work also included evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Directors, as well as evaluating the overall presentation of the Historical Financial Information.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion, the Historical Financial Information gives, for the purposes of the accountants' report, a true and fair view of the financial position of the Target Group and the Target Company as at 31 December 2014, 2015 and 2016 and 30 June 2017 and of the financial performance and cash flows of the Target Group for each of the Relevant Periods in accordance with the basis of presentation and the basis of preparation set out in notes 2.1 and 2.2 to the Historical Financial Information, respectively.

Review of interim comparative financial information

We have reviewed the interim comparative financial information of the Target Group which comprises the consolidated statement of profit or loss and other comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the six months ended 30 June 2016 and other explanatory information (the "Interim Comparative Financial Information"). The Directors are responsible for the preparation and presentation of the Interim Comparative Financial Information in accordance with the basis of presentation and the basis of preparation set out in notes 2.1 and 2.2 to the Historical Financial Information, respectively. Our responsibility is to express a conclusion on the Interim Comparative Financial Information based on our review. We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410 *Review of Interim Financial Information Performed by the Independent Auditor of the Entity* issued by the HKICPA. A review consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion. Based on our review, nothing has come to our attention that causes us to believe that the Interim Comparative Financial Information, for the purposes of the accountants' report, is not prepared, in all material respects, in accordance with the basis of presentation and the basis of preparation set out in notes 2.1 and 2.2 to the Historical Financial Information, respectively.

Report on matters under the Rules Governing the Listing of Securities on the Main Board of the Stock Exchange and the Companies (Winding Up and Miscellaneous Provisions) Ordinance

Adjustments

In preparing the Historical Financial Information, no adjustments to the Underlying Financial Statements as defined on page III-4 have been made.

Dividends

No dividends have been paid by the Target Company in respect of the Relevant Periods.

No historical financial statements for the Target Company

As at the date of this report, no statutory financial statements have been prepared for the Target Company since its date of incorporation.

Yours faithfully,
Ernst & Young
Certified Public Accountants
Hong Kong

29 December 2017

I. HISTORICAL FINANCIAL INFORMATION

Preparation of Historical Financial Information

Set out below is the Historical Financial Information which forms an integral part of this accountants' report.

The financial statements of the Target Group for the Relevant Periods, on which the Historical Financial Information is based, were audited by Ernst & Young, Hong Kong in accordance with Hong Kong Standards on Auditing issued by the HKICPA (the "Underlying Financial Statements").

The Historical Financial Information is presented in United States dollars ("US$") and all values are rounded to the nearest thousand ("US$'000") except when otherwise indicated.

CONSOLIDATED STATEMENTS OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

	Notes	Year ended 31 December			Six months ended 30 June	
		2014	2015	2016	2016	2017
		US$'000	*US$'000*	*US$'000*	*US$'000* *(Unaudited)*	*US$'000*
REVENUE	5	161,444	163,689	204,315	101,191	99,432
Cost of sales		(112,110)	(111,907)	(138,883)	(67,980)	(67,955)
Gross profit		49,334	51,782	65,432	33,211	31,477
Selling expenses		(9,609)	(10,233)	(11,043)	(5,571)	(4,583)
General and administrative expenses		(36,069)	(27,152)	(33,956)	(18,407)	(16,718)
Other operating income/(expenses), net		92	35	(119)	162	87
Finance costs	6	(8,769)	(8,785)	(10,793)	(5,285)	(5,386)
Share of profit of a joint venture		2	1	14	17	35
PROFIT/(LOSS) BEFORE TAX	7	(5,019)	5,648	9,535	4,127	4,912
Income tax credit/(expense)	9	(2,610)	5,945	(4,163)	(1,363)	(1,308)
PROFIT/(LOSS) FOR THE YEAR/PERIOD		(7,629)	11,593	5,372	2,764	3,604
OTHER COMPREHENSIVE INCOME						
Other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods:						
Exchange differences on translation of foreign operations		1,501	1,096	591	(259)	(1,270)
Other comprehensive income/(loss) not to be reclassified to profit or loss in subsequent periods:						
Actuarial gains/(losses) on defined benefit plans	23	6	(130)	213	45	112
Income tax effect	14	(28)	125	(82)	(232)	(215)
		(22)	(5)	131	(187)	(103)
OTHER COMPREHENSIVE INCOME/(LOSS) FOR THE YEAR/PERIOD, NET OF TAX		1,479	1,091	722	(446)	(1,373)
TOTAL COMPREHENSIVE INCOME/(LOSS) FOR THE YEAR/PERIOD		(6,150)	12,684	6,094	2,318	2,231

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

	Notes	As at 31 December 2014	2015	2016	As at 30 June 2017
		US$'000	*US$'000*	*US$'000*	*US$'000*
NON-CURRENT ASSETS					
Property, plant and equipment	10	34,343	38,730	34,165	31,789
Goodwill	11	106,714	109,373	109,153	109,453
Other intangible assets	12	105,831	111,626	115,185	119,036
Investment in a joint venture	13	35	36	50	85
Deferred tax assets	14	—	468	—	—
Prepayment		216	177	142	125
Total non-current assets		247,139	260,410	258,695	260,488
CURRENT ASSETS					
Inventories	15	39,054	46,419	52,001	59,638
Trade and other receivables	16	12,012	24,700	16,582	17,060
Due from fellow subsidiaries	17	5,968	3,254	3,734	2,344
Prepayments		5,139	5,071	3,874	2,556
Restricted bank balance	18	8,083	—	—	—
Cash and cash equivalents	18	13,191	9,419	14,105	8,460
Total current assets		83,447	88,863	90,296	90,058
CURRENT LIABILITIES					
Trade payables, other payables and accruals	19	21,013	25,123	22,718	19,795
Interest-bearing loans and borrowings	20	346	5,959	21,600	21,600
Deferred revenue	21	184	122	466	143
Provisions and other liabilities	22	6,558	2,972	4,164	4,109
Due to the immediate holding company	17	1,176	437	741	1,216
Due to fellow subsidiaries	17	3,991	23,895	38,670	49,298
Tax payable		152	277	4	78
Total current liabilities		33,420	58,785	88,363	96,239
NET CURRENT ASSETS/(LIABILITIES)		50,027	30,078	1,933	(6,181)
TOTAL ASSETS LESS CURRENT LIABILITIES		297,166	290,488	260,628	254,307
NON-CURRENT LIABILITIES					
Interest-bearing loans and borrowings	20	257,568	256,367	222,824	216,128
Deferred revenue	21	3,020	3,239	4,234	4,321
Provisions and other liabilities	22	36,940	23,004	15,849	13,112
Defined benefit obligations	23	751	983	853	558
Due to the immediate holding company	17	868	2,153	2,318	2,194
Deferred tax liabilities	14	5,961	—	3,714	4,927
Total non-current liabilities		305,108	285,746	249,792	241,240
Net assets/(liabilities)		(7,942)	4,742	10,836	13,067
EQUITY/(DEFICIENCY IN ASSETS)					
Share capital	24	20,000	20,000	20,000	20,000
Reserves	25(a)	(27,942)	(15,258)	(9,164)	(6,933)
Total equity/(deficiency in assets)		(7,942)	4,742	10,836	13,067

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

	Share capital	Reserve fund (Note 25(b))	Foreign currency translation reserve	Accumulated losses	Total equity/ (deficiency in assets)
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
At 1 January 2014	20,000	—	(158)	(21,634)	(1,792)
Loss for the year	—	—	—	(7,629)	(7,629)
Other comprehensive income/(loss)	—	—	1,501	(22)	1,479
Total comprehensive income/(loss) for the year	—	—	1,501	(7,651)	(6,150)
At 31 December 2014 and 1 January 2015	20,000	—*	1,343*	(29,285)*	(7,942)
Profit for the year	—	—	—	11,593	11,593
Other comprehensive income/(loss)	—	—	1,096	(5)	1,091
Total comprehensive income for the year	—	—	1,096	11,588	12,684
At 31 December 2015 and 1 January 2016	20,000	—*	2,439*	(17,697)*	4,742
Profit for the year	—	—	—	5,372	5,372
Other comprehensive income	—	—	591	131	722
Total comprehensive income for the year	—	—	591	5,503	6,094
Transfer to reserve fund	—	3	—	(3)	—
At 31 December 2016 and 1 January 2017	20,000	3*	3,030*	(12,197)*	10,836
Profit for the period	—	—	—	3,604	3,604
Other comprehensive loss	—	—	(1,270)	(103)	(1,373)
Total comprehensive income/(loss) for the period	—	—	(1,270)	3,501	2,231
At 30 June 2017	20,000	3*	1,760*	(8,696)*	13,067
At 1 January 2016	20,000	—	2,439	(17,697)	4,742
Profit for the period	—	—	—	2,764	2,764
Other comprehensive loss	—	—	(259)	(187)	(446)
Total comprehensive income/(loss) for the period	—	—	(259)	2,577	2,318
At 30 June 2016 (Unaudited)	20,000	—	2,180	(15,120)	7,060

* *These reserve accounts comprised the negative reserves of US$27,942,000, US$15,258,000, US$9,164,000 and US$6,933,000 as at 31 December 2014, 2015 and 2016 and 30 June 2017, respectively, in the consolidated statements of financial position.*

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Notes	Year ended 31 December 2014 US$'000	2015 US$'000	2016 US$'000	Six months ended 30 June 2016 US$'000 (Unaudited)	2017 US$'000
CASH FLOWS FROM OPERATING ACTIVITIES						
Profit/(loss) before tax		(5,019)	5,648	9,535	4,127	4,912
Adjustments for:						
Finance costs	6	8,769	8,785	10,793	5,285	5,386
Depreciation	7	6,466	6,141	6,001	2,953	3,108
Amortisation of intangible assets	7	3,714	4,319	4,632	2,346	2,301
Provision/(reversal of provision) of trade receivables	7	(138)	687	(217)	—	350
Impairment of items of property, plant and equipment	7	—	—	306	—	—
Impairment of goodwill	7	—	—	86	—	—
Loss/(gain) on disposal of items of property, plant and equipment	7	1	—	75	(31)	—
Loss on disposal of other intangible assets	7	30	2	91	—	—
Reversal of provisions for deposits	7	—	(619)	(136)	—	—
Pension scheme expense under defined benefit schemes	7	515	506	479	239	242
Share of profit of a joint venture		(2)	(1)	(14)	(17)	(35)
		14,336	25,468	31,631	14,902	16,264
Decrease/(increase) in inventories		1,722	708	(5,593)	(3,918)	(7,189)
Decrease/(increase) in trade and other receivables		(398)	(9,530)	8,334	(4,012)	(722)
Decrease/(increase) in prepayments		(2,651)	106	1,232	1,078	1,351
Decrease/(increase) in amounts due from fellow subsidiaries		3,277	2,209	(480)	(243)	1,390
Increase in amounts due to fellow subsidiaries		148	—	975	394	628
Increase in an amount due to the immediate holding company		714	533	467	216	432
Increase/(decrease) in trade payables, other payables and accruals		7,473	2,497	(2,408)	(2,295)	(2,775)
Increase/(decrease) in deferred revenue		894	157	1,339	4,231	(236)
Decrease in provisions and other liabilities		(11,366)	(17,380)	(5,947)	(1,659)	(3,095)
Benefits paid from defined benefit schemes	23	(12)	(74)	(59)	(31)	(22)
Contribution to defined benefit schemes	23	(367)	(330)	(337)	(171)	(403)
Cash generated from operations		13,770	4,364	29,154	8,492	5,623
Profits tax paid		(361)	(234)	(336)	(192)	(235)
Net cash flows from operating activities		13,409	4,130	28,818	8,300	5,388

	Notes	Year ended 31 December 2014 US$'000	2015 US$'000	2016 US$'000	Six months ended 30 June 2016 US$'000 (Unaudited)	2017 US$'000
CASH FLOWS FROM INVESTING ACTIVITIES						
Purchase of items of property, plant and equipment	10	(4,043)	(5,669)	(4,037)	(778)	(2,070)
Proceeds from disposal of items of property, plant and equipment		167	42	1,885	52	2,076
Additions to other intangible assets	12	(6,890)	(6,663)	(8,803)	(3,993)	(4,987)
Acquisitions of businesses	26	(723)	(24,069)	—	—	—
Net cash flows used in investing activities		(11,489)	(36,359)	(10,955)	(4,719)	(4,981)
CASH FLOWS FROM FINANCING ACTIVITIES						
New bank loans		—	22,000	2,000	1,000	—
Loans from a fellow subsidiary		3,991	24,400	13,800	3,800	10,000
Repayment of a loan from a fellow subsidiary		—	(3,991)	—	—	—
Repayment of bank loans		—	(11,467)	(17,600)	(4,800)	(10,800)
Decrease in a restricted bank balance		—	8,083	—	—	—
Capital element of finance lease rental payments		(324)	(346)	(471)	(178)	—
Interest paid		(8,769)	(8,785)	(10,793)	(5,285)	(5,386)
Net cash flows from/(used in) financing activities		(5,102)	29,894	(13,064)	(5,463)	(6,186)
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS		(3,182)	(2,335)	4,799	(1,882)	(5,779)
Cash and cash equivalents at beginning of year/period		18,170	13,191	9,419	9,419	14,105
Effect of foreign exchange rate changes, net		(1,797)	(1,437)	(113)	45	134
CASH AND CASH EQUIVALENTS AT END OF YEAR/PERIOD		13,191	9,419	14,105	7,582	8,460
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS						
Cash and cash equivalents as stated in the consolidated statements of financial position and the consolidated statements of cash flows		13,191	9,419	14,105	7,582	8,460

STATEMENTS OF FINANCIAL POSITION OF THE TARGET COMPANY

					As at
		As at 31 December			**30 June**
	Notes	**2014**	**2015**	**2016**	**2017**
		US$'000	*US$'000*	*US$'000*	*US$'000*
NON-CURRENT ASSET					
Investment in a subsidiary	34(a)	—	—	—	—
CURRENT ASSETS					
Due from the immediate holding company	34(b)	1	—	1	1
Due from a subsidiary	34(b)	19,973	19,978	19,973	19,973
Total current assets		19,974	19,978	19,974	19,974
CURRENT LIABILITY					
Due to the immediate holding company	34(b)	—	4	—	—
NET CURRENT ASSETS AND NET ASSETS		19,974	19,974	19,974	19,974
EQUITY					
Share capital	24	20,000	20,000	20,000	20,000
Foreign currency translation reserve		(26)	(26)	(26)	(26)
Total equity		19,974	19,974	19,974	19,974

II. NOTES TO THE HISTORICAL FINANCIAL INFORMATION

1. CORPORATE INFORMATION

The Target Company is a limited liability company incorporated in the British Virgin Islands ("BVI"). The principal activity of the Target Company is investment holding. The address of its registered office is Morgan & Morgan Building, Pasea Estate, Road Town, Tortola, British Virgin Islands.

During the year, the Target Group's principal activities were the design, development and production of aircraft engines and spare parts and the provision of repair and maintenance services for aircraft engines.

In the opinion of the directors of the Target Company, Aviation Industry Corporation of China, a company established in the People's Republic of China (the "PRC"), is the Target Company's ultimate holding company.

As at the date of this report, the Target Company had direct and indirect interests in its subsidiaries, all of which are private limited liability companies (or, if incorporated outside Hong Kong, have substantially similar characteristics to a private company incorporated in Hong Kong), the particulars of which are set out below:

Name	Place and date of incorporation/ registration and place of operations	Issued ordinary/ registered share capital	Percentage of equity attributable to the Target Company		Principal activities
			Direct	Indirect	
Continental Motors Group Limited (note (a))	Hong Kong/ 26 November 2010	HK$100	100	—	Investment holding
Technify Motor (USA), Inc. (note (b))	United States of America ("USA")/ 1 December 2010	US$1	—	100	Investment holding
Continental Motors, Inc. ("CMI") (note (c))	USA/ 6 December 2001	US$10	—	100	Design, development and production of aircraft engines and spare parts
Continental Motors Services, Inc. ("CMS") (note (c))	USA/ 23 September 1999	US$1	—	100	Provision of repair and maintenance services for aircraft engines
Mangrove Insurance Solutions, PCC (note (c))	USA/ 25 April 2011	US$25,000	—	100	Acquisition of aviation liability reinsurance contracts
Continental Motors (Beijing) Co., Ltd. ("CMB") (note (c))	PRC/ 6 January 2014	US$4,000,000	—	100	Distribution and sale of aircraft engines and engine components

Name	Place and date of incorporation/ registration and place of operations	Issued ordinary/ registered share capital	Percentage of equity attributable to the Target Company Direct	Indirect	Principal activities
Continental Motors Deutschland (note (c))	BVI/ 16 July 2012	US$1	—	100	Investment holding
Technify Motors GmbH (note (d))	Germany/ 1 November 2012	EUR25,000	—	100	Design, development and production of aircraft engines and spare parts
Technify Aircraft UG, St. Egidien (note (c))	Germany/ 19 February 2013	EUR500	—	100	Provision of aircraft rental services

Notes:

(a) The statutory financial statements of this entity for the years ended 31 December 2014, 2015 and 2016 prepared under Hong Kong Financial Reporting Standards ("HKFRSs") were audited by Mak Siu Hong & Co., certified public accountants registered in Hong Kong.

(b) The audited consolidated financial statements of this entity and its subsidiaries for the years ended 31 December 2014, 2015 and 2016 prepared under International Financial Reporting Standards ("IFRSs") were audited by Ernst & Young, Hong Kong.

(c) No audited financial statements have been prepared for these entities for the years ended 31 December 2014, 2015 and 2016 (or since the date of incorporation, where later than the beginning of the Relevant Periods), as the entities were not subject to any statutory audit requirements under the relevant rules and regulations in their jurisdiction of incorporation/establishment.

(d) The statutory financial statements of this entity for the years ended 31 December 2014, 2015 and 2016 prepared under IFRSs were audited by Ernst & Young GmbH.

2.1 BASIS OF PRESENTATION

As at 31 December 2014, the Target Group had deficiency in assets of approximately US$7,942,000. As at 30 June 2017, the Target Group's current liabilities exceeded its current assets by approximately US$6,181,000. As the continuation of the business of the Target Group largely depends on continuing financial support from the Company and the existing shareholder of the Target Company, the Company and the existing shareholders of the Target Company indicated their intention to provide financial support to the Target Group to operate without significant curtailment of its operations and to meet its liabilities as and when they would fall due. Accordingly, the directors of the Target Company consider that it is appropriate to prepare the Historical Financial Information on a going concern basis.

Should the Target Group be unable to continue its business as a going concern, adjustments would have to be made to restate the values of assets to their recoverable amounts, to provide for any further liabilities which might arise and to reclassify non-current assets as current assets. The Historical Financial Information does not include any adjustments that would result from the failure of the Target Group to continue its business as a going concern.

Basis of consolidation

The Historical Financial Information include the financial statements of the Target Company and its subsidiaries for the Relevant Periods. A subsidiary is an entity (including a structured entity), directly or indirectly, controlled by the Target Company. Control is achieved when the Target Company is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee (i.e., existing rights that give the Target Company the current ability to direct the relevant activities of the investee).

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

(a) the contractual arrangement with the other vote holders of the investee;

(b) rights arising from other contractual arrangements; and

(c) the Target Company's voting rights and potential voting rights.

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

All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Target Group are eliminated in full on consolidation.

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

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

2.2 BASIS OF PREPARATION

The Historical Financial Information has been prepared in accordance with HKFRSs (which include all HKFRSs, Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the HKICPA and accounting principles generally accepted in Hong Kong. All HKFRSs effective for the accounting period commencing from 1 January 2017, together with the relevant transitional provisions, have been early adopted by the Target Group in the preparation of the Historical Financial Information throughout the Relevant Periods and in the period covered by the Interim Comparative Financial Information.

The Historical Financial Information has been prepared under the historical cost convention, except to the extent that assets and liabilities were valued at fair value at the time of acquisition in accordance with the guidance outlined in HKFRS 3 *Business Combinations*.

2.3 ISSUED BUT NOT YET EFFECTIVE HKFRSS

At the date of this report, the HKICPA has issued the following new and amendments to HKFRSs that are not yet effective. The Target Group has not early adopted these new and amendments to HKFRSs in the Historical Financial Information.

Amendments to HKFRS 2	*Classification and Measurement of Share-based Payment Transactions*[1]
Amendments to HKFRS 4	*Applying HKFRS 9 Financial Instruments with HKFRS 4 Insurance Contracts*[1]
HKFRS 9	*Financial Instruments*[1]
Amendments to HKFRS 10 and HKAS 28 (2011)	*Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*[3]
HKFRS 15	*Revenue from Contracts with Customers*[1]
Amendments to HKFRS 15	*Clarifications to HKFRS 15 Revenue from Contracts with Customers*[1]
HKFRS 16	*Leases*[2]
Amendments to HKAS 40	*Transfers of Investment Property*[1]
HK(IFRIC)-Int 22	*Foreign Currency Transactions and Advance Consideration*[1]
HK(IFRIC)-Int 23	*Uncertainty over Income Tax Treatments*[2]
Annual Improvements to HKFRSs 2014-2016 Cycle	*Amendments to the following two HKFRSs:* - HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards*[1] - HKAS 28 *Investments in Associates and Joint Ventures*[1]

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

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

3 No mandatory effective date yet determined but available for adoption

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

HKFRS 9 Financial Instruments

In September 2014, the HKICPA issued the final version of HKFRS 9, bringing together all phases of the financial instruments project to replace HKAS 39 and all previous versions of HKFRS 9. The standard introduces new requirements for classification and measurement, impairment and hedge accounting. The Group expects to adopt HKFRS 9 from 1 January 2018. During 2016, the Target Group performed a high-level assessment of the impact of the adoption of HKFRS 9. This preliminary assessment is based on currently available information and may be subject to changes arising from further detailed analyses or additional reasonable and supportable information being made available to the Target Group in the future. The expected impacts arising from the adoption of HKFRS 9 are summarised as follows:

(a) ***Classification and measurement***

The Target Group does not expect that the adoption of HKFRS 9 will have any significant impact on the classification and measurement of its financial assets.

(b) ***Impairment***

HKFRS 9 requires an impairment on debt instruments recorded at amortised cost or at fair value through other comprehensive income, lease receivables, loan commitments and financial guarantee contracts that are not accounted for at fair value through profit or loss under HKFRS 9, to be recorded based on an expected credit loss model either on a twelve-month basis or a lifetime basis. The Target Group expects to apply the simplified approach and record lifetime expected losses that are estimated based on the present value of all cash shortfalls over the remaining life of all of its trade and other receivables. The Target Group will perform a more detailed analysis which considers all reasonable and supportable information, including forward-looking elements, for estimation of expected credit losses on its trade and other receivables upon the adoption of HKFRS 9.

HKFRS 15 Revenue from Contracts with Customers

HKFRS 15 establishes a single comprehensive model for entities to use in the accounting for revenue arising from contracts with customers. HKFRS 15 will supersede the current revenue recognition guidance including HKAS 18 *Revenue*, HKAS 11 *Construction Contracts* and the related interpretations when it becomes effective. The core principle of HKFRS 15 is that an entity should recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the standard introduces a 5-step approach to revenue recognition:

- Step 1: Identify the contract(s) with a customer

- Step 2: Identify the performance obligations in the contract

- Step 3: Determine the transaction price

- Step 4: Allocate the transaction price to the performance obligations in the contract

- Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation

Under HKFRS 15, an entity recognises revenue when (or as) a performance obligation is satisfied, i.e. when "control" of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in HKFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by HKFRS 15.

In 2016, the HKICPA issued clarifications to HKFRS 15 in relation to the identification of performance obligations, principal versus agent considerations, as well as licensing application guidance.

The directors of the Target Company consider that the performance obligations are similar to the current identification of separate revenue components under HKAS 18, however, the allocation of total consideration to the respective performance obligations will be based on relative fair values which will potentially affect the timing and amounts of revenue recognition. In addition, the application of HKFRS 15 may result in more disclosures in the financial statements of the Target Group. The standard also introduces extensive qualitative and quantitative disclosure requirements, including disaggregation of total revenue, information about performance obligations, changes in contract asset and liability account balances between periods and key judgements and estimates. However, the directors of the Target Company do not anticipate that the application of HKFRS 15 will have a material impact on the timing and amounts of revenue recognised in the future.

HKFRS 16 Leases

HKFRS 16 introduces a comprehensive model for the identification of lease arrangements and accounting treatments for both lessors and lessees. HKFRS 16 will supersede HKAS 17 *Leases* and the related interpretations when it becomes effective.

HKFRS 16 distinguishes lease and service contracts on the basis of whether an identified asset is controlled by a customer. For a lessee, a right-of-use asset and a corresponding liability have to be recognised for all leases by lessees, except for short-term leases and leases of low value assets.

The right-of-use asset is initially measured at cost and subsequently measured at cost (subject to certain exceptions) less accumulated depreciation and impairment losses, adjusted for any remeasurement of the lease liability. The lease liability is initially measured at the present value of the lease payments that are not paid at that date. Subsequently, the lease liability is adjusted for interest and lease payments, as well as the impact of lease modifications, among others. For the classification of cash flows, the Target Group currently presents operating lease payments as operating cash flows. Under HKFRS 16, lease payments in relation to the lease liability will be allocated into a principal and an interest portion which will be presented as financing cash flows.

In contrast to lessee accounting, HKFRS 16 substantially carries forward the lessor accounting requirements in HKAS 17, and continues to require a lessor to classify a lease either as an operating lease or a finance lease.

Furthermore, extensive disclosures are required by HKFRS 16.

As at 30 June 2017, the Target Group had non-cancellable operating lease commitments of US$4,997,000 as the lessee as disclosed in note 29. A preliminary assessment indicates that these arrangements will meet the definition of a lease under HKFRS 16, and hence the Target Group will recognise a right-of-use asset and a corresponding liability in respect of all these leases unless they qualify for low value or short-term leases upon the application of HKFRS 16. In addition, the application of new requirements may result in more disclosures as indicated above. The directors of the Target Company do not expect the adoption of HKFRS 16 as compared with the current accounting policy would result in any significant impact on the Target Group's financial performance in the future.

Except for the above, management of the Target Company anticipates that the application of other new and amendments to HKFRSs will have no material impact on the financial statements of the Target Group.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investment in a joint venture

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

The Target Group's investment in a joint venture is stated in the consolidated statement of financial position at the Target Group's share of net assets under the equity method of accounting, less any impairment losses. Adjustments are made to bring into line any dissimilar accounting policies that may exist. The Target Group's share of the post-acquisition results and other comprehensive income of the joint venture is included in the consolidated statement of profit or loss and consolidated other comprehensive income, respectively. In addition, when there has been a change recognised directly in the equity of the joint venture, the Target Group recognises its share of any changes, when applicable, in the consolidated statement of changes in equity. Unrealised gains and losses resulting from transactions between the Target Group and its joint venture are eliminated to the extent of the Target Group's investments in the joint venture, except where unrealised losses provide evidence of an impairment of the assets transferred. Goodwill arising from the acquisition of the joint venture is included as part of the Target Group's investments in the joint venture.

Business combinations and goodwill

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

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

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

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

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

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

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

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

Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either in the principal market for the asset or liability, or in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or the most advantageous market must be accessible by the Target Group. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Target Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

Level 1 — based on quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2 — based on valuation techniques for which the lowest level input that is significant to the fair value measurement is observable, either directly or indirectly

Level 3 — based on valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Target Group determines whether transfers have occurred between levels in the hierarchy by reassessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

Impairment of non-financial assets

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

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

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

Related parties

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

(a) the party is a person or a close member of that person's family and that person:

(i) has control or joint control over the Target Company;

(ii) has significant influence over the Target Company; or

(iii) is a member of the key management personnel of the Target Group or of a parent of the Target Company;

or

(b) the party is an entity where any of the following conditions applies:

(i) the entity and the Target Company are members of the same group;

(ii) one entity is an associate or joint venture of the other entity (or of a parent, subsidiary or fellow subsidiary of the other entity);

(iii) the entity and the Target Company are joint ventures of the same third party;

(iv) one entity is a joint venture of a third entity and the other entity is an associate of the third entity;

(v) the entity is a post-employment benefit plan for the benefit of employees of either the Target Group or an entity related to the Target Group;

(vi) the entity is controlled or jointly controlled by a person identified in (a);

(vii) a person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity); and

(viii) the entity, or any member of a group of which it is a part, provides key management personnel services to the Target Group or to the parent of the Target Company.

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

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

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

Building and leasehold land	2 to 33 years
Machinery and equipment	2 to 24 years
Leasehold improvements	Over the lease terms or 2¾ to 40 years

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

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

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

Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value at the date of acquisition. The useful lives of intangible assets are assessed to be either finite or indefinite.

Intangible assets with finite lives are subsequently amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year/period end.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash generating unit level. Such intangible assets are not amortised. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether the indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is accounted for on a prospective basis.

Trademarks

Trademarks are stated at cost less any impairment losses and are amortised on the straight-line basis over their estimated useful lives of thirty to forty years.

Product technology, licence and completed programs

The product technology, licence and completed programs are stated at cost less any impairment losses and are amortised on the straight-line basis over their estimated useful lives of ten to thirty years.

Customer relationships

Customer relationships are stated at cost less any impairment losses and are amortised on the straight-line basis over their useful lives of fourteen to fifteen years.

Other intangible assets are stated at cost less any impairment losses and are amortised on the straight-line basis over their useful lives of two to five years.

Research and development costs

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

Expenditure incurred on projects to develop new products is capitalised and deferred only when the Target Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development. Product development expenditure which does not meet these criteria is expensed when incurred. Development costs are stated at cost less any impairment losses. No amortisation is recognised for development costs as the projects are still in development stage. Management is in the process of assessing the amortisation period applicable to the development costs.

Leases

Leases that transfer substantially all the rewards and risks of ownership of assets to the Target Group, other than legal title, are accounted for as finance leases. At the inception of a finance lease, the cost of the leased asset is capitalised at the present value of the minimum lease payments and recorded together with the obligation, excluding the interest element, to reflect the purchase and financing. Assets held under capitalised finance leases, including prepaid land lease payments under finance leases, are included in property, plant and equipment, and depreciated over the shorter of the lease terms and the estimated useful lives of the assets. The finance costs of such leases are charged to profit or loss so as to provide a constant periodic rate of charge over the lease terms.

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

Financial assets

Initial recognition and measurement

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

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

Subsequent measurement

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

Loans and receivables

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

Derecognition of financial assets

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

- the rights to receive cash flows from the asset have expired; or

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

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

Financial liabilities

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, loans and borrowings, or as derivatives designated as hedging instruments in an effective hedge, as appropriate.

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

The Target Group's financial liabilities include trade payables, other payables and accruals, interest-bearing loans and borrowings and amounts payable to group companies. All these financial liabilities are initially stated at fair value less directly attributable transaction costs and are subsequently measured at amortised cost, using the effective interest rate method unless the effect of discounting would be immaterial, in which case they are stated at cost. The related interest expense is recognised within finance costs in profit or loss. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the effective interest rate amortisation process.

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

Derecognition of financial liabilities

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

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

Offsetting of financial instruments

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

Inventories

Inventories are stated at the lower of cost and net realisable value. Costs incurred in bringing each product to its present location and conditions are accounted for as follows:

- Raw materials - Purchase cost on a first in/first out basis.

- Finished goods and work in progress - Cost of direct materials and labour and a proportion of manufacturing overhead based on normal operating capacity, but excluding borrowing costs.

Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Cash and cash equivalents

For the purpose of the consolidated statement of cash flows, cash and cash equivalents comprise cash on hand with original maturity of less than three months when acquired.

For the purpose of the consolidated statement of financial position, cash and cash equivalents comprise cash on hand and at banks, which are not restricted as to use.

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the end of the reporting period of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in profit or loss.

Warranty provisions

Provisions for warranty-related costs are recognised when the product is sold or service is provided to the customer. Initial recognition is based on historical experience. The initial estimate of warranty-related costs is revised annually.

The adequacy of the pre-existing warranty liabilities is assessed regularly and the reserve is adjusted as necessary based on a review of historic warranty experience with respect to the applicable business or products, as well as the length and actual terms of the warranties, which are typically three years. The warranty reserve is included in other provisions within the consolidated statement of financial position.

Product liability provisions

Provisions for product liability claims are made when there are present or future expected claims which challenge the safety of the products. The Target Group has general liability and other insurance policies to cover product liabilities. Initial recognition is based on historical experience. The initial estimate of product liability costs is revised annually based on current year's development of present and future expected claims.

The adequacy of the pre-existing product liabilities is assessed regularly and the provision is adjusted as necessary based on a review of historic claim experience with respect to the relevant businesses or products, as well as the length and actual terms of the possible claims.

Other liabilities

Other liabilities mainly include provisions for deposits. Customer deposits are payments from customers related to engines. Once engines are returned, these amounts are refunded to the customers. The utilisation of these provisions is uncertain as it depends on the customer returning the engines.

The adequacy of the pre-existing provisions for deposits is assessed regularly and the provisions are adjusted as necessary based on a review of historic claim experience with respect to the relevant businesses or products, as well as the length and actual terms of the possible claims.

Income tax

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

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

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

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

- when the deferred tax liability arises from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with investments in subsidiaries and a joint venture, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

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

- when the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with investments in subsidiaries and a joint venture, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

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

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

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

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Target Group and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received or receivable, net of returns and discounts.

Revenue from the sale of goods is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer, usually on delivery of the goods.

Revenue from the provision of services is recognised when the service is performed.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e., 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. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised. All other borrowing costs are expensed in the period in which they are incurred. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

Foreign currencies

The Historical Financial Information is presented in US$. The Target Company's functional currency is Hong Kong dollar. The presentation currency of the Target Group is different from the functional currency of the Target Company because the functional currency of the major subsidiaries of the Target Group is US$. Each entity in the Target Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions recorded by the entities in the Target Group are initially recorded using their respective functional currency rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rates of exchange ruling at the end of the reporting period. Differences arising on settlement or translation of monetary items are recognised in profit or loss.

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

The functional currency of the subsidiaries are currencies other than the US$. As at the end of each of the Relevant Periods, the assets and liabilities of the entity is translated into US$ at the exchange rates prevailing at the end of each of the Relevant Periods and its profit or loss is translated into US$ at the weighted average exchange rates for the year/period.

The resulting exchange differences are recognised in other comprehensive income and accumulated in the foreign currency translation reserve. On disposal of a foreign operation, the component of other comprehensive income relating to that particular foreign operation is recognised in profit or loss.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on acquisition are treated as assets and liabilities of the foreign operation and translated at the closing rate.

For the purpose of the consolidated statement of cash flows, the cash flows of overseas subsidiaries are translated into US$ at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of the overseas subsidiary which arise throughout the year/period are translated into US$ at the weighted average exchange rates for the year/period.

Employee benefits

Pension schemes

CMI sponsors a defined benefit pension plan as well as a retiree medical and life insurance plan. CMI's defined benefit pension plan requires contributions to be made to a third party trustee managed fund. The cost of providing benefits under the defined benefit plan is determined actuarially. Actuarial gains and losses for the defined benefit plan are recognised in other comprehensive income and are not reclassified to profit or loss in subsequent periods.

The defined benefit asset or liability comprises the present value of the defined benefit obligation (using a discount rate based on high quality corporate bonds), less past service costs and less the fair value of plan assets out of which the obligations are to be settled.

The Target Group's accounting policy for defined benefit plans is to recognise actuarial gains and losses in the period in which they occur in full in other comprehensive income in accordance with HKAS 19 *Employee Benefits*.

The employees of a subsidiary of the Target Company which operates in Mainland China are required to participate in a central pension scheme operated by the local municipal government. The subsidiary is required to contribute a certain percentage of their payroll costs to the central pension scheme. The contributions are charged to profit or loss as they become payable in accordance with the rules of the central pension scheme.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

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

Judgements

In the process of applying the Target Company's accounting policies, management has not made any significant judgement, apart from those involving estimations, which have significant effect on the amounts recognised in the Historical Financial Information.

Estimation uncertainty

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

Impairment of goodwill

The Target Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value is use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Target Group to make an estimate of the expected future cash flows from the cash-generating units and also to choose a suitable discount rate in order to calculate the present value of those cash flows.

Impairment of non-financial assets (other than goodwill)

Impairment exists when the carrying value of an asset or cash generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The fair value less costs to sell calculation is based on available data from binding sales transactions, conducted at arm's length, for similar assets or observable market prices less incremental costs for disposing of the asset. The value in use calculation is based on a discounted cash flow model. The cash flows are derived from the budget for the next five years and do not include restructuring activities that the Target Group is not yet committed to or significant future investments that will enhance the asset's performance of the cash generating unit being tested. The recoverable amount is most sensitive to the discount rate used for the discounted cash flow model as well as the expected future cash-inflows and the growth rate used for extrapolation purposes.

Taxes

Uncertainties exist with respect to the interpretation of complex tax regulations, changes in tax laws, and the amount and timing of future taxable income. Differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to tax income and expense already recorded. The Target Group establishes provisions, based on reasonable estimates, for possible consequences of audits by the tax authorities of the respective jurisdictions in which it operates. The amount of such provisions is based on various factors, such as experience of previous tax audits and differing interpretations of tax regulations by the taxable entity and the responsible tax authority. As the Target Group assesses the probability for litigation and subsequent cash outflow with respect to taxes as remote, no contingent liability has been recognised.

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and the level of future taxable profits together with future tax planning strategies.

Pension benefits

The cost of defined benefit pension plans and other post-employment medical benefits and the present value of the pension obligation are determined using actuarial valuations. An actuarial valuation involves making various assumptions which may differ from actual developments in the future. These include the determination of the discount rate, mortality rates and retirement dates. Due to the complexity of the valuation, the underlying assumptions and its long-term nature, a defined benefit obligation is highly sensitive to changes in these assumptions. All assumptions are reviewed at each reporting date.

Development programs in progress

Development costs are capitalised in accordance with the accounting policy in note 2.4. Initial capitalisation of costs is based on management's judgment that technological and economic feasibility is confirmed, usually when a product development project has reached a defined milestone according to an established project management model. Further information about the reconciliation of the carrying amount at the beginning and end of the reporting periods is included in note 12.

Provisions

Provisions are recorded in accordance with the accounting policy in note 2.4. Initial recognition and regular assessment for the adequacy of the provisions are estimated based on historical experience and management judgment. These include the determination of the timing, amount of future expenditures expected to be required to settle the obligation and the discount rate when the effect of discounting is material.

4. SEGMENT INFORMATION

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

(a) the engines and parts business segment engages in the design, development and production of new and rebuilt piston engines, ignition systems and spare parts for major general aviation airframe manufacturers; and

(b) the repair and maintenance business segment engages in the provision repair and maintenance services for aircraft engines.

Management monitors the results of the Target Group's operating segments separately for the purpose of making decisions about resources allocation and performance assessment. Segment performance is evaluated based on reportable segment profit, which is a measure of adjusted profit before tax for the years ended 31 December 2014, 2015 and 2016 and six months ended 30 June 2016 and 2017. The adjusted profit before tax for the years ended 31 December 2014, 2015 and 2016 and six months ended 30 June 2016 and 2017 is measured consistently with the Target Group's profit/(loss) before tax for the years ended 31 December 2014, 2015 and 2016 and the six months ended 30 June 2016 and 2017 except that certain income and gains or losses relating to impairment of goodwill, finance costs and other unallocated expenses are excluded from such measurement.

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

	Engines and parts business			Repair and maintenance business			Total		
	Year ended 31 December			Year ended 31 December			Year ended 31 December		
	2014	2015	2016	2014	2015	2016	2014	2015	2016
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*
Segment revenue:									
Sales to external customers	154,784	150,160	185,074	6,660	13,529	19,241	161,444	163,689	204,315
Intersegment sales	8,187	11,862	3,669	575	501	419	8,762	12,363	4,088
	162,971	162,022	188,743	7,235	14,030	19,660	170,206	176,052	208,403
Reconciliation:									
Elimination of intersegment sales							(8,762)	(12,363)	(4,088)
Reportable segment revenue							161,444	163,689	204,315
Segment results	3,300	15,551	19,819	1,377	(259)	1,105	4,677	15,292	20,924
Reconciliation:									
Elimination of intersegment results							(42)	(37)	—
Impairment of goodwill							—	—	(86)
Finance costs							(8,769)	(8,785)	(10,793)
Corporate and other unallocated expenses							(885)	(822)	(510)
Profit/(loss) before tax for the year							(5,019)	5,648	9,535
Other segment information:									
Depreciation	(6,127)	(5,568)	(5,397)	(294)	(528)	(568)	(6,421)	(6,096)	(5,965)
Unallocated depreciation							(45)	(45)	(36)
							(6,466)	(6,141)	(6,001)
Amortisation	(3,576)	(3,763)	(4,199)	(138)	(556)	(433)	(3,714)	(4,319)	(4,632)
Reversal of provision/(provision) of trade receivables	150	(647)	217	(12)	(40)	—	138	(687)	217
Capital expenditure	(10,442)	(16,275)	(12,093)	(877)	(6,633)	(747)	(11,319)	(22,908)	(12,840)

	Engines and parts business Six months ended 30 June		Repair and maintenance business Six months ended 30 June		Total Six months ended 30 June	
	2016	**2017**	**2016**	**2017**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*
	(Unaudited)		*(Unaudited)*		*(Unaudited)*	
Segment revenue:						
Sales to external customers	90,148	93,018	11,043	6,414	101,191	99,432
Intersegment sales	3,589	165	114	574	3,703	739
	93,737	93,183	11,157	6,988	104,894	100,171
Reconciliation:						
Elimination of intersegment sales					(3,703)	(739)
Reportable segment revenue					101,191	99,432
Segment results	8,600	10,806	858	(264)	9,458	10,542
Reconciliation:						
Finance costs					(5,285)	(5,386)
Corporate and other unallocated expenses					(46)	(244)
Profit before tax for the period					4,127	4,912
Other segment information:						
Depreciation	(2,672)	(2,766)	(260)	(327)	(2,932)	(3,093)
Unallocated depreciation					(21)	(15)
					(2,953)	(3,108)
Amortisation	(2,095)	(2,123)	(251)	(178)	(2,346)	(2,301)
Provision of trade receivables	—	(150)	—	(200)	—	(350)
Capital expenditure	(4,667)	(6,701)	(104)	(356)	(4,771)	(7,057)

* Capital expenditure consists of additions to property, plant and equipment and intangible assets excluding goodwill from business combinations.

Geographical information

(a) Revenue from external customers

	Year ended 31 December			Six months ended 30 June	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
				(Unaudited)	
North America	125,650	128,788	162,980	78,752	76,829
Europe	19,737	20,187	25,357	12,409	11,651
Others	16,057	14,714	15,978	10,030	10,952
	161,444	163,689	204,315	101,191	99,432

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

(b) Non-current assets

Over 90% of the Target Group's assets were located in the USA as at 31 December 2014, 2015 and 2016. 89% and 11% of the Target Group's assets were located in the USA and Germany, respectively, as at 30 June 2017.

Information about major customers

Revenue from each of the major customers, which individually amounted to 10% or more of the Target Group's revenue, is set out below:

	Year ended 31 December			Six months ended 30 June	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
				(Unaudited)	
Customer A	20,226	18,912	*N/A*	10,801	*N/A*
Customer B	17,371	*N/A*	*N/A*	*N/A*	*N/A*
Customer C	*N/A*	*N/A*	48,215	13,134	33,726

[N/A] *Less than 10% of the Target Group's total revenue.*

5. REVENUE

Revenue represents the net invoiced value of goods sold, after allowances for returns and trade discounts and services rendered during the Relevant Periods. An analysis of revenue is as follows:

	Year ended 31 December			Six months ended 30 June	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
				(Unaudited)	
Revenue					
Sales of goods	154,784	150,160	185,074	90,148	93,018
Rendering of services	6,660	13,529	19,241	11,043	6,414
	161,444	163,689	204,315	101,191	99,432

6. FINANCE COSTS

An analysis of finance costs is as follows:

	Year ended 31 December			Six months ended 30 June	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
				(Unaudited)	
Interest on interest-bearing loans and borrowings	7,916	8,040	8,974	4,576	4,469
Interest on an amount due to a fellow subsidiary (note 30(v))	38	171	1,109	299	601
Guarantee fee recharged by the immediate holding company (note 30(ii))	744	502	630	393	273
Others	71	72	80	17	43
	8,769	8,785	10,793	5,285	5,386

7. PROFIT/(LOSS) BEFORE TAX

Profit/(loss) before tax is arrived at after charging/(crediting):

	Year ended 31 December			Six months ended 30 June	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
				(Unaudited)	
Cost of inventories sold	100,696	92,131	127,024	61,228	62,955
Cost of services provided	11,414	19,776	11,859	6,752	5,000
Research and development costs:					
Current year expenditure	4,278	5,433	5,168	2,880	2,269
Depreciation (note 10)	6,466	6,141	6,001	2,953	3,108
Amortisation of intangible assets (note 12)	3,714	4,319	4,632	2,346	2,301
Minimum lease payments under operating leases	575	1,524	1,983	1,099	954
Employee benefit expense:					
Wages and salaries	16,008	16,796	17,318	8,442	8,883
Pension scheme contributions					
- defined contribution schemes	1,702	1,626	1,621	816	828
- defined benefit schemes	515	506	479	239	242
	18,225	18,928	19,418	9,497	9,953
Provision/(reversal of provision) of trade receivables (note 16)	(138)	687	(217)	—	350
Impairment of items of property, plant and equipment (note 10)*	—	—	306	—	—
Impairment of goodwill (note 11)*	—	—	86	—	—
Loss/(gain) on disposal of items of property, plant and equipment, net*	1	—	75	(31)	—
Loss on disposal of other intangible assets*	30	2	91	—	—
Reversal of provisions for deposits*	—	(619)	(136)	—	—
Foreign exchange differences, net*	277	631	(61)	5	(16)

* *These items are included in the "Other operating income/(expenses), net" in the consolidated statement of profit or loss and other comprehensive income.*

8. DIRECTORS' REMUNERATION AND FIVE HIGHEST PAID EMPLOYEES

(a) Directors' remuneration

No director of the Target Company received any fees or emoluments in respect of their services rendered to the Target Group during the years ended 31 December 2014, 2015 and 2016 and the six months ended 30 June 2016 and 2017.

There was no arrangement under which a director waived or agreed to waive any remuneration during the years ended 31 December 2014, 2015 and 2016 and the six months ended 30 June 2016 and 2017.

During the years ended 31 December 2014, 2015 and 2016 and the six months ended 30 June 2016 and 2017, no remuneration was paid by the Target Group to the directors of the Target Company as an inducement to join or upon joining the Target Group or as compensation for loss of office.

(b) Five highest paid employees

Details of the remuneration of the five highest paid employees as the Target Group who are not directors of the Target Company for the Relevant Periods are as follows:

	Year ended 31 December			Six months ended 30 June	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
				(Unaudited)	
Salaries, allowances and benefits in kind	1,852	1,997	1,895	1,077	1,353

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

	Year ended 31 December			Six months ended 30 June	
	2014	2015	2016	2016	2017
				(Unaudited)	
HK$500,001 to HK1,000,000 (US$64,433 to US$128,866)	—	—	—	1	—
HK$1,000,001 to HK1,500,000 (US$128,866 to US$193,299)	—	—	—	2	1
HK$1,500,001 to HK2,000,000 (US$193,299 to US$257,732)	—	—	—	1	2
HK$2,000,001 to HK$2,500,000 (US$257,732 to US$322,165)	2	—	2	—	1
HK$2,500,001 to HK$3,000,000 (US$322,165 to US$386,598)	2	4	2		
HK$3,500,001 to HK4,000,000 (US$451,031 to US$515,464)	—	—	—	1	—
HK$4,000,001 to HK4,500,000 (US$515,464 to US$579,897)	—	—	—	—	1
HK$4,500,001 to HK$5,000,000 (US$579,897 to US$644,330)	1	1	—	—	—
HK$5,000,001 to HK$5,500,000 (US$644,330 to US$708,763)	—	—	1	—	—
	5	5	5	5	5

9. INCOME TAX

No provision for Hong Kong profits tax has been made as the Target Group did not generate any assessable profits arising in Hong Kong during the Relevant Periods. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries in which the Target Group operates.

	Year ended 31 December			Six months ended 30 June	
	2014	2015	2016	2016	2017
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
				(Unaudited)	
Current - Elsewhere					
Charge for the year/period	225	359	288	212	217
Underprovision/(overprovision) in prior years	124	—	(225)	(104)	93
Deferred (note 14)	2,261	(6,304)	4,100	1,255	998
Total tax charge/(credit) for the year/period	2,610	(5,945)	4,163	1,363	1,308

A reconciliation of the tax expense/(credit) applicable to profit/(loss) before tax at the statutory rates for the countries in which the Target Group's subsidiaries are domiciled to the tax expense/(credit) at the Target Group's effective tax rate, are as follows:

	Year ended 31 December						Six months ended 30 June			
	2014		2015		2016		2016		2017	
	US$'000	*%*	*US$'000*	*%*	*US$'000*	*%*	*US$'000*	*%*	*US$'000*	*%*
							(Unaudited)			
Profit/(loss) before tax	(5,019)		5,648		9,535		4,127		4,912	
Tax at the statutory tax rates	(1,207)	24.0	2,537	44.9	3,754	39.4	1,521	36.9	1,681	34.2
Adjustments in respect of current tax of previous years	124	(2.5)	—	—	(225)	(2.4)	(104)	(2.5)	93	1.9
Expenses not deductible for tax	22	(0.4)	4	0.1	563	5.9	530	12.8	18	0.3
Recognition of temporary differences in prior years	—	—	(9,628)	(170.5)	—	—	(338)	(8.2)	(286)	(5.8)
Tax losses not recognised	3,569	(71.1)	1,226	21.7	167	1.8	—	—	—	—
Others	102	(2.0)	(84)	(1.5)	(96)	(1.0)	(246)	(6.0)	(198)	(4.0)
Tax expense/(credit) at the effective rate	2,610	(52.0)	(5,945)	(105.3)	4,163	43.7	1,363	33.0	1,308	26.6

At the end of the Relevant Periods, the principal component of the Target Group's unrecognised deferred tax asset is as follows:

	As at 31 December			As at 30 June
	2014	2015	2016	2017
	US$'000	*US$'000*	*US$'000*	*US$'000*
Estimated tax losses available for offset against future taxable profits	52,319	15,124	15,153	15,372

The tax losses have not been recognised as it is not probable that sufficient future taxable profits will be available against which the temporary difference can be utilised.

10. PROPERTY, PLANT AND EQUIPMENT

	Building and leasehold land	Machinery and equipment	Leasehold improvements	Construction in progress	Total
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
31 December 2014					
At 1 January 2014:					
Cost	6,989	33,761	6,123	1,143	48,016
Accumulated depreciation	(100)	(8,609)	(1,320)	—	(10,029)
Net carrying amount	6,889	25,152	4,803	1,143	37,987
At 1 January 2014 , net of accumulated depreciation	6,889	25,152	4,803	1,143	37,987
Additions	136	582	109	3,216	4,043
Acquisition of business (note 26)	—	342	—	44	386
Transfers	—	1,758	696	(2,454)	—
Depreciation provided during the year	(168)	(5,755)	(543)	—	(6,466)
Disposals	—	(168)	—	—	(168)
Exchange realignment	(726)	(689)	—	(24)	(1,439)
At 31 December 2014, net of accumulated depreciation	6,131	21,222	5,065	1,925	34,343
At 31 December 2014:					
Cost	6,376	35,169	6,928	1,925	50,398
Accumulated depreciation	(245)	(13,947)	(1,863)	—	(16,055)
Net carrying amount	6,131	21,222	5,065	1,925	34,343

	Building and leasehold land	Machinery and equipment	Leasehold improvements	Construction in progress	Total
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
31 December 2015					
At 1 January 2015:					
Cost	6,376	35,169	6,928	1,925	50,398
Accumulated depreciation	(245)	(13,947)	(1,863)	—	(16,055)
Net carrying amount	6,131	21,222	5,065	1,925	34,343
At 1 January 2015 , net of accumulated depreciation	6,131	21,222	5,065	1,925	34,343
Additions	170	1,202	—	4,297	5,669
Acquisitions of businesses (note 26)	—	5,779	—	147	5,926
Transfers	6	1,352	1,233	(2,591)	—
Depreciation provided during the year	(147)	(5,363)	(631)	—	(6,141)
Disposals	—	(42)	—	—	(42)
Exchange realignment	(554)	(444)	—	(27)	(1,025)
At 31 December 2015, net of accumulated depreciation	5,606	23,706	5,667	3,751	38,730
At 31 December 2015:					
Cost	5,975	42,483	8,161	3,751	60,370
Accumulated depreciation	(369)	(18,777)	(2,494)	—	(21,640)
Net carrying amount	5,606	23,706	5,667	3,751	38,730
31 December 2016					
At 1 January 2016:					
Cost	5,975	42,483	8,161	3,751	60,370
Accumulated depreciation	(369)	(18,777)	(2,494)	—	(21,640)
Net carrying amount	5,606	23,706	5,667	3,751	38,730
At 1 January 2016 , net of accumulated depreciation	5,606	23,706	5,667	3,751	38,730
Additions	9	2,821	45	1,162	4,037
Transfers	40	1,141	1,799	(2,980)	—
Disposals	—	(1,345)	(62)	(553)	(1,960)
Depreciation provided during the year	(147)	(5,058)	(796)	—	(6,001)
Impairment	—	(306)	—	—	(306)

	Building and leasehold land	Machinery and equipment	Leasehold improvements	Construction in progress	Total
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
Exchange realignment	(173)	(160)	—	(2)	(335)
At 31 December 2016, net of accumulated depreciation and impairment	5,335	20,799	6,653	1,378	34,165
At 31 December 2016:					
Cost	5,833	43,896	9,924	1,378	61,031
Accumulated depreciation and impairment	(498)	(23,097)	(3,271)	—	(26,866)
Net carrying amount	5,335	20,799	6,653	1,378	34,165
30 June 2017					
At 1 January 2017:					
Cost	5,833	43,896	9,924	1,378	61,031
Accumulated depreciation and impairment	(498)	(23,097)	(3,271)	—	(26,866)
Net carrying amount	5,335	20,799	6,653	1,378	34,165
At 1 January 2017 , net of accumulated depreciation and impairment	5,335	20,799	6,653	1,378	34,165
Additions	—	854	—	1,216	2,070
Transfers	55	259	50	(364)	—
Disposals	—	(1,388)	—	(688)	(2,076)
Depreciation provided during the period	(73)	(2,380)	(655)	—	(3,108)
Exchange realignment	389	341	—	8	738
At 30 June 2017, net of accumulated depreciation and impairment	5,706	18,485	6,048	1,550	31,789
At 30 June 2017:					
Cost	6,317	44,084	9,974	1,550	61,925
Accumulated depreciation and impairment	(611)	(25,599)	(3,926)	—	(30,136)
Net carrying amount	5,706	18,485	6,048	1,550	31,789

Management made a provision for impairment of US$306,000 on certain idle property, plant and equipment by comparing to their recoverable amounts in profit or loss for the year ended 31 December 2016. The recoverable amounts of the assets are determined based on management estimated fair value less cost of disposal based on the actual sales proceeds subsequent to the end of that year.

11. GOODWILL

	US$'000
Cost at 1 January 2014	107,180
Business combination (note 26)	86
Exchange realignment	(552)
At 31 December 2014 and 1 January 2015	106,714
Business combinations (note 26)	3,081
Exchange realignment	(422)
At 31 December 2015 and 1 January 2016	109,373
Impairment during the year	(86)
Exchange realignment	(134)
At 31 December 2016 and 1 January 2017	109,153
Exchange realignment	300
Net carrying amount at 30 June 2017	109,453

The gross amount of goodwill and accumulated impairment losses amounted to US$109,239,000 and US$86,000 as at 31 December 2016 and amounted to US$109,539,000 and US$86,000 at 30 June 2017, respectively.

Impairment testing of goodwill

Goodwill has been allocated to the following cash-generating units ("CGU") for impairment testing:

- Sale of engines and parts and repair and maintenance business in Alabama, USA CGU ("Alabama CGU");
- Repair and maintenance business in Florida, USA CGU ("Florida CGU"); and
- Sale of engines and parts in Germany CGU ("Germany CGU")

The carrying amount of goodwill allocated to each of the CGUs is as follows:

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Alabama CGU	102,458	104,484	104,484	104,484
Florida CGU	—	1,055	1,055	1,055
Germany CGU	4,170	3,748	3,614	3,914
Others	86	86	—	—
	106,714	109,373	109,153	109,453

The recoverable amount of the cash-generating unit has been determined based on a value in use calculation using cash flow projections based on financial budgets covering a five-year period approved by management. The discount rates applied to the cash flow projections and the growth rates used to extrapolate the cash flows beyond the five-year period periods are as follows:

	Year ended 31 December			Six months ended 30 June
	2014	**2015**	**2016**	**2017**
	%	%	%	%
Alabama CGU				
Discount rate	12.5	12.5	13.5	13.5
Growth rate	5	5	5	5
Florida CGU				
Discount rate	N/A	20.4	30.0	30.0
Growth rate	N/A	5	5	5
Germany CGU				
Discount rate	10.6	7.7	9.5	9.5
Growth rate	1	1	1	1

Assumptions were used in the value in use calculation of the CGUs for 31 December 2014, 2015 and 2016 and 30 June 2017. The following describes each key assumption on which management has based its cash flow projections to undertake impairment testing of goodwill:

Financial budget - The basis used to determine the value assigned to the financial budget is the best estimate based on the comparable of the same industry and the respective long term growth rates are applied to extrapolate the cash flows beyond the five-year period.

Discount rates - The discount rates used are before tax and reflect specific risks relating to the relevant units. The discount rates are consistent with external information sources.

During the year ended 31 December 2016, the Target Group recognised an impairment loss of US$86,000 in connection with the goodwill arising from the acquisition of the business of Southern Avionics and Communications, Inc. ("SAC") by CMS. The impairment was recognised based on the results of the impairment test for the goodwill for which the recoverable amount is the value in use.

No impairment of goodwill was recognised for the years ended 31 December 2014 and 2015 and the six months ended 30 June 2016 and 2017.

12. OTHER INTANGIBLE ASSETS

	Development programs in progress	Trademarks	Product technology, licence and completed programs	Customer relationships	Others	Total other intangible assets
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*
31 December 2014						
Cost at 1 January 2014, net of accumulated amortisation	11,996	21,697	65,687	4,329	456	104,165
Additions	6,622	—	128	—	140	6,890
Transfers	(2,232)	—	2,232	—	—	—
Amortisation provided during the year	—	(668)	(2,489)	(383)	(174)	(3,714)
Disposals	—	—	—	—	(30)	(30)
Exchange realignment	(226)	(252)	(1,002)	—	—	(1,480)
At 31 December 2014	16,160	20,777	64,556	3,946	392	105,831
At 31 December 2014:						
Cost	16,160	22,883	72,782	5,362	966	118,153
Accumulated amortisation	—	(2,106)	(8,226)	(1,416)	(574)	(12,322)
Net carrying amount	16,160	20,777	64,556	3,946	392	105,831
31 December 2015						
Cost at 1 January 2015, net of accumulated amortisation	16,160	20,777	64,556	3,946	392	105,831
Additions	6,159	—	92	—	412	6,663
Acquisitions of businesses (note 26)	—	410	1,000	2,920	320	4,650
Transfers	(14,772)	—	14,772	—	—	—
Amortisation provided during the year	—	(733)	(2,628)	(510)	(448)	(4,319)
Disposals	—	—	—	—	(2)	(2)
Exchange realignment	(256)	(185)	(756)	—	—	(1,197)
At 31 December 2015	7,291	20,269	77,036	6,356	674	111,626

	Development programs in progress	Trademarks	Product technology, licence and completed programs	Customer relationships	Others	Total other intangible assets
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*
At 31 December 2015:						
Cost	7,291	23,086	87,831	8,282	1,696	128,186
Accumulated amortisation	—	(2,817)	(10,795)	(1,926)	(1,022)	(16,560)
Net carrying amount	7,291	20,269	77,036	6,356	674	111,626
31 December 2016						
Cost at 1 January 2016, net of accumulated amortisation	7,291	20,269	77,036	6,356	674	111,626
Additions	8,294	—	55	—	454	8,803
Amortisation provided during the year	—	(735)	(2,998)	(584)	(315)	(4,632)
Disposals	—	—	(91)	—	—	(91)
Exchange realignment	(257)	(45)	(219)	—	—	(521)
At 31 December 2016	15,328	19,489	73,783	5,772	813	115,185
At 31 December 2016:						
Cost	15,328	23,020	87,531	8,282	2,150	136,311
Accumulated amortisation	—	(3,531)	(13,748)	(2,510)	(1,337)	(21,126)
Net carrying amount	15,328	19,489	73,783	5,772	813	115,185
30 June 2017						
Cost at 1 January 2017, net of accumulated amortisation	15,328	19,489	73,783	5,772	813	115,185
Additions	4,758	—	17	—	212	4,987
Transfers	(823)	2	821	—	—	—
Amortisation provided during the period	—	(355)	(1,516)	(292)	(138)	(2,301)
Exchange realignment	527	99	539	—	—	1,165
At 30 June 2017	19,790	19,235	73,644	5,480	887	119,036
At 30 June 2017:						
Cost	19,790	23,169	89,004	8,282	2,272	142,517
Accumulated amortisation	—	(3,934)	(15,360)	(2,802)	(1,385)	(23,481)
Net carrying amount	19,790	19,235	73,644	5,480	887	119,036

13. INVESTMENT IN A JOINT VENTURE

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Share of net assets	35	36	50	85

Particulars of the Target Group's joint venture at the end of each of the Relevant Periods are as follows:

Name	Particulars of issued shares held	Place of registration and business	Percentage of Ownership interest	Percentage of Voting power	Percentage of Profit Sharing	Principal activities
Southern Star Avionics, LLC	Registered capital of US$1 each	USA	50	50	50	Design and installation of modifications to aircrafts

The investment in the joint venture is directly held by a wholly-owned subsidiary of the Target Company.

14. DEFERRED TAX ASSETS/(LIABILITIES)

The movements in the Target Group's deferred tax assets/(liabilities) during the Relevant Periods are as follows:

	Consolidated statement of financial position				Consolidated statement of profit or loss and other comprehensive income				
	As at 31 December			As at 30 June	Year ended 31 December			Six months ended 30 June	
	2014	**2015**	**2016**	**2017**	**2014**	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*
								(Unaudited)	
Provisions	—	3,645	2,882	3,491	1,225	3,645	(763)	(473)	609
Inventories - capitalisation	—	4,947	1,757	2,192	—	4,947	(3,190)	(3,153)	435
Decelerated/(accelerated) depreciation and amortisaton for tax purposes	—	(8,143)	(9,551)	(10,316)	—	(8,143)	(1,408)	(757)	(765)
Goodwill arising from business combinations	(5,961)	(8,246)	(10,626)	(11,963)	(2,261)	(2,285)	(2,380)	(1,141)	(1,337)
Tax losses	—	5,779	8,713	8,443	—	5,779	2,934	3,286	(270)
Others	—	2,486	3,111	3,226	(1,253)	2,486	625	751	115
Deferred tax credit/(expense)					(2,289)	6,429	(4,182)	(1,487)	(1,213)
Deferred tax assets/(liabilities)	(5,961)	468	(3,714)	(4,927)					

Reconciliation of deferred tax assets/(liabilities) is as follows:

	As at 31 December			As at 30 June
	2014	2015	2016	2017
	US$'000	*US$'000*	*US$'000*	*US$'000*
At 1 January	(3,672)	(5,961)	468	(3,714)
Tax credit/(expense) for the year/period recognised in profit or loss	(2,261)	6,304	(4,100)	(998)
Tax credit/(expense) for the year/period recognised in other comprehensive income	(28)	125	(82)	(215)
At 31 December/30 June	(5,961)	468	(3,714)	(4,927)

As at 31 December 2015 and 2016 and 30 June 2017, the Target Group had estimated USA federal tax losses totalling US$14,200,000, US$23,300,000 and US$22,000,000, respectively, that will expire starting from 2032.

At 31 December 2015 and 2016 and 30 June 2017, the Target Group had estimated USA state net operating losses totalling US$19,700,000, US$27,200,000 and US$32,700,000, respectively, that will expire starting from 2026.

15. INVENTORIES

	As at 31 December			As at 30 June
	2014	2015	2016	2017
	US$'000	*US$'000*	*US$'000*	*US$'000*
Raw materials	25,009	31,902	34,824	42,018
Work in progress	10,949	11,620	13,019	13,944
Finished goods	3,096	2,897	4,158	3,676
	39,054	46,419	52,001	59,638

16. TRADE AND OTHER RECEIVABLES

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Trade receivables	11,588	23,762	14,949	16,067
Impairment	(452)	(1,139)	(729)	(1,079)
Trade receivables, net	11,136	22,623	14,220	14,988
Other receivables	876	2,077	2,362	2,072
Total trade and other receivables, net	12,012	24,700	16,582	17,060

Notes:

(a) The Target Group's trading terms with its customers are mainly on credit, where partial advanced payment is required for certain customers. The credit period is generally 30 days. Each customer has a maximum credit limit. The Target Group seeks to maintain strict control over its outstanding receivables to minimise credit risk. Overdue balances are reviewed regularly by senior management. As at 31 December 2014, 2015 and 2016 and 30 June 2017, the Target Group had certain concentrations of credit risk as 11%, 6%, 39% and 39%, respectively, of the Target Group's trade receivables were due from one of the Target Group's key customers. The Target Group does not hold any collateral or other credit enhancements over its trade receivable balances. Trade receivables are non-interest-bearing.

(b) An aging analysis of trade receivables as at the end of each of the Relevant Periods, based on the invoice date and net of impairment, is as follows:

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Within 1 month	6,759	2,689	8,090	8,825
1 to 2 months	3,149	5,066	2,115	2,381
2 to 3 months	685	3,816	921	902
Over 3 months	543	11,052	3,094	2,880
	11,136	22,623	14,220	14,988

(c) The movements in the provision for impairment of trade receivables are as follows:

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
At beginning of year/period	617	452	1,139	729
Impairment losses/(reversal of impairment losses) recognised (note 7)	(138)	687	(217)	350
Amount written off as uncollectable	(27)	—	(193)	—
At end of year/period	452	1,139	729	1,079

Included in the above provisions for impairment of trade receivables are provisions for individually impaired trade receivables of US$452,000, US$1,139,000, US$729,000 and US$1,079,000 with carrying amounts before provision of US$452,000, US$1,139,000, US$729,000 and US$1,079,000 as at 31 December 2014, 2015 and 2016 and 30 June 2017, respectively.

(d) An aging analysis of trade receivables as at the end of each of the Relevant Periods, that are neither individually nor collectively considered to be impaired, is as follows:

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Neither past due nor impaired	6,759	2,689	8,090	8,825
Past due but not impaired:				
Less than 1 month past due	3,149	5,066	2,115	2,381
Over 1 month past due	1,228	14,868	4,015	3,782
	11,136	22,623	14,220	14,988

Receivables that were neither past due nor impaired relate to customers for whom there was no recent history of default.

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

17. BALANCES WITH GROUP COMPANIES

Balances with fellow subsidiaries

Except for the amounts due to a fellow subsidiary of US$3,991,000, US$24,400,000, US$38,200,000 and US$48,200,000 as at 31 December 2014, 2015 and 2016 and 30 June 2017, respectively, which bore interest at rates ranging from 2.8% to 5.9% per annum, all balances with fellow subsidiaries were interest-free, unsecured and repayable on demand as at the end of each of the Relevant Periods.

Balances with the immediate holding company

Except for the amounts due to the immediate holding company of US$868,000, US$2,153,000, US$2,318,000 and US$2,194,000 as at 31 December 2014, 2015 and 2016 and 30 June 2017, respectively, which were interest-free, unsecured and not repayable within one year as at the end of each of the Relevant Periods, all balances with the immediate holding company were interest-free, unsecured and repayable on demand as at the end of each of the Relevant Periods.

18. CASH AND CASH EQUIVALENTS AND RESTRICTED BANK BALANCE

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Cash and bank balances	21,274	9,419	14,105	8,460
Less: restricted bank balance	(8,083)	—	—	—
Cash and cash equivalents	13,191	9,419	14,105	8,460

Cash at banks earns interest at floating rates based on daily bank deposit rates. The bank balances are deposited with creditworthy banks with no recent history of default. The restricted bank balance was used to secure a bank guarantee for the payment of value added tax for the business combination in 2013.

19. TRADE PAYABLES, OTHER PAYABLES AND ACCRUALS

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Trade payables	5,713	9,788	5,992	8,988
Other payables	1,496	1,280	2,581	1,611
Accruals	13,804	14,055	14,145	9,196
	21,013	25,123	22,718	19,795

An aged analysis of the trade payables as at the end of each of the Relevant Periods, based on the invoice date, is as follows:

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Within 1 month	2,336	6,327	4,989	7,704
1 to 2 months	38	735	447	710
2 to 3 months	17	295	27	276
Over 3 months	3,322	2,431	529	298
	5,713	9,788	5,992	8,988

Trade and other payables are non-interest-bearing and are normally settled on 60-days terms.

20. INTEREST-BEARING LOANS AND BORROWINGS

	As at 31 December									As at 30 June		
	2014			2015			2016			2017		
	Effective interest rate (%)	*Maturity*	*US$'000*	*Effective interest rate (%)*	*Maturity*	*US$'000*	*Effective interest rate (%)*	*Maturity*	*US$'000*	*Effective interest rate (%)*	*Maturity*	*US$'000*
Current												
Finance lease payables (note 27)	3.65%	2013 -2017	346	3.65%	2013 -2017	359	—	—	—	—	—	—
Bank loan — secured (note a)	—	—	—	—	—	—	4.22%	2026	20,000	4.44%	2026	20,000
Bank loan — unsecured (note b)	—	—	—	2.17%	On demand	4,000	—	—	—	—	—	—
Bank loan — unsecured (note c)	—	—	—	2.17%	2015 - 2020	1,600	2.17%	2015 - 2020	1,600	2.17%	2015 - 2020	1,600
			346			5,959			21,600			21,600
Non-current												
Finance lease payables (note 27)	3.65%	2013 - 2017	471	3.65%	2013 - 2017	112	—	—	—	—	—	—
Bank loan — secured (note a)	3.41%	2026	200,000	3.49%	2026	200,000	4.22%	2026	170,000	4.44%	2026	160,000
Bank loan — unsecured (note c)	—	—	—	2.17%	2015 - 2020	4,933	2.17%	2015 - 2020	3,333	2.17%	2015 - 2020	2,533
Bank loan — secured (note d)	1.99%	2016	57,097	1.58%	2019	51,322	1.46%	2019	49,491	1.50%	2019	53,595
			257,568			256,367			222,824			216,128
Total interest — bearing loans and borrowings			257,914			262,326			244,424			237,728

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Analysed into:				
Bank loans repayable:				
Within one year or on demand	—	5,600	21,600	21,600
In the second year	67,097	31,600	21,600	75,195
In the third to fifth years, inclusive	60,000	114,655	111,224	60,933
Beyond five years	130,000	110,000	90,000	80,000
	257,097	261,855	244,424	237,728
Finance lease payables:				
Within one year	346	359	—	—
In the second year	359	112	—	—
In the third to fifth years, inclusive	112	—	—	—
	817	471	—	—
	257,914	262,326	244,424	237,728

Notes:

(a) This loan is secured and carries an annual interest rate of 6-month London Interbank Offered Rate ("LIBOR") + 3% payable quarterly. Starting from October 2016, the Target Group is obligated to repay the loan principal at US$10,000,000 every 6 months until October 2026. This loan is guaranteed by the Target Company's immediate holding company and ultimate holding company.

(b) This loan was unsecured and carried an annual interest rate of 1-month LIBOR + 2%. The loan had no fixed term of repayment and subject to quarterly bank review. The loan was repaid in 2016.

(c) This loan is unsecured and carries an annual interest rate of 1-month LIBOR + 2%. The loan is repayable by monthly instalment from 2015 to 2020.

(d) This loan is secured and carries an annual interest rate of Euro Interbank Offered Rate ("EURIBOR") + 1.4% (2014 and 2015: EURIBOR + 1.5%) payable annually. The loan is repayable by 2016 for the year ended 31 December 2014 and extended in 2015 to be repayable by 2019 for the years ended 31 December 2015 and 2016. This loan is secured by an irrevocable letter of guarantee issued by the Bank of China, Beijing, which is secured by a guarantee of the Target Company's immediate holding company.

Except for the secured bank loan in note (d) which is denominated in Euro, all borrowings are denominated in US dollars.

21. DEFERRED REVENUE

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Deferred revenue	3,204	3,361	4,700	4,464
Portion classified as current liabilities	(184)	(122)	(466)	(143)
Non-current portion	3,020	3,239	4,234	4,321

22. PROVISIONS AND OTHER LIABILITIES

	Warranty provisions	**Product liability provisions**	**Other liabilities**	**Total provisions**
	US$'000	*US$'000*	*US$'000*	*US$'000*
31 December 2014				
At 1 January 2014	3,411	42,916	5,940	52,267
Provided/(reversed)	2,234	(2,250)	4,192	4,176
Utilised during the year	(2,670)	(4,813)	(4,817)	(12,300)
Increase/(decrease) in discounted amounts arising from the passage of time	5	—	(12)	(7)
Exchange realignment	(129)	—	(509)	(638)
At 31 December 2014	2,851	35,853	4,794	43,498
Portion classified as current liabilities	(1,388)	(4,528)	(642)	(6,558)
Non-current portion	1,463	31,325	4,152	36,940
31 December 2015				
At 1 January 2015	2,851	35,853	4,794	43,498
Provided/(reversed)	2,415	(14,925)	3,349	(9,161)
Utilised during the year	(2,992)	(1,479)	(3,448)	(7,919)
Increase in discounted amounts arising from the passage of time	18	—	17	35
Exchange realignment	(83)	—	(394)	(477)
At 31 December 2015	2,209	19,449	4,318	25,976
Portion classified as current liabilities	(1,239)	(851)	(882)	(2,972)
Non-current portion	970	18,598	3,436	23,004

	Warranty provisions	Product liability provisions	Other liabilities	Total provisions
	US$'000	*US$'000*	*US$'000*	*US$'000*
31 December 2016				
At 1 January 2016	2,209	19,449	4,318	25,976
Provided/(reversed)	4,058	(5,115)	2,639	1,582
Utilised during the year	(3,179)	(834)	(3,453)	(7,466)
Increase in discounted amounts arising from the passage of time	—	—	41	41
Exchange realignment	(25)	—	(95)	(120)
At 31 December 2016	3,063	13,500	3,450	20,013
Portion classified as current liabilities	(1,958)	(1,118)	(1,088)	(4,164)
Non-current portion	1,105	12,382	2,362	15,849
30 June 2017				
At 1 January 2017	3,063	13,500	3,450	20,013
Provided/(reversed)	1,079	(3,500)	1,020	(1,401)
Utilised during the period	(1,047)	—	(647)	(1,694)
Exchange realignment	57	—	246	303
At 30 June 2017	3,152	10,000	4,069	17,221
Portion classified as current liabilities	(1,380)	(1,118)	(1,611)	(4,109)
Non-current portion	1,772	8,882	2,458	13,112

The Target Group is currently involved in legal proceedings related to product liability claims. An estimate for the probable costs has been made for these claims. This estimate has been developed in consultation with the Target Group's insurers, legal counsels, historical experience and is based upon an analysis of potential results. In the opinion of the directors of the Target Company, these proceedings will not have a material adverse effect on the Target Group's consolidated financial statements. The product liability provisions were made for any present or future expected product liability claims as a result of the assessment at the respective end of the Relevant Periods.

23. DEFINED BENEFIT OBLIGATIONS

CMI United Auto Workers Pension Plan ("UAW Pension Plan")

The Target Group has a defined benefit pension plan. It is a pension plan for the United States employees which require contributions to be made to a separately administered fund. This benefit pension plan is funded. Under the plan, the employees are entitled to monthly retirement benefits or early or postponed retirement benefits when they have early or postponed retirements subject to other conditions.

Continental Motors Postretirement Life & Health Plan (formerly known as CMI Retiree Medical and Life Plan) ("CMI Life & Health Plan")

The Target Group also provides certain additional post-employment medical and life benefits to employees in the United States. These benefits are unfunded. Under the plan, the employees are entitled to receive post-employment medical benefits.

The actuarial valuations of the present value of the defined benefit obligations were carried out as at the end of each of the Relevant Periods by Newport Group, Inc. (formerly known as Daily Access Corporation), a qualified actuary, using the projected unit credit actuarial valuation method.

The principal assumptions used at the end of each of the Relevant Periods are as follows:

	As at 31 December			**As at 30 June**
	2014	**2015**	**2016**	**2017**
	%	%	%	%
Discount rate				
CMI UAW Pension Plan	4.05	4.20	4.05	3.90
CMI Life & Health Plan	3.85	4.22	4.03	3.29

A quantitative sensitivity analysis for significant assumptions at the end of each of the Relevant Periods is shown below:

	Increase in rate	**Decrease in defined benefit obligations**	**Decrease in rate**	**Increase in defined benefit obligations**
	%	*US$'000*	%	*US$'000*
As at 31 December 2014				
Discount rate	1	(299)	(1)	369
As at 31 December 2015				
Discount rate	1	(367)	(1)	440
As at 31 December 2016				
Discount rate	1	(409)	(1)	505
As at 30 June 2017				
Discount rate	1	(470)	(1)	552

The sensitivity analyses above have been determined based on a method that extrapolates the impact on defined benefit obligations as a result of reasonable changes in key assumptions occurring at the end of each of the Relevant Periods. The sensitivity analysis is based on a change in a significant assumption, keeping all other assumptions constant. The sensitivity analysis may not be representative of an actual change in the defined benefit obligations as it is unlikely that changes in assumptions would occur in isolation of one another.

The total expenses recognised as general and administrative expenses in the Target Group's profit or loss in respect of the plans are as follows:

	Year ended 31 December			**Six months ended 30 June**	
	2014	**2015**	**2016**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
				(Unaudited)	
Current service cost	472	496	459	228	232
Net interest expense	43	10	20	11	10
Net benefit expenses	515	506	479	239	242

The movements in the present value of the defined benefit obligations are as follows:

	As at 31 December			**As at 30 June**
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
At 1 January	621	751	983	853
Current service cost	472	496	459	232
Net interest expense	43	10	20	10
Benefit paid	(12)	(74)	(59)	(22)
Remeasurement losses/(gains)	(6)	130	(213)	(112)
Contribution by employer	(367)	(330)	(337)	(403)
At 31 December/30 June	751	983	853	558

The movements in the defined benefit obligations and the fair value of plan assets are as follows:

	Pension cost charged to profit or loss					Remeasurement losses/(gains) recognised in other comprehensive income					
	At 1 January	Service cost	Net interest expense/ (income)	Sub-total included in profit or loss	Benefits paid	Return on plan assets (excluding amounts included in net interest expense)	Actuarial changes arising from changes in demographic assumptions	Actuarial changes arising from changes in financial assumptions	Sub-total included in other com-prehensive income	Contribution by employer	At 31 December /30 June
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*
31 December 2014											
Defined benefit obligations	2,178	472	133	605	(29)	—	—	18	18	—	2,772
Fair value of plan assets	(1,557)	—	(90)	(90)	17	(24)	—	—	(24)	(367)	(2,021)
	621	472	43	515	(12)	(24)	—	18	(6)	(367)	751
31 December 2015											
Defined benefit obligations	2,772	496	97	593	(97)	—	75	(57)	18	—	3,286
Fair value of plan assets	(2,021)	—	(87)	(87)	23	112	—	—	112	(330)	(2,303)
	751	496	10	506	(74)	112	75	(57)	130	(330)	983
31 December 2016											
Defined benefit obligations	3,286	459	123	582	(79)	—	(58)	(128)	(186)	—	3,603
Fair value of plan assets	(2,303)	—	(103)	(103)	20	(27)	—	—	(27)	(337)	(2,750)
	983	459	20	479	(59)	(27)	(58)	(128)	(213)	(337)	853
30 June 2017											
Defined benefit obligations	3,603	232	70	302	(38)	—	—	(29)	(29)	—	3,838
Fair value of plan assets	(2,750)	—	(60)	(60)	16	(83)	—	—	(83)	(403)	(3,280)
	853	232	10	242	(22)	(83)	—	(29)	(112)	(403)	558

The major categories of the fair value of the total plan assets of the CMI UAW Pension Plan are as follows:

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Equity instruments	999	1,044	1,281	1,039
Debt instruments	998	1,047	1,378	1,569
Others	24	212	91	672
	2,021	2,303	2,750	3,280

The Target Group expects to contribute US$330,000, US$338,000, US$330,000 and US$450,000 to the CMI UAW Pension Plan for the years ended 31 December 2014, 2015 and 2016 and six months ended 30 June 2017, respectively.

Since the CMI Life & Health Plan is unfunded, there are no plan assets for the disclosure for the CMI Life & Health Plan for the years ended 31 December 2014, 2015 and 2016 and six months ended 30 June 2017.

The average durations of the CMI UAW Pension Plan as at 31 December 2014, 2015 and 2016 and 30 June 2017 are 18, 16, 15 and 15 years, respectively. The average durations of the CMI Life & Health Plan as at 31 December 2014, 2015 and 2016 and 30 June 2017 are 13, 12, 11 and 10 years, respectively.

24. SHARE CAPITAL

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Issued and fully paid:				
2 ordinary shares	20,000	20,000	20,000	20,000

25. RESERVES

(a) Reserves

The amounts of the Target Group's reserves and movements therein for the Relevant Periods are presented in the consolidated statements of changes in equity in the Historical Financial Information.

(b) Reserve fund

Pursuant to the articles of association of a subsidiary operating as a foreign-owned enterprise in Mainland China and the relevant PRC Company Law, the subsidiary shall make an allocation from its profit after tax at the rate of 10% to the statutory surplus reserve fund, until such reserve reaches 50% of the registered capital of the subsidiary. Part of the statutory surplus reserve fund may be capitalised as the subsidiary's registered capital, provided that the remaining balance after the capitalisation is not less than 25% of the registered capital of the subsidiary. The statutory reserve will be reclassified to the retained profits upon disposal of the subsidiary.

26. BUSINESS COMBINATIONS

During the year ended 31 December 2015, CMS entered into a sale and purchase agreement each with United Turbine Corp. ("UT") and with Danbury AeroSpace, Inc. ("Danbury") to acquire UT's and Danbury's businesses for a total consideration of US$9,079,000 and US$14,991,000, respectively. The Target Group acquired the businesses of UT and Danbury to enlarge the range of repair and maintenance services for aircraft engines and the range of products that can be offered to its customers, respectively.

The fair values of identifiable assets and liabilities acquired from UT and Danbury during the year ended 31 December 2015 were:

	Notes	**Fair value recognised on acquisition of UT on 30 January 2015**	**Fair value recognised on acquisition of Danbury on 19 July 2015**	**Total fair values**
		US$'000	*US$'000*	*US$'000*
Cash and bank balances		—	1	1
Trade receivables		1,862	1,996	3,858
Inventories		1,801	6,351	8,152
Property, plant and equipment	10	3,184	2,742	5,926
Intangible assets	12	1,660	2,990	4,650
Trade and other payables		(483)	(1,115)	(1,598)
Total identifiable net assets at fair value		8,024	12,965	20,989
Goodwill on acquisition	11	1,055	2,026	3,081
Satisfied by cash		9,079	14,991	24,070

An analysis of the cash flows in respect of the acquisition of the businesses of UT and Danbury is as follows:

	Acquisition of UT	**Acquisition of Danbury**	**Total**
	US$'000	*US$'000*	*US$'000*
Cash consideration paid	(9,079)	(14,991)	(24,070)
Cash and bank balances acquired	—	1	1
Net outflow of cash and cash equivalents included in cash flows from investing activities	(9,079)	(14,990)	(24,069)

During the year ended 31 December 2015, the businesses of UT and Danbury contributed post-acquisition revenue of US$7,561,000 and US$6,295,000 and post-acquisition loss of US$396,000 and US$713,000, respectively, to the Target Group.

Had the combination taken place at the beginning of 2015, the revenue of the Target Group and the profit of the Target Group for that year would have been US$189,771,000 and US$11,303,000, respectively.

During the year ended 31 December 2014, CMS entered into a sale and purchase agreement with SAC to acquire its business for a total consideration of US$850,000. As of 20 November 2014, the acquisition date, the fair value of the acquired net identifiable assets of SAC was assessed to be US$764,000 and goodwill of US$86,000 was recorded by the Target Group as a result of such acquisition.

The fair values of identifiable assets and liabilities acquired from SAC during the year ended 31 December 2014 were:

	Notes	**Fair value recognised on acquisition**
		US$'000
Trade receivables		181
Inventories		276
Property, plant and equipment	10	386
Investment in a joint venture		33
Trade and other payables		(112)
Total identifiable net assets at fair value		764
Goodwill on acquisition	11	86
		850
Satisfied by cash		723
Other payable		127
		850

An analysis of the cash flows in respect of the acquisition of SAC is as follows:

	US$'000
Cash consideration paid and net outflow of cash and cash equivalents included in cash flows from investing activities	(723)

During the year ended 31 December 2014, SAC contributed US$110,000 to the Target Group's revenue and recorded a loss of US$22,000 between the date of acquisition and the end of that year, respectively.

Had the combination taken place at the beginning of 2014, the revenue of the Target Group and the loss of the Target Group for that year would have been US$163,825,000 and US$7,657,000, respectively.

27. FINANCE LEASE PAYABLES

The Target Group leases certain of its machinery. These leases are classified as finance leases and have remaining lease terms ranging from 1 to 5 years.

At the end of each of the Relevant Periods, the total future minimum lease payments under finance leases and their present values were as follows:

	Minimum lease payments				Present value of minimum lease payments			
	As at 31 December			As at 30 June	As at 31 December			As at 30 June
	2014	2015	2016	2017	2014	2015	2016	2017
	US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*	*US$'000*
Amounts payable:								
Within one year	370	370	—	—	346	359	—	—
In the second year	370	123	—	—	346	112	—	—
In the third to fifth years, inclusive	155	—	—	—	125	—	—	—
Total minimum finance lease payments	895	493	—	—	817	471	—	—
Future finance charges	(78)	(22)	—	—				
Total net finance lease payables	817	471	—	—				
Portion classified as current liabilities (note 20)	(346)	(359)	—	—				
Non-current portion (note 20)	471	112	—	—				

28. NOTE TO CONSOLIDATED STATEMENTS OF CASH FLOWS

Reconciliation of movements of financing activities are as follows:

	Restricted bank balance *US$'000*	Interest-bearing loans and borrowings *US$'000*	Due to a fellow subsidiary *US$'000*
At 1 January 2014	9,154	265,807	—
Cash inflows/(outflows)	—	(324)	3,991
Non-cash changes — foreign exchange movement	(1,071)	(7,569)	—
At 31 December 2014 and 1 January 2015	8,083	257,914	3,991
Cash inflows/(outflows)	(8,083)	10,187	20,409
Non-cash changes — foreign exchange movement	—	(5,775)	—
At 31 December 2015 and 1 January 2016	—	262,326	24,400
Cash inflows/(outflows)	—	(16,071)	13,800
Non-cash changes — foreign exchange movement	—	(1,831)	—
At 31 December 2016 and 1 January 2017	—	244,424	38,200
Cash inflows/(outflows)	—	(10,800)	10,000
Non-cash changes — foreign exchange movement	—	4,104	—
At 30 June 2017	—	237,728	48,200

29. OPERATING LEASE COMMITMENTS

The Target Group leases certain of its offices, factories and cars under operating lease arrangements. Leases for the offices, factories and cars are negotiated for terms ranging from two to twenty-five years.

At the end of each of the Relevant Periods, the Target Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Within one year	296	1,746	843	722
In the second to fifth years, inclusive	715	1,984	1,230	1,390
After five years	583	3,325	3,032	2,885
	1,594	7,055	5,105	4,997

30. RELATED PARTY TRANSACTIONS

(a) In addition to the transactions detailed elsewhere in the Historical Financial Information, the Target Group had the following transactions with related parties during the Relevant Periods:

	Notes	Year ended 31 December			Six months ended 30 June	
		2014	**2015**	**2016**	**2016**	**2017**
		US$'000	*US$'000*	*US$'000*	*US$'000*	*US$'000*
					(Unaudited)	
The immediate holding company:						
Consultation fee	(i)	278	—	—	—	—
Loan guarantee fee	(ii)	744	502	630	393	273
Fellow subsidiaries:						
Sales	(iii)	21,215	19,058	19,952	10,801	8,402
Service fee paid	(iv)	14	—	—	—	—
Interest expense	(v)	38	171	1,109	299	601

(i) The consultation fee to the immediate holding company was made for the provision of corporate services at rates agreed between the respective parties.

(ii) The loan guarantee fee to the immediate holding company was determined on bases agreed between the respective parties.

(iii) The sales to fellow subsidiaries were made according to the published prices and conditions offered to the major customers of the Target Group.

(iv) The service fee to a fellow subsidiary was charged at rates agreed between the respective parties.

(v) The interest expense paid to a fellow subsidiary was charged on an amount due to a fellow subsidiary at interest rates from 2.8% to 5.9% per annum for the Relevant Periods.

(b) **Other transactions with a related party:**

The Target Group's immediate holding company has guaranteed bank loans made to the Target Group of up to the carrying amount of the bank loan at the end of each of the Relevant Periods, as further detailed in note 20 to the Historical Financial Information.

(c) **Outstanding balances with related parties:**

Details of balances with group companies are disclosed in note 17 to the Historical Financial Information.

(d) **Compensation of key management personnel of the Target Company:**

Key management personnel of the Target Group comprises the directors of the Target Company. Details of the directors' remuneration of the Target Company are included in note 8 to the Historical Financial Information.

31. FINANCIAL INSTRUMENTS BY CATEGORY

The carrying amounts of each of the categories of financial instruments as at the end of each of the Relevant Periods are as follows:

Financial assets

	Loans and receivables			
	As at 31 December			**As at 30 June**
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Trade and other receivables	12,012	24,700	16,582	17,060
Due from fellow subsidiaries	5,968	3,254	3,734	2,344
Restricted bank balance	8,083	—	—	—
Cash and cash equivalents	13,191	9,419	14,105	8,460
	39,254	37,373	34,421	27,864

Financial liabilities

	Financial liabilities at amortised cost			
	As at 31 December			As at 30 June
	2014	2015	2016	2017
	US$'000	*US$'000*	*US$'000*	*US$'000*
Financial liabilities included in trade payables, other payables and accruals	16,333	21,754	18,062	15,748
Interest-bearing loans and borrowings	257,914	262,326	244,424	237,728
Due to the immediate holding company	2,044	2,590	3,059	3,410
Due to fellow subsidiaries	3,991	23,895	38,670	49,298
	280,282	310,565	304,215	306,184

32. FAIR VALUES OF FINANCIAL INSTRUMENTS

Management has assessed that the fair values of cash and bank balances, trade and other receivables, balances with group companies, financial liabilities included in trade payables, other payables and accruals and interest-bearing loans and borrowings approximate to their carrying amounts largely due to the short term maturities of these instruments.

The fair values of the non-current portion of interest-bearing loans and borrowings and the amount due to the immediate holding company have been calculated by discounting the expected future cash flows using rates currently available for instruments with similar terms, credit risk and remaining maturities. Their carrying amounts reasonably approximate to fair values.

33. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Target Group's principal financial instruments comprise cash and bank balances, trade and other receivables, balances with group companies, financial liabilities included in trade payables, other payables and accruals and interest-bearing loans and borrowings. The main purpose of these financial instruments is to provide finance for the Target Group's operations.

The main risks arising from the Target Group's financial instruments are interest rate risk, credit risk and liquidity risk. These risks are managed by the Target Group's financial management policies and practices described below.

Interest rate risk

The Target Group's exposure to interest rate risk relates principally to the Target Group's interest-bearing loans and borrowings from financial institutions (note 20). The Target Group mitigates the risk by monitoring closely the movements in interest rates and reviewing its banking facilities regularly.

The sensitivity analysis below has been determined based on the exposure to interest rates for variable-rate bank borrowings at the end of each of the Relevant Periods. The analysis is prepared assuming the amount of liability outstanding at the end of each of the Relevant Periods was outstanding for the whole year. A 100 basis point increase or decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the reasonably possible change in interest rates.

	Increase/ (decrease) in basis points	**Increase/ (decrease) in profit before tax**	**Increase/ (decrease) in equity***
		US$'000	*US$'000*
As at 31 December 2014			
LIBOR	100	(2,000)	—
LIBOR	(100)	2,000	—
EURIBOR	100	(571)	—
EURIBOR	(100)	571	—
As at 31 December 2015			
LIBOR	100	(2,105)	—
LIBOR	(100)	2,105	—
EURIBOR	100	(513)	—
EURIBOR	(100)	513	—
As at 31 December 2016			
LIBOR	100	(1,949)	—
LIBOR	(100)	1,949	—
EURIBOR	100	(495)	—
EURIBOR	(100)	495	—
As at 30 June 2017			
LIBOR	100	(1,841)	—
LIBOR	(100)	1,841	—
EURIBOR	100	(536)	—
EURIBOR	(100)	536	—

* *Excluding retained profits*

Sensitivity analysis on bank deposits is not presented as the directors of the Target Company consider that the Target Group's exposure to interest rate fluctuations on bank deposits is insignificant.

Credit risk

The Target Group trades only with recognised and creditworthy third parties. In addition, receivable balances are monitored on an ongoing basis and the Target Group's exposure to bad debts is not significant.

With respect to credit risk arising from the other financial assets of the Target Group, which comprise trade and other receivables, amounts due from group companies and cash and bank balances, the Target Group's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

Since the Target Group trades only with recognised and creditworthy third parties, there is no requirement for collateral. Concentrations of credit risk are managed by customer. As at 31 December 2014, 31 December 2015, 31 December 2016 and 30 June 2017, the Target Group had certain concentrations of credit risk as 11%, 6%, 39% and 39%, respectively, of the Target Group's trade receivables were due from one of the Target Group's key customers.

Liquidity risk

The Target Group monitors its risk to a shortage of funds using a recurring liquidity planning tool. This tool considers the maturity of both its financial instruments and financial assets and projected cash flows from operations.

The Target Group's objective is to maintain a balance between continuity of funding and flexibility through the funding from group companies and bank borrowings.

The maturity profile of the Target Group's financial liabilities as at the end of each of the Relevant Periods, based on the contractual undiscounted payments, was as follows:

	Less than 3 months or on demand	Less than 12 months	Over 1 year	Total
	US$'000	*US$'000*	*US$'000*	*US$'000*
31 December 2014				
Financial liabilities included in trade payables, other payables and accruals	16,333	—	—	16,333
Interest-bearing loans and bank borrowings	89	269	265,539	265,897
Due to the immediate holding company	1,176	—	868	2,044
Due to a fellow subsidiary	3,991	—	—	3,991
	21,589	269	266,407	288,265
31 December 2015				
Financial liabilities included in trade payables, other payables and accruals	21,754	—	—	21,754
Interest-bearing loans and bank borrowings	4,092	1,915	264,267	270,274
Due to the immediate holding company	437	—	2,153	2,590
Due to a fellow subsidiary	23,895	—	—	23,895
	50,178	1,915	266,420	318,513
31 December 2016				
Financial liabilities included in trade payables, other payables and accruals	18,062	—	—	18,062
Interest-bearing loans and bank borrowings	—	22,479	230,791	253,270
Due to the immediate holding company	741	—	2,318	3,059
Due to fellow subsidiaries	38,670	—	—	38,670
	57,473	22,479	233,109	313,061
30 June 2017				
Financial liabilities included in trade payables, other payables and accruals	15,748	—	—	15,748
Interest-bearing loans and bank borrowings	—	22,524	224,099	246,623
Due to the immediate holding company	1,216	—	2,194	3,410
Due to fellow subsidiaries	49,298	—	—	49,298
	66,262	22,524	226,293	315,079

Capital management

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

The Target Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions and the risk characteristics of the underlying assets. The Target Group is not subject to any externally imposed capital requirements. No changes were made in the objectives, policies or processes for managing capital during the Relevant Periods.

The Target Group monitors capital using a gearing ratio, which is debts divided by total equity/(deficiency in assets) plus debts. Debts include loans and borrowings and an amount due to a fellow subsidiary. The gearing ratios as at the end of each of the Relevant Periods were as follows:

	As at 31 December			As at 30 June
	2014	**2015**	**2016**	**2017**
	US$'000	*US$'000*	*US$'000*	*US$'000*
Due to fellow subsidiaries	3,991	23,895	38,670	49,298
Interest-bearing loans and borrowings	257,914	262,326	244,424	237,728
Debts	261,905	286,221	283,094	287,026
Total equity/(deficiency in assets)	(7,942)	4,742	10,836	13,067
Total equity/(deficiency in assets) plus interest-bearing debts	253,963	290,963	293,930	300,093
Gearing ratio	103%	98%	96%	96%

34. COMPANY — BALANCES WITH GROUP COMPANIES

(a) Investment in a subsidiary

Investment in a subsidiary represents an investment in Continental Motors Group Limited.

(b) Balances with group companies

The balances with group companies are unsecured, interest-free and repayable on demand.

35. SUBSEQUENT FINANCIAL STATEMENTS

No audited financial statements have been prepared by the Target Group in respect of any period subsequent to 30 June 2017.

UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

Introduction

The accompanying unaudited pro forma consolidated statement of financial position, the unaudited pro forma consolidated statement of profit or loss and the unaudited pro forma consolidated statement of cash flows of the Enlarged Group (collectively, the "Unaudited Pro Forma Financial Information") have been prepared by the directors of the Company ("Directors") in accordance with paragraph 29 of Chapter 4 of the Listing Rules for the purpose of illustrating the effects on the historical consolidated financial position and the consolidated results and cash flows of the Enlarged Group upon the completion of the proposed acquisition by the Company of 100% equity interest of Motto Investment Limited (the "Target Company") held by AVIC International (HK) Group Limited ("AVIC HK") and the shareholder's loan note(s) owing by the Target Company to AVIC HK (the "Loan Note(s)") (collectively, the "Acquisition") and upon the completion of the settlement of certain loans owed by the Target Group as conditions precedent to the completion of the Acquisition (the "Preceding Loans Restructuring").

The unaudited pro forma consolidated statement of financial position of the Enlarged Group has been prepared based on the unaudited consolidated statement of financial position of the Group as at 30 June 2017, which has been extracted from the Group's published interim report for the six months ended 30 June 2017; and the audited consolidated statement of financial position of the Target Group as at 30 June 2017 which has been extracted from the accountants' report of the Target Company set out in Appendix III to this Circular; and after taking into account the pro forma adjustments relating to the Acquisition and the Preceding Loans Restructuring as described in the notes thereto, that are (i) clearly shown and explained; (ii) directly attributable to the Acquisition and the Preceding Loans Restructuring and not relating to future events or decisions; and (iii) factually supportable, as explained in the accompanying notes, as if the Acquisition and the Preceding Loans Restructuring had been effected on 30 June 2017.

The unaudited pro forma consolidated statement of profit or loss and the unaudited pro forma consolidated statement of cash flows of the Enlarged Group have been prepared based on the audited consolidated statement of profit or loss and the audited consolidated statement of cash flows of the Group for the year ended 31 December 2016, which have been extracted from the Group's published annual report for the year ended 31 December 2016; and the audited consolidated profit or loss and the audited consolidated statement of cash flows of the Target Group for the year ended 31 December 2016, which have been extracted from the accountants' report of the Target Company set out in Appendix III to this Circular; and after taking into account the pro forma adjustments relating to the Acquisition and the Preceding Loans Restructuring as described in the notes thereto; that are (i) clearly shown and explained; (ii) directly attributable to the Acquisition and the Preceding Loans Restructuring and not relating to future events or decisions; and (iii) factually supportable, as explained in the accompanying notes, as if the Acquisition and the Preceding Loans Restructuring had been effected on 1 January 2016.

The accompanying Unaudited Pro Forma Financial Information of the Enlarged Group is prepared by the Directors based on a number of assumptions, estimates, uncertainties and currently available information to provide information of the Enlarged Group upon completion of the Acquisition and the Preceding Loans Restructuring. As the Unaudited Pro Forma Financial Information of the Enlarged Group is prepared for illustrative purpose only, and because of its hypothetical nature, it may not give a true picture of the financial position and results of the Enlarged Group following the completion of the Acquisition and the Preceding Loans Restructuring and does not purport to describe the actual financial position, results of operations and cash flows of the Enlarged Group that would have been attained had the Acquisition and the Preceding Loans Restructuring been effected on the dates indicated herein. Further, the accompanying Unaudited Pro Forma Financial Information of the Enlarged Group does not purport to predict the future financial position, results of operations or cash flows of the Enlarged Group after the completion of the Acquisition and the Preceding Loans Restructuring.

The Unaudited Pro Forma Financial Information of the Enlarged Group has been prepared in accordance with paragraph 29 of Chapter 4 and paragraph 69(4)(a)(ii) of Chapter 14 of the Listing Rules. The Unaudited Pro Forma Financial Information of the Enlarged Group should be read in conjunction with the financial information of the Group as set out in Appendix II to the Circular, the accountants' report of the Target Company as set out in Appendix III to this Circular and other financial information included elsewhere in the Circular.

Unaudited Pro Forma Consolidated Statement of Financial Position of the Enlarged Group

	The Group as at 30 June 2017	The Target Group as at 30 June 2017	Subtotal	Pro forma adjustments		Enlarged Group
	(unaudited)	*(audited)*				
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*		*HK$'000*
	(Note 1)	*(Note 2)*			*Notes*	
NON-CURRENT ASSETS						
Property, plant and equipment	23,425	246,365	269,790	90,008	5(a)	359,798
Investment properties	325,391	—	325,391			325,391
Goodwill	—	848,261	848,261			848,261
Other intangible assets	—	922,529	922,529	727,345	5(a)	1,649,874
Investment in joint ventures	50,137	659	50,796			50,796
Investment in associates	12,265	—	12,265			12,265
Available-for-sale investments	192,897	—	192,897			192,897
Derivative financial instruments	68	—	68			68
Deferred tax assets	10,327	—	10,327			10,327
Prepayment	—	968	968			968
Total non-current assets	**614,510**	**2,018,782**	**2,633,292**			**3,450,645**
CURRENT ASSETS						
Properties under development and completed properties held for sale	4,326,947	—	4,326,947			4,326,947
Inventories	—	462,195	462,195	77,616	5(a)	539,811
Trade receivables	88,307	116,157	204,464			204,464
Due from fellow subsidiaries	2,646	18,166	20,812			20,812
Loans to associates	9,783	—	9,783			9,783
Loans to a related company	17,265	—	17,265			17,265
Prepayments, deposits and other receivables	45,575	35,867	81,442			81,442
Available-for-sale investments	48,636	—	48,636			48,636
Derivative financial instruments	184	—	184			184
Equity investment at fair value through profit or loss	61,714	—	61,714			61,714
Prepaid taxes	23,078	—	23,078			23,078
Cash and cash equivalents	670,377	65,565	735,942	(225,412)	4(a), 8	510,530
Total current assets	**5,294,512**	**697,950**	**5,992,462**			**5,844,666**

	The Group as at 30 June 2017	The Target Group as at 30 June 2017	Subtotal	Pro forma adjustments		Enlarged Group
	(unaudited)	*(audited)*				
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*		*HK$'000*
	(Note 1)	*(Note 2)*			*Notes*	
CURRENT LIABILITIES						
Due to non-controlling shareholders of subsidiaries	(117,783)	—	(117,783)			(117,783)
Due to intermediate holding companies	(7,535)	—	(7,535)	(809,424)	4(b), 9	(816,959)
Due to fellow subsidiaries	(2,969)	(8,510)	(11,479)			(11,479)
Due to the immediate holding company	—	(9,424)	(9,424)	9,424	9	—
Loans from fellow subsidiaries	(621,547)	(373,550)	(995,097)	373,550	3(b)	(621,547)
Interest-bearing bank borrowings	—	(167,400)	(167,400)	155,000	3(a)	(12,400)
Trade payables	(35,178)	(69,657)	(104,835)			(104,835)
Other payables, accruals, provisions and other liabilities	(22,217)	(116,707)	(138,924)			(138,924)
Customer deposits	(1,367,722)	—	(1,367,722)			(1,367,722)
Tax payables	(36,954)	(605)	(37,559)			(37,559)
Total current liabilities	**(2,211,905)**	**(745,853)**	**(2,957,758)**			**(3,229,208)**
NET CURRENT ASSETS/ (LIABILTIES)	3,082,607	(47,903)	3,034,704			2,615,458
TOTAL ASSETS LESS CURRENT LIABILITIES	**3,697,117**	**1,970,879**	**5,667,996**			**6,066,103**
NON-CURRENT LIABILITIES						
Loans from an intermediate holding company	(489,756)	—	(489,756)			(489,756)
Loans from a fellow subsidiary	(540,976)	—	(540,976)			(540,976)
Due to an intermediate holding company	—	—	—	(17,004)	9	(17,004)
Due to the immediate holding company	—	(17,004)	(17,004)	17,004	9	—
Interest-bearing bank borrowings	—	(1,674,992)	(1,674,992)	1,655,363	3(a)	(19,629)
Other payables, provisions and other liabilities	—	(135,105)	(135,105)			(135,105)
Defined benefit obligations	—	(4,325)	(4,325)			(4,325)
Deferred tax liabilities	(134,328)	(38,184)	(172,512)	(313,990)	5	(486,502)

	The Group as at 30 June 2017	The Target Group as at 30 June 2017	Subtotal	Pro forma adjustments		Enlarged Group
	(unaudited)	*(audited)*				
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*		*HK$'000*
	(Note 1)	*(Note 2)*			*Notes*	
Total non-current liabilities	**(1,165,060)**	**(1,869,610)**	**(3,034,670)**			**(1,693,297)**
Net assets	**2,532,057**	**101,269**	**2,633,326**			**4,372,806**
EQUITY						
Equity attributable to owners of the Company						
Share capital	(551,959)	(155,000)	(706,959)	(223,378)	3(b), 4(c), 5	(930,337)
Reserves	(1,416,273)	53,731	(1,362,542)	(1,516,102)	4(c), 5, 8	(2,878,644)
	(1,968,232)	(101,269)	(2,069,501)			(3,808,981)
Non-controlling interests	(563,825)	—	(563,825)			(563,825)
Total equity	**(2,532,057)**	**(101,269)**	**(2,633,326)**			**(4,372,806)**

Unaudited Pro Forma Consolidated Statement of Profit or Loss of the Enlarged Group

	The Group year ended 31 December 2016	The Target Group year ended 31 December 2016	Subtotal	Pro forma adjustments		Enlarged Group
	(audited)	*(audited)*				
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*		*HK$'000*
	(Note 1)	*(Note 2)*			*Notes*	
Revenue	102,786	1,583,441	1,686,227			1,686,227
Cost of sales	(74,269)	(1,076,343)	(1,150,612)	(89,954)	6	(1,240,566)
Gross profit	28,517	507,098	535,615			445,661
Other income	12,765	—	12,765			12,765
Selling and distribution expenses	(31,694)	(85,583)	(117,277)			(117,277)
Administrative expenses	(41,611)	(263,160)	(304,771)	(79,290)	6, 8	(384,061)
Other operating expenses	(54,633)	(922)	(55,555)			(55,555)
Finance costs	(77)	(83,646)	(83,723)	80,011	7	(3,712)
Net gain on deemed disposal of associates	3,386	—	3,386			3,386
Share of profits and losses of:						
Joint ventures	(215,369)	109	(215,260)			(215,260)
Associates	(3,013)	—	(3,013)			(3,013)
Impairment of an available-for- sale investment (transfer from available-for-sale investment revaluation reserve)	(134,107)	—	(134,107)			(134,107)
Fair value loss of available-for-sale investments (transfer from equity on derecognition)	(490)	—	(490)			(490)
Fair value loss on derivative financial Instruments, net	(108,558)	—	(108,558)			(108,558)
Fair value loss on equity investment at fair value through profit or loss	(198,094)	—	(198,094)			(198,094)
Gain on bargain purchase	—	—	—	390,485	5(b)	390,485
Profit/(loss) before tax from continuing operations	(742,978)	73,896	(669,082)			(367,830)
Income tax credit/(expense)	6,685	(32,263)	(25,578)	24,622	6, 7	(956)

	The Group year ended 31 December 2016	The Target Group year ended 31 December 2016	Subtotal	Pro forma adjustments		Enlarged Group
	(audited)	*(audited)*				
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*		*HK$'000*
	(Note 1)	*(Note 2)*			*Notes*	
Profit/(loss) for the year from continuing operations	**(736,293)**	**41,633**	**(694,660)**			**(368,786)**
Discontinued operation						
Profit for the year from a discontinued operation	27,362	—	27,362			27,362
Profit/(loss) for the year	**(708,931)**	**41,633**	**(667,298)**			**(341,424)**
Attributable to:						
Owners of the Company	(685,842)	41,633	(644,209)	325,874	5(b), 6, 7, 8	(318,335)
Non-controlling interests	(23,089)	—	(23,089)			(23,089)
	(708,931)	**41,633**	**(667,298)**			**(341,424)**

Unaudited Pro Forma Consolidated Statement of Cash Flows of the Enlarged Group

	The Group year ended 31 December 2016	The Target Group year ended 31 December 2016	Subtotal	Pro forma adjustments		Enlarged Group
	(audited)	*(audited)*				
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*		*HK$'000*
	(Note 1)	*(Note 2)*			*Notes*	
Cash flows from operating activities						
Profit/(loss) before tax:						
From continuing operations	(742,978)	73,896	(669,082)	301,252	5(b), 6, 7, 8	(367,830)
From a discontinued operations	(5,075)	—	(5,075)			(5,075)
Adjustments for:						
Finance costs	1,265	83,646	84,911	(80,011)	7	4,900
Share of profits and losses of joint ventures and associates	218,382	(109)	218,273			218,273
Bank interest income	(2,176)	—	(2,176)			(2,176)
Interest income on a convertible bond	(1,036)	—	(1,036)			(1,036)
Interest income on loans to associates	(577)	—	(577)			(577)
Interest income on loans to related companies	(1,076)	—	(1,076)			(1,076)
Net gain on deemed disposal of associates	(3,386)	—	(3,386)			(3,386)
Depreciation	2,487	46,508	48,995	21,863	6	70,858
Amortisation of intangible assets	95	35,898	35,993	44,353	6	80,346
Recognition of prepaid land lease payments	13	—	13			13
Provision for impairment of a loan to a related company	12,608	—	12,608			12,608
Provision for impairment of prepayments and other receivables	4,345	—	4,345			4,345
Loss/(gain) on disposal of items of property, plant and equipment	(222)	581	359			359
Fair value losses on investment properties	34,047	—	34,047			34,047

	The Group year ended 31 December 2016	The Target Group year ended 31 December 2016	Subtotal	Pro forma adjustments		Enlarged Group
	(audited)	*(audited)*				
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*		*HK$'000*
	(Note 1)	*(Note 2)*			*Notes*	
Impairment of an investment in a joint venture	7,745	—	7,745			7,745
Fair value loss on equity investment at fair value through profit or loss	198,094	—	198,094			198,094
Fair value loss of available-for-sale investments (transfer from equity on derecognition)	490	—	490			490
Impairment of an available-for-sale investment	134,107	—	134,107			134,107
Fair value loss on derivative financial instruments, net	108,558	—	108,558			108,558
Reversal of provision of trade receivables	—	(1,682)	(1,682)			(1,682)
Impairment of items of property, plant and equipment	—	2,372	2,372			2,372
Impairment of goodwill	—	667	667			667
Loss on disposal of items of other intangible assets	—	705	705			705
Reversal of provision for deposits	—	(1,054)	(1,054)			(1,054)
Pension scheme expense under defined benefit schemes	—	3,712	3,712			3,712
Gain on bargain purchase	—	—	—	(390,485)	5(b)	(390,485)
	(34,290)	245,140	210,850			107,822
Increase in properties under development and completed properties held for sale	(172,696)	—	(172,696)			(172,696)
Decrease/(increase) in inventories	502	(43,346)	(42,844)	77,616	6	34,772
Decrease in trade and bills receivables	83,708	66,797	150,505			150,505
Decrease in prepayments, deposits and other receivables	12,108	7,339	19,447			19,447
Decrease in trade and bills payables	(31,988)	(29,442)	(61,430)			(61,430)

	The Group year ended 31 December 2016	The Target Group year ended 31 December 2016	Subtotal	Pro forma adjustments		Enlarged Group
	(audited)	*(audited)*				
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*		*HK$'000*
	(Note 1)	*(Note 2)*			*Notes*	
Increase/(decrease) in other payables, accruals, provisions and other liabilities	6,696	(24,932)	(18,236)			(18,236)
Increase in customer deposits	689,909	—	689,909			689,909
Decrease/(increase) in amounts due from fellow subsidiaries	34,671	(3,720)	30,951			30,951
Increase in amounts due to fellow subsidiaries	—	7,556	7,556			7,556
Increase in amounts due to an intermediate holding company	—	—	—	3,619	9	3,619
Decrease in an amount due from a non- controlling shareholder of a subsidiary	323	—	323			323
Increase in an amount due to the immediate holding company	—	3,619	3,619	(3,619)	9	—
Benefits paid from defined benefit schemes	—	(457)	(457)			(457)
Contribution to defined benefit schemes	—	(2,612)	(2,612)			(2,612)
	588,943	225,942	814,885			789,473
Overseas tax paid	(41,544)	(2,604)	(44,148)			(44,148)
Net cash flows from operating activities	547,399	223,338	770,737			745,325
Cash flows from investing activities						
Purchases of items of property, plant and equipment	(96)	(31,287)	(31,383)			(31,383)
Additions to other intangible assets	—	(68,223)	(68,223)			(68,223)
Proceeds from disposal of items of property, plant and equipment	746	14,609	15,355			15,355

	The Group year ended 31 December 2016	The Target Group year ended 31 December 2016	Subtotal	Pro forma adjustments		Enlarged Group
	(audited)	*(audited)*				
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*		*HK$'000*
	(Note 1)	*(Note 2)*			*Notes*	
Proceeds from disposal of available-for-sale investments	1,800	—	1,800			1,800
Repayment of loans to a related company	22	—	22			22
Disposal of a subsidiary	3,716	—	3,716			3,716
Bank interest received	2,072	—	2,072			2,072
Interest received on a convertible bond	1,036	—	1,036			1,036
Interest received on loans to associates	427	—	427			427
Interest received on loans to related companies	790	—	790			790
Increase in pledged time deposits	(2,815)	—	(2,815)			(2,815)
Acquisition of subsidiaries	—	—	—	(200,000)	4	(200,000)
Net cash flows from/(used in) investing activities	7,698	(84,901)	(77,203)			(277,203)
Cash flows from financing activities						
New bank loans	230,134	15,500	245,634			245,634
Repayment of bank loans	—	(136,400)	(136,400)			(136,400)
Repayment of loans from fellow subsidiaries	(495,008)	—	(495,008)	(373,550)	3(b)	(868,558)
Capital injection received from AVIC International Holding Corporation	—	—	—	373,550	3(b)	373,550
Loan from a fellow subsidiary	—	106,950	106,950			106,950
Increase in amounts due to non-controlling shareholders of subsidiaries	28,817	—	28,817			28,817
Decrease in an amount due to an intermediate holding company	(15,189)	—	(15,189)			(15,189)
Increase in an amounts due to fellow subsidiaries	713	—	713			713

	The Group year ended 31 December 2016	The Target Group year ended 31 December 2016	Subtotal	Pro forma adjustments		Enlarged Group
	(audited)	*(audited)*				
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*		*HK$'000*
	(Note 1)	*(Note 2)*			*Notes*	
Capital element of finance lease rental payments	—	(3,650)	(3,650)			(3,650)
Interest paid	(162,359)	(83,646)	(246,005)	80,011	7	(165,994)
Net cash flows used in financing activities	(412,892)	(101,246)	(514,138)			(434,127)
Net increase/(decrease) in cash and cash equivalents	142,205	37,191	179,396			33,995
Cash and cash equivalents at beginning of year	473,330	72,997	546,327			546,327
Effect of foreign exchange rate changes, net	(9,610)	(874)	(10,484)			(10,484)
Cash and cash equivalents at end of year	**605,925**	**109,314**	**715,239**			**569,838**
Analysis of balances of cash and cash equivalents						
Cash and bank balances	307,215	109,314	416,529	(145,401)	4(a), 7, 8	271,128
Non-pledged time deposit with original maturity of less than three months when acquired	298,710	—	298,710			298,710
Cash and cash equivalents at end of year	**605,925**	**109,314**	**715,239**			**569,838**

Notes:

1. The unaudited consolidated statement of financial position as at 30 June 2017 was extracted from the published interim report of the Group for the six months ended 30 June 2017. The audited consolidated statement of profit or loss and audited consolidated statement of cash flows for the year ended 31 December 2016 of the Group were extracted from the published annual report of the Group for the year ended 31 December 2016.

2. The audited consolidated statement of financial position of the Target Group as at 30 June 2017 and the audited consolidated profit or loss and audited consolidated statement of cash flows for the year ended 31 December 2016 of the Target Group were derived from the accountants' report as set out in Appendix III to this Circular which were converted from US$ to HK$ at the rate of US$1.00 to HK$7.75.

3. Pursuant to the terms of the acquisition agreement, as conditions precedent to the completion of the Acquisition, certain loans of the Target Group shall be settled under the following Preceding Loans Restructuring arrangement:

(a) Bank loans of US$180,000,000 and EUR46,975,000 (equivalent to HK$1,810,363,000 in aggregate) borrowed by the subsidiaries of the Target Company shall be purchased by AVIC HK which shall subsequently sell these two loans to the Target Company in return for the issuance by the Target Company of interest free, unsecured and repayable on demand loan note(s) in the same aggregate principal amount as the two loans (the "Loan Note(s)"). Such Loan Note(s) together with the entire issued share capital of the Target Company will be sold to the Company.

(b) The Target Group shall repay the loan due to a fellow subsidiary of the Group amounting to US$48,200,000 (equivalent to HK$373,550,000) using the funds from additional equity investment by AVIC International Holding Corporation ("AVIC International"), the immediate holding company of the Target Company before the completion of the Acquisition. For the purpose of the Unaudited Pro Forma Financial Information, the additional equity investment will be in the same amount as the loan.

4. The total purchase consideration of the Acquisition shall be satisfied by the Company by the issue and allotment of 3,783,783,783 consideration shares and cash consideration of HK$1,000,000,000 payable in two instalments as set out in (a) and (b) below and is calculated as follows:

	HK$'000
Cash consideration (a), (b)	1,000,000
Consideration shares (c)	1,475,676
Total consideration	2,475,676

In exchange for:

	HK$'000
Acquisition of 100% equity interest of the Target Company	665,313
Acquisition of the Loan Note(s) owing by the Target Company to AVIC HK (Note 3(a))	1,810,363
	2,475,676

(a) Initial cash consideration of HK$200,000,000 to be settled upon completion.

(b) Deferred consideration of HK$800,000,000 to be settled upon the earlier occurrence of the following events:

(i) the Company having received the proceeds from the disposal of its real estate business resulting in the Company having net cash balance of more than HK$800,000,000; and

(ii) the Company having net cash balance of more than HK$800,000,000.

(c) For the purpose of the Unaudited Pro Forma Financial Information, the closing price of the share of the Company at HK$0.39 each as at 30 June 2017 was adopted for the calculation of the fair value of the consideration shares, as if the Acquisition had been effected on 30 June 2017. The actual fair value of the consideration shares will be determined upon completion of the actual Acquisition, which consequently may result in a financial effect which is materially different from the above.

5. The identifiable assets and liabilities of the Target Group acquired by the Group will be accounted for in the consolidated financial statements of the Enlarged Group at fair value under acquisition accounting in accordance with Hong Kong Financial Reporting Standard 3 *Business Combinations* ("HKFRS 3") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA").

For the purpose of the Unaudited Pro Forma Financial Information, the allocation of the purchase price is determined based on an independent professional valuer's estimates of the fair values of the identified assets and liabilities of the Target Group as at 30 June 2017 as follows.

	HK$'000	*HK$'000*	*HK$'000*
Consideration so determined per note 4 above			2,475,676
Less: Net assets acquired:			
Carrying amount of the net assets of the Target Group as at 30 June 2017	(101,269)		
Additional equity investment in the Target Group (Note 3(b))	(373,550)	(474,819)	
Fair value adjustments (a)		(894,969)	
Loan Note(s) owing by the Target Company to AVIC HK (Note 3(a))		(1,810,363)	
Add: Deferred tax liabilities related to the fair value adjustments		313,990	(2,866,161)
Gain on bargain purchase (b)			(390,485)

(a) The estimated fair values of the identifiable assets and liabilities of the Target Group were based on the independent valuation conducted by Duff & Phelps, LLC, an independent professional valuer, as at 30 June 2017. The details of the fair value adjustments are as follows:

Identifiable assets subject to fair value adjustments:

	Fair values	**Carrying amounts**	**Fair value adjustments**
	HK$'000	*HK$'000*	*HK$'000*
Property, plant and equipment	336,373	246,365	90,008
Inventories	539,811	462,195	77,616
Other intangible assets including backlog, trademarks, product technology, licence and completed programs and customer relationships	1,649,874	922,529	727,345
Total	2,526,058	1,631,089	894,969

(b) Actual goodwill or gain on bargain purchase arising from the Acquisition will be determined based on fair values of the identifiable assets and liabilities of the Target Group and the aggregate fair value of the total consideration at the actual completion date. When the actual transactions take place, different fair values may be determined which consequently may result in a financial effect which is materially different from the above.

Since the fair value of the consideration shares and the fair value of the underlying assets and liabilities of the Target Group as at the completion date may be different from the above, the resulting amount of goodwill or gain on bargain purchase at the date of Acquisition may be different. If the fair value of the underlying assets and liabilities of the Target Group is higher than the fair value of the total consideration transferred as at the completion date, a gain on bargain purchase will be resulted. If the fair value of the underlying assets and liabilities of the Target Group is lower than the fair value of the total consideration transferred as at the completion date, goodwill will be resulted.

6. The adjustments represent the additional cost of sales, depreciation and amortisation together with the corresponding deferred income tax impact for the year ended 31 December 2016 arising from the fair value adjustments per Note 5(a) above as if the Acquisition had been effected on 1 January 2016.

7. The adjustment represents savings in finance costs incurred for the loans in Note 3 above and the corresponding income tax impact for the year ended 31 December 2016, as if the Acquisition and the Preceding Loans Restructuring had been effected on 1 January 2016.

8. The adjustment represents estimated direct expenses of audit, legal, valuation and other professional services of approximately HK$25,412,000 related to the Acquisition and the Preceding Loans Restructuring. For the purpose of preparation of the Unaudited Pro Forma Financial Information of the Enlarged Group, these expenses are charged to the Enlarged Group's consolidated statement of profit or loss. The adjustment is not expected to have a continuing effect on the Enlarged Group.

9. The adjustments represent the reclassification of balances with AVIC International as balances with the immediate holding company recorded by the Target Group to balances with an intermediate holding company of the Enlarged Group.

10. For the purpose of the above Unaudited Pro Forma Financial Information, foreign currency amounts in US$ and EUR have been translated into HK$ at the exchange rate of US$1.00 to HK$7.75 and EUR1.00 to HK$8.84, respectively.

11. Apart from the effects of the Acquisition and the Preceding Loans Restructuring, no other adjustments have been made to the Unaudited Pro Forma Financial Information of the Enlarged Group to reflect any trading results or other transactions entered into by the Group or the Target Group subsequent to 30 June 2017 for their consolidated statements of financial position as at 30 June 2017, and subsequent to 31 December 2016 for their consolidated statements of profit or loss and consolidated statements of cash flows for the year ended 31 December 2016 as if the Acquisition and the Preceding Loans Restructuring had taken place at 30 June 2017 and 1 January 2016, respectively.

The following is the text of a report from the reporting accountants, Ernst & Young, Certified Public Accountants, Hong Kong, prepared for the purpose of incorporation in this circular in respect of the unaudited pro forma financial information of the Enlarged Group.

INDEPENDENT REPORTING ACCOUNTANTS' ASSURANCE REPORT ON THE COMPILATION OF UNAUDITED PRO FORMA FINANCIAL INFORMATION

EY 安永

To the Directors of AVIC International Holding (HK) Limited

We have completed our assurance engagement to report on the compilation of the unaudited pro forma financial information of AVIC International Holding (HK) Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group") by the directors of the Company (the "Directors") for illustrative purposes only. The unaudited pro forma financial information consists of the unaudited pro forma consolidated statement of financial position as at 30 June 2017, and unaudited pro forma consolidated statement of profit or loss and unaudited consolidated statement of cash flows for the year ended 31 December 2016, and related notes as set out in Appendix IV of the circular dated 29 December 2017 issued by the Company (the "Circular") (the "Unaudited Pro Forma Financial Information"). The applicable criteria on the basis of which the Directors have compiled the Unaudited Pro Forma Financial Information are described in Appendix IV of the Circular.

The Unaudited Pro Forma Financial Information has been compiled by the Directors to illustrate the impact of the proposed acquisition of 100% equity interest of Motto Investment Limited (the "Target Company") and its subsidiaries (collectively, the "Target Group") and the shareholder's loan note(s) owing by the Target Company to AVIC HK (the "Loan Note(s)") (collectively, the "Acquisition") and of the completion of the settlement of certain loans owed by the Target Group as conditions precedent to the completion of the Acquisition (the "Preceding Loans Restructuring") on the Group's financial position as at 30 June 2017 and the Group's financial performance and cash flows for the year ended 31 December 2016 as if the Acquisition and the Preceding Loans Restructuring had taken place at 30 June 2017 and 1 January 2016, respectively. As part of this process, information about the Group's financial position, financial performance and cash flows has been extracted by the Directors from the Group's audited financial statements for the year ended 31 December 2016 as set out in the published annual report of the Company dated 14 March 2017 and the Group's unaudited interim financial information for the six months ended 30 June 2017 as set out in the published interim report of the Company dated 25 August 2017. Information about the Target Group's financial position, financial performance and cash flows has been extracted by the Directors from the audited financial information of the Target Group as set out in its accountants' report included in Appendix III to the Circular.

Directors' responsibility for the Unaudited Pro Forma Financial Information

The Directors are responsible for compiling the Unaudited Pro Forma Financial Information in accordance with paragraph 4.29 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 ("AG") 7 *Preparation of Pro Forma Financial Information for Inclusion in Investment Circulars* issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA").

Our independence and quality control

We have complied with the independence and other ethical requirements of the *Code of Ethics for Professional Accountants* issued by the HKICPA, which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior.

Our firm applies Hong Kong Standard on Quality Control 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, and accordingly maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

Reporting accountants' responsibilities

Our responsibility is to express an opinion, as required by paragraph 4.29(7) 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.

We conducted our engagement in accordance with Hong Kong Standard on Assurance Engagements 3420 *Assurance Engagements to Report on the Compilation of Pro Forma Financial Information Included in a Prospectus* issued by the HKICPA. This standard requires that the reporting accountants plan and perform procedures to obtain reasonable assurance about whether the Directors have compiled the Unaudited Pro Forma Financial Information in accordance with paragraph 4.29 of the Listing Rules and with reference to AG 7 issued by the HKICPA.

For purposes of this engagement, we are not responsible for updating or reissuing any reports or opinions on any historical financial information used in compiling the Unaudited Pro Forma Financial Information, nor have we, in the course of this engagement, performed an audit or review of the financial information used in compiling the Unaudited Pro Forma Financial Information.

The purpose of the Unaudited Pro Forma Financial Information included in the Circular is solely to illustrate the impact of the Acquisition and the Preceding Loans Restructuring on unadjusted financial information of the Group as if the Acquisition and the Preceding Loans Restructuring had been undertaken at an earlier date selected for purpose of the illustration. Accordingly, we do not provide any assurance that the actual outcome of the Acquisition and the Preceding Loans Restructuring would have been as presented.

A reasonable assurance engagement to report on whether the Unaudited Pro Forma Financial Information has been properly compiled on the basis of the applicable criteria involves performing procedures to assess whether the applicable criteria used by the Directors in the compilation of the Unaudited Pro Forma Financial Information provide a reasonable basis for presenting the significant effects directly attributable to the Acquisition and the Preceding Loans Restructuring, and to obtain sufficient appropriate evidence about whether:

- the related pro forma adjustments give appropriate effect to those criteria; and

- the Unaudited Pro Forma Financial Information reflects the proper application of those adjustments to the unadjusted financial information.

The procedures selected depend on the reporting accountants' judgment, having regard to the reporting accountants' understanding of the nature of the Group, the Acquisition and the Preceding Loans Restructuring in respect of which the Unaudited Pro Forma Financial Information has been compiled, and other relevant engagement circumstances.

The engagement also involves evaluating the overall presentation of the Unaudited Pro Forma Financial Information.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion:

(a) the Unaudited Pro Forma Financial Information has been properly compiled on the basis stated;

(b) such basis is consistent with the accounting policies of the Group; and

(c) the adjustments are appropriate for the purpose of the Unaudited Pro Forma Financial Information as disclosed pursuant to paragraph 4.29(1) of the Listing Rules.

Yours faithfully,
Ernst & Young
Certified Public Accountants
Hong Kong

29 December 2017

The following is the text of a letter and valuation certificates, prepared for the purpose of incorporation in this circular received from Jones Lang LaSalle Corporate Appraisal and Advisory Limited, an independent valuer and consultant, in connection with its valuation as at 31 October 2017 of the property interests held by the Group.

JLL
仲量聯行

Jones Lang LaSalle Corporate Appraisal and Advisory Limited
6/F Three Pacific Place 1 Queen's Road East Hong Kong
tel +852 2846 5000 fax +852 2169 6001
Licence No.: C-030171

29 December 2017

The Board of Directors

AVIC International Holding (HK) Limited

Unit B, 15th, United Centre
No. 95 Queensway
Hong Kong

Dear Sirs,

Jones Lang LaSalle Corporate Appraisal and Advisory Limited ("**JLL**" or "**we**") is instructed by AVIC International Holding (HK) Limited (the "**Company**") to provide valuation service on two properties in which Dalian Hanghua Real Estate Development Company Limited ("**Dalian Hanghua**", a 52.08% interest owned subsidiary of the Company) and Chongqing Hanglong Real Estate Development Company Limited ("**Chongqing Hanglong**", a 99% interest owned subsidiary of the Company) (hereinafter together with the Company referred to as the "**Group**") have interest in the People's Republic of China (the "**PRC**"). We confirm that we have carried out inspections, made relevant enquiries and searches and obtained such further information as we consider necessary for the purpose of providing you with our opinion on the market values of the property interests as at 31 October 2017 (the "**valuation date**").

Our valuation is carried out on a market value basis. Market value is defined as "the estimated amount for which an asset or liability should exchange on the valuation date 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".

We have valued the properties held by the Group for sale and for future development by the comparison approach assuming sale of the property interests in their existing states with the benefit of immediate vacant possession and by making reference to comparable sales transactions as available in the market. This approach rests on the wide acceptance of the market transactions as the best indicator and pre-supposes that evidence of relevant transactions in the market place can be extrapolated to similar properties, subject to allowances for variable factors.

For the purpose of our valuation, completed properties for sale are those the Construction Work Completion and Inspection Certificate/Tables or Building Ownership Certificates/Real Estate Title Certificates thereof are issued by the relevant local authorities or are in the process of application, this also includes those property interests which have been contracted to be sold, but the formal assignment procedures of which have not yet been completed; and properties for future development are those the Construction Work Commencement Permits are not issued while the State-owned Land Use Rights Certificates have been obtained.

We have valued the properties held by the Group for investment by the income approach by taking into account the net rental income of the properties derived from the existing leases and/or achievable in the existing market with due allowance for the reversionary income potential of the leases, which have been then capitalized to determine the market value at an appropriate capitalization rate. Where appropriate, reference has also been made to the comparable sales transactions as available in the relevant market.

Our valuation has been made on the assumption that the seller sells the property interests in the market without the benefit of a deferred term contract, leaseback, joint venture, management agreement or any similar arrangement, which could serve to affect the values of the property interests.

No allowance has been made in our report for any charge, mortgage or amount owing on any of the property interests valued nor for any expense or taxation which may be incurred in effecting a sale. Unless otherwise stated, it is assumed that the properties are free from encumbrances, restrictions and outgoings of an onerous nature, which could affect their values.

In valuing the property interests, we have complied with all requirements contained in Chapter 5 and Practice Note 12 of the Rules Governing the Listing of Securities issued by the Stock Exchange of Hong Kong Limited; Rule 11 of the Code on Takeovers and Mergers issued by Securities and Futures Commission; the RICS Valuation — Global Standards published by the Royal Institution of Chartered Surveyors; the HKIS Valuation Standards published by the Hong Kong Institute of Surveyors, and the International Valuation Standards published by the International Valuation Standards Council.

We have relied to a very considerable extent on the information given by the Group and have accepted advice given to us on such matters as tenure, planning approvals, statutory notices, easements, particulars of occupancy, lettings, and all other relevant matters.

We have been shown copies of title documents including State-owned Land Use Rights Certificates, Real Estate Title Certificates, Construction Work Planning Permits, Construction Work Commencement Permits and other official plans relating to the property interests and have made relevant enquiries. Where possible, we have examined the original documents to verify the existing title to the property interests in the PRC and any material encumbrance that might be attached to the property interests or any tenancy amendment. If necessary, we recommend that a PRC legal opinion is sought to verify the existing title to the property interests in the PRC.

We have not carried out detailed measurements to verify the correctness of the areas in respect of the properties but have assumed that the areas shown on the title documents and official site plans handed to us are correct. All documents and contracts have been used as reference only and all dimensions, measurements and areas are approximations. No on-site measurement has been taken.

We have inspected the exterior and, where possible, the interior of the properties. However, we have not carried out investigation to determine the suitability of the ground conditions and services for any development thereon. Our valuation has been prepared on the assumption that these aspects are satisfactory and that no unexpected cost and delay will be incurred during construction. Moreover, no structural survey has been made, but in the course of our inspection, we did not note any serious defect. We are not, however, able to report whether the property is free of rot, infestation or any other structural defect. No tests were carried out on any of the services.

The site inspection was carried out in the period from 11 September 2017 to 14 September 2017 by Mr. Jack Ye who is a certified public valuer in the PRC and has 11 years' experience in property valuation in the PRC.

We have had no reason to doubt the truth and accuracy of the information provided to us by the Group. We have also sought confirmation from the Group that no material factors have been omitted from the information supplied. We consider that we have been provided with sufficient information to arrive an informed view, and we have no reason to suspect that any material information has been withheld.

All monetary figures stated in this report are in Renminbi (RMB).

Our summary of values and valuation certificates are attached below for your attention.

As advised by the Company, potential tax liabilities would be incurred on sales of the properties and they are mainly PRC value added tax and associated surcharges, PRC corporate income tax, PRC land appreciation tax and PRC stamp duty. The estimated total potential tax liability would be RMB308 million based on the assumption that the properties were to be sold at the amount of valuation in this report.

The Company is continuing to explore opportunities to dispose of the Group's real estate business. If the Company disposes of its real estate business through an equity transfer of the HK holding company of such real estate business, there will be no tax liability incurred in the PRC and only HK stamp duties (0.1% of the consideration) would apply.

Yours faithfully,
For and on behalf of
Jones Lang LaSalle Corporate Appraisal and Advisory Limited
Gilbert C. H. Chan
MRICS MHKIS RPS (GP)
Director

Note: *Gilbert C.H. Chan is a Chartered Surveyor who has 24 years' experience in the valuation of properties in the PRC.*

SUMMARY OF VALUES

Group I: Properties held for sale by the Group in the PRC
Group II: Properties held for investment by the Group in the PRC
Group III: Properties held for future development by the Group in the PRC

No.	Property [1]	Market value in existing state as at the valuation date *RMB* **Group I:**	Market value in existing state as at the valuation date *RMB* **Group II:**	Market value in existing state as at the valuation date *RMB* **Group III:**	The total market value of the property in existing state as at the valuation date *RMB*
1.	Project Zhonghang International Square located at southeastern of Zhongshan Road Shahekou District Dalian City Liaoning Province The PRC	1,801,000,000	305,900,000	694,800,000	2,801,700,000
2.	12 parcels of land located at Longxing Town Liangjiangxin District Chongqing The PRC	—	—	811,100,000	811,100,000
	Total:	**1,801,000,000**	**305,900,000**	**1,505,900,000**	**3,612,800,000**

Notes:

(1) The property does not include the portions which have been sold out before the valuation date and the proceeds from which have already been recognized as revenue.

VALUATION CERTIFICATE

No.	Property	Description and tenure	Particulars of occupancy	Market value in existing state as at the valuation date *RMB*
1.	Project Zhonghang International Square located at southeastern of Zhongshan Road Shahekou District Dalian City Liaoning Province The PRC	Project Zhonghang International Square (the "**Project**") is situated at southeastern of Zhongshan Road, Shahekou District, Dalian City. It occupies 4 parcels of land with a total site area of approximately 46,937.50 sq.m. which will be developed into a development complex with residential, apartment, retail, office and basement car parking spaces. The Project is well served by commercial and public facilities. The Project also enjoys easy access as it is only 1 kilometers off Subway Station. The Project is developed into 4 zones ("**Zone A**", "**Zone B**", "**Zone C**" and "**Zone D**"). Upon completion, the Project will have a total gross floor area ("**GFA**") of approximately 432,967.85 sq.m. Zone A and Zone C of the Project were completed in 2015. Zone D of the Project was completed in 2017. Zone B of the Project is currently a vacant land The property comprises the unsold residential, apartment and retail units, storerooms and car parking spaces of Zones A, C and D of the Project, a 12-storey office building of Zone A and the vacant land of Zone B of the Project. Details of GFA of the property are set out in note 7. The land use rights of the property have been granted for terms expiring on 13 February 2052 for commercial and financial uses and on 13 February 2082 for residential use respectively.	As at the valuation date, the unsold residential, apartment and retail units, storerooms and car parking spaces of Zones A, C and D of the Project are held by the Group for sale. Portions of the office building of Zone A, which are held by the Group for investment purpose, with a total GFA of approximately 17,871.91 sq.m. were rented to various tenants, whilst the remaining portion of the office building was vacant. Zone B is a vacant land.	2,801,700,000 (100% interest)

Notes:

1. As advised by the Group, Dalian Hanghua Real Estate Development Company Limited ("**Dalian Hanghua**") is a 52.08% interest owned subsidiary of the Company.

2. Pursuant to 4 State-owned Land Use Rights Certificates — Da Guo Yong (2013) Di Nos. 03015 to 03018, the land use rights of 4 parcels of land with a total site area of approximately 46,937.50 sq.m., on which the property is located, have been granted to Dalian Hanghua for terms expiring on 13 February 2052 for commercial and financial uses and on 13 February 2082 for residential use respectively.

3. Pursuant to 8 Real Estate Title Certificates — Sha You Xian Nos. 2016600757 to 2016600764, the building ownership of Zones A and C of the Project (including the unsold units of Zones A and C of the property) with a total GFA of approximately 128,541.43 sq.m. was owned by Dalian Hanghua.

4. Pursuant to a Construction Work Planning Permit —Jian Zi Di No.210204201300009 in favour of Dalian Hanghua, the construction works of Zone D with a total planned GFA of approximately 130,379.00 sq.m. (including the unsold units of Zone D of the property) have been approved for construction.

5. Pursuant to a Construction Work Commencement Permit — No. 210200201404251001 in favour of Dalian Hanghua, permissions by the relevant local authority were given to commence the construction of Zone D with a total GFA of approximately 130,379.00 sq.m. (including the unsold units of Zone D of the property) has been approved for construction.

6. Pursuant to 3 Pre-sale Permits — Da Fang Yu Xu Zi Di Nos. 20150035, 20160105 and 20170009, in favour of Dalian Hanghua, the Group is entitled to sell the Zone D of the property (representing a total GFA of approximately 94,135.00 sq.m.) to purchasers.

7. According to the information provided by the Group, details of the GFA of the property are set out below:

Zone	**Usage**	**GFA (sq.m.)**	**Car Parking Space (lot)**
Zone A	Office	21,147.87	
	Apartment	19,286.49	
	Retail	3,373.06	
	Car parking	1,091.50	91
	Sub-total:	**44,898.92**	**91**
Zone C	Retail	229.28	
	Car parking	2,757.00	229
	Storeroom	36.34	
	Sub-total:	**3,022.62**	**229**
Zone D	Residential	63,437.95	
	Retail	6,108.56	
	Car parking	6,057.02	488
	Storeroom	996.55	
	Sub-total:	**76,600.08**	**488**
Zone B	Office	92,409.00	
(planned)	Car parking	36,738.00	
	Ancillary	1,662.00	
	Sub-total:	**130,809.00**	
	Grand total:	**255,330.62**	**808**

8. As advised by Dalian Hanghua, 427 residential units with a total GFA of approximately 56,460.01 sq.m., 18 retail units with a total GFA of approximately 2,874.83 sq.m, 16 storerooms with a total GFA of approximately 256.84 sq.m and 295 car parking spaces of Zones A and C have been pre-sold to various third parties at a total consideration of RMB1,195,278,566. Such portions of the property have not been legally and virtually transferred and therefore we have included the units, the storerooms and the car parking spaces in our valuation. In arriving at our opinion on the market value of the property, we have taken into account the contracted prices of such portions of the property.

9. The Group has not obtained Construction Work Planning Permit and Construction Work Commencement Permit for Zone B of the property.

10. As advised by Dalian Hanghua, 45 office units of Zone A of the property with a total lettable area of approximately 17,871.91 sq.m. were rented to various tenants as at the valuation date for various terms with the expiry dates between 19 September 2017 and 14 October 2025 at a total annual rental of RMB21,992,975 exclusive of water and electricity charges.

11. Our valuation has been made on the following basis and analysis:

    a. For office, we have considered the actual rents in the existing tenancy agreements and also compared with similar properties located in the same business circle and/or nearby within reasonable walking distance, for the calculation of market rent in considering (1) the reversionary rental income after the expiry of the existing leases for occupied area, and (2) the rental income of vacant area;

    b. Based on our research, office unit rent of the comparable properties is in the range of RMB93 to RMB96 per sq.m. per month, appropriate adjustments and analysis are considered to the differences in location, size and other characters between the comparable properties and the property to arrive at the property market rent and/or market price.

    c. Based on our research, the stabilized market yield of similar properties is in the range of 5.5% to 6.0% for office use as at the valuation date. Considering the location and characteristics of the property, we have applied a market yield of 6.0% in the valuation.

    d. Based on our research, the stabilized market occupancy rate of similar properties is in the range of 85% to 90% for office use as at the valuation date. Considering the location and characteristics of the property, we have applied a market occupancy rate of 90% in the valuation.

    e. For residential, retail and car parking spaces, we have identified and analyzed various relevant sales evidences in the locality which have similar characteristics as the property. The unit prices of these comparable properties range from RMB15,000 to RMB18,000 per sq.m. for residential units, RMB35,000 to RMB40,000 per sq.m. for retail units on the first floor and RMB220,000 to RMB300,000 per lot for car parking spaces. Appropriate adjustments and analysis are considered to the differences in location, size and other characters between the comparable properties and the property to arrive at an assumed unit rate for the property.

    f. We have also made reference to sales prices of land within the locality which have the similar characteristics comparable to Zone B of the property. The prices of these comparable land sites are about RMB9,000 to RMB10,000 per sq.m. on floor area basis. Appropriate adjustments and analysis are considered to the differences in location, size and other characters between the comparable properties and the property to arrive at our assumed unit rate.

12. In valuing the property, we have assumed that:

    a. All land premium payments and other costs such as resettlement and ancillary utilities services have been paid in full and there is no requirement for payment of further land premium or other onerous payments to the government;

    b. The design and construction of the property are in compliance with the local planning regulations and have been approved by the relevant government authorities and all necessary authorizations and permits have been obtained in respect of the construction works. For Zone D of the property, there should not be any material legal impediment to obtain the relevant building ownership certificate by Dalian Hanghua; and

    c. The property can be freely transferred, leased or mortgaged by Dalian Hanghua without payment of any further land premium or transfer fees.

13. A summary of major certificates/approvals is shown as follows:

a.	State-owned Land Use Rights Certificate	Yes
b.	Construction Work Planning Permit	Yes
c.	Construction Work Commencement Permit	Yes
d.	Pre-sale Permit	Yes
e.	Real Estate Title Certificates	Portion

14. For the purpose of this report, the property is classified into the following groups according to the purpose for which it is held, we are of the opinion that the market value of each group as at the valuation date in its existing state is set out as below:

Group	**Market value in existing state as at the valuation date** *(RMB)*
Group I — held for sale	1,801,000,000
Group II — held for investment	305,900,000
Group III — held for future development	694,800,000
Grand total:	**2,801,700,000**

VALUATION CERTIFICATE

No.	Property	Description and tenure	Particulars of occupancy	Market value in existing state as at the valuation date *RMB*
2.	12 parcels of land located at Longxing Town Liangjiangxin District Chongqing The PRC	The property occupies 12 parcels of land with a total site area of approximately 375,252.00 sq.m. The land use rights of the property have been granted for a term expiring on 30 June 2064 for residential use.	The property is currently vacant land	811,100,000 (100% interest)

Notes:

1. As advised by the Group, Chongqing Hanglong Real Estate Development Company Limited ("**Chongqing Hanglong**") is a 99% interest owned subsidiary of the Company.

2. Pursuant to 2 State-owned Land Use Rights Grant Contracts dated on 29 September 2014, the land use rights of 2 parcels of land (on which the property is located) with a total site area of approximately 375,252.00 sq.m. were contracted to be granted to Chongqing Hanglong for a term of 40 years for commercial use and 50 years for residential use respectively. The total land premium was RMB740,590,000.00. As advised by Chongqing Hanglong, the land premium has been fully paid.

3. Pursuant to 2 Construction Land Planning Permits — Di Zi Di Nos. 500141201500056 and 500141201500058, permission towards the planning of the aforesaid 2 land parcels with a total site area of approximately 375,252.00 sq.m. has been granted to Chongqing Hanglong.

4. Pursuant to 12 Real Estate Title Certificates — 108 Fang Di Zheng 2014 Zi Di Nos. 14505, 14511, 14514, 14525, 14535, 14539, 14540, 14543, 14555, 14557, 14559 and 14562, the land use rights of 12 parcels of land (the 2 parcels of land mentioned in note 1) with a total site area of approximately 375,252.00 sq.m., on which the property is located, have been granted to Chongqing Hanglong for a term expiring on 30 June 2064 for residential use.

5. The Group has not obtained Construction Work Planning Permit and Construction Work Commencement Permit for the property.

6. Our valuation has been made on the following basis and analysis:

   a. we have made reference to sales prices of land within the locality which have the similar characteristics comparable to the property. The prices of these comparable land sites range from about RMB2,200 to RMB2,400 per sq.m. on floor area basis. Appropriate adjustments and analysis are considered to the differences in location, size and other characters between the comparable properties and the property to arrive at our assumed unit rate.

7. In valuing the property, we have assumed that:

   a. All land premium payments and other costs such as resettlement and ancillary utilities services have been paid in full and there is no requirement for payment of further land premium or other onerous payments to the government; and

   b. The property can be freely transferred, leased or mortgaged by Chongqing Hanglong without payment of any further land premium or transfer fees.

8. A summary of major certificates/approvals is shown as follows:

a.	State-owned Land Use Rights Grant Contract	Yes
b.	Real Estate Title Certificates	Yes
c.	Construction Work Planning Permit	No
d.	Construction Work Commencement Permit	No
e.	Pre-sale Permit	No
f.	Construction Work Completion and Inspection Certificate/Table	No
g.	Building Ownership Certificates	No

9. For the purpose of this report, the property is classified into the following groups according to the purpose for which it is held, we are of the opinion that the market value of each group as at the valuation date in its existing state is set out as below.

Group	**Market value in existing state as at the valuation date** *(RMB)*
Group I — held for sale	—
Group II — held for investment	—
Group III — held for future development	811,100,000
Grand total:	**811,100,000**

Mr. Zhang Ping

Mr. Zhang Ping, aged 53, was appointed as an independent non-executive Director and a member of the Audit Committee of the Company on 26 May 2017. He received a doctoral degree in Economics from Chinese Academy of Social Science Graduate School (中國社會科學院研究生院). Mr. Zhang started working at the Institute of Economics under Chinese Academy of Social Science (中國社會科學院經濟研究所) since July 1988. He once led and organized key national research project on economics. He published several essays based on theory research and surveys. His major research fields are the growth of China economy and macroeconomic policies. Mr. Zhang was an independent non-executive director of AVIC International Holdings Limited, a company listed on the Stock Exchange, until December 2014. He is currently an independent director of Minsheng Tonghui Asset Management Co., Ltd (民生通惠資產管理有限公司).

The Company has entered into a letter of appointment with Mr. Zhang and his term of appointment is three years commencing on 26 May 2017 which may be terminated by the Company upon not less than one month's notice. Mr. Zhang is subject to retirement by rotation and re-election at annual general meetings of the Company in accordance with the Bye-laws of the Company. Mr. Zhang's emoluments consist of a director's fee determined in consideration of his duties, experience and responsibilities and are subject to review by the Board from time to time pursuant to the power conferred on it at annual general meetings of the Company. The director's fee to Mr. Zhang annually amounts to HK$220,000.

Save as disclosed above, Mr. Zhang does not have any relationship with any Directors, senior management or substantial or controlling Shareholders of the Company and he did not hold any directorship in other listed public companies in the last three years. Mr. Zhang does not hold any other position with the Company and other members of the Group.

As at the Latest Practicable Date, Mr. Zhang did not have any interest in the shares of the Company within the meaning of Part XV of the SFO.

Save as set out above, there are no other matters regarding the re-election of Mr. Zhang which need to be brought to the attention of the Shareholders and there is no other information needs to be disclosed pursuant to the requirement of Rule 13.51(2) of the Listing Rules.

1. RESPONSIBILITY STATEMENT

This circular, for which the Directors of the Company jointly and severally accept full responsibility, includes particulars given in compliance with the Hong Kong Listing Rules, and the Takeovers Code for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that to the best of their knowledge and belief the information contained in this circular (other than those relating to the Concert Group) is accurate and complete in all material respects and not misleading or deceptive, opinions expressed in this circular (other than those expressed by the Concert Group) have been arrived at after due and careful consideration and there are no other matters the omission of which would make any statement in this circular misleading.

Further, the Directors jointly and severally accept full responsibility for the accuracy of information contained in this circular (other than those in respect of the Concert Group) and confirm, having made all reasonable enquiries, that to the best of their knowledge, opinions expressed in this circular (other than those expressed by the Concert Group) have been arrived at after due and careful consideration, and there are no other facts not contained in this circular, the omission of which would make any statement in this circular misleading.

The directors of AVIC HK, namely Mr. Liu Hongde, Mr. Lai Weixuan, Mr. Sun Jiguang, Ms. Zhou Chunhua and Mr. Liu Jun, jointly and severally accept full responsibility for the accuracy of the information contained in this circular relating to the Concert Group and confirms, having made all reasonable enquiries, that to the best of its knowledge, opinions expressed in this circular (other than those expressed by the Group) have been arrived at after due and careful consideration, and there are no other facts not contained in this circular the omission of which would make any statement in this circular misleading.

The directors of AVIC International, namely Mr. Liu Hongde, Mr. Sun Jiguang, Mr. Rong Yichao, Mr. Li Shangfu, Mr. Yan Dong, Mr. Lai Weixuan, Ms. Zhou Chunhua, Mr. You Lei, Ms. Sun Hongyan, Ms. Zhao Hongtao; Mr. Hui Xiaobing, Mr. Wang Huaishu and Ms. Kong Lingfen, jointly and severally accept full responsibility for the accuracy of the information contained in this circular relating to the Concert Group and confirm, having made all reasonable enquiries, that to the best of their knowledge, opinions expressed in this circular (other than those expressed by the Group) have been arrived at after due and careful consideration and there are no other facts not contained in this circular, the omission of which would make any statements in this circular misleading.

The directors of Aviation Industry, namely Mr. Lin Zuoming, Mr. Wang Jianqiang, Mr. Tan Ruisong, Mr. Li Wanyu, Mr. Chen Yuanxian, Mr. Liu Xihan and Mr. Zhao Zhengping, jointly and severally accept full responsibility for the accuracy of the information contained in this circular relating to the Concert Group and confirm, having made all reasonable enquiries, that to the best of their knowledge, opinions expressed in this circular (other than those expressed by the Group) have been arrived at after due and careful consideration and there are no other facts not contained in this circular, the omission of which would make any statements in this circular misleading.

2. SHARE CAPITAL

As at the Latest Practicable Date, the authorised and issued share capital of the Company were as follows:

Authorised:		*HK$*
10,000,000,000	Shares	1,000,000,000
Issued and fully paid, or credited as fully paid:		*HK$*
5,519,591,000	Shares	551,959,100

Upon allotment and issue of all the Consideration Shares, the authorised and issued share capital of the Company will be as follows:

Authorised:		*HK$*
10,000,000,000	Shares	1,000,000,000
Issued and fully paid, or credited as fully paid:		*HK$*
9,303,374,783	Shares	930,337,478

All Shares in issue rank *pari passu* in all respects regarding their rights to capital, dividends and voting.

No new Shares were issued since 31 December 2016, being the end of the last financial year of the Company to the Latest Practicable Date.

As at the Latest Practicable Date, the Company had no outstanding options, warrants, derivatives or securities convertible or exchangeable into Shares or other relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code).

3. MARKET PRICE

The table below shows the closing price per Share as quoted by the Stock Exchange (i) on the last day on which trading took place in each of the six calendar months during the period commencing six months preceding the Last Trading Day and ending on the Latest Practicable Date; (ii) on 19 September 2017, being the Last Trading Day; and (iii) as at the Latest Practicable Date:

Date	**Closing price per share** *(HK$)*
31 March 2017	0.45
28 April 2017	0.435
31 May 2017	0.42
30 June 2017	0.39
31 July 2017	0.385
31 August 2017	0.375
19 September 2017 (Last Trading Day)	0.365
29 September 2017	0.58
31 October 2017	0.52
30 November 2017	0.465
Latest Practicable Date	0.455

During the Whitewash Relevant Period, the lowest closing price of the Shares as quoted on the Stock Exchange was HK$0.36 per share on 25 August 2017, 29 August 2017, 1 September 2017, 13 September 2017, 18 September 2017, and the highest closing price of the Shares as quoted on the Stock Exchange was HK$0.73 per share on 22 September 2017.

4. INTEREST IN AND DEALINGS IN SECURITIES OF AVIC HK

a. As at the Latest Practicable Date, the Company was not interested in any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in AVIC HK, and had not dealt in any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in AVIC HK during the Whitewash Relevant Period.

b. None of the Directors had dealt in any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company or AVIC HK during the Whitewash Relevant Period.

c. As at the Latest Practicable Date, save as disclosed in the paragraph headed "6. Disclosure of interests" in this Appendix, none of the Directors were interested in any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company or AVIC HK.

d. As at the Latest Practicable Date, none of the subsidiaries of the Company, the pension fund of the Company or its subsidiaries, or the adviser to the Company as specified in class (2) of the definition of "associate" under the Takeovers Code owned or controlled any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company, or had dealt in any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company during the Whitewash Relevant Period.

e. As at the Latest Practicable Date and during the Whitewash Relevant Period, there was no arrangement of the kind referred to in Note 8 to Rule 22 of the Takeovers Code between any person and the Company or any person who is an associate of the Company by virtue of classes (1), (2), (3) and (4) of the definition of "associate" under the Takeovers Code.

f. As at the Latest Practicable Date, there were no relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company which were managed on a discretionary basis by fund managers connected with the Company, and none of them had dealt in any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company during the Whitewash Relevant Period.

g. As at the Latest Practicable Date, none of the Company or the Directors had borrowed or lent any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) in the Company.

5. SHAREHOLDING AND DEALING IN SECURITIES OF THE COMPANY

As at the Latest Practicable Date:

(a) save as disclosed under the section headed "V. Effect of the Acquisition and Offering on the Shareholding Structure of the Company" in the letter from the Board, none of AVIC HK, the directors of AVIC HK, and/or any of AVIC HK's parties acting in concert with it owned or had control or direction over any voting rights or rights over the Shares or convertible securities, warrants, options of the Company or any derivatives in respect of such securities;

(b) there is no outstanding derivative in respect of the securities in the Company entered into by AVIC HK or parties acting in concert with it;

(c) none of AVIC HK, its ultimate beneficial owners and/or parties acting in concert with any of them had borrowed or lent any Shares or any relevant securities (as defined in Note 4 to Rule 22 of the Takeovers Code) of the Company;

(d) none of AVIC HK, and/or any parties acting in concert with it has received any irrevocable commitment in relation to voting of the resolutions in respect of the Acquisition, the Whitewash Waiver or any transactions contemplated thereunder at the coming SGM;

(e) there was no arrangement of the kind referred to in Note 8 to Rule 22 of the Takeovers Code existed between AVIC HK or any party acting in concert with it and any other person, or between any other associate of AVIC HK and any other person;

(f) there is no agreement or arrangement to which AVIC HK, and/or any parties acting in concert with it is a party which relates to circumstances in which it may or may not invoke or seek to invoke a pre-condition or a condition to the Acquisition, the Whitewash Waiver or any transactions contemplated thereunder, including any break fees being payable; and

(g) there was no agreement (whether by way of options, indemnity or otherwise) in relation to the shares of AVIC HK and parties acting in concert with it or the Company which might be material to the Acquisition and Whitewash Waiver.

6. DISCLOSURE OF INTERESTS

AVIC HK is a direct wholly owned subsidiary of AVIC International, which in turn is a non-wholly owned subsidiary of Aviation Industry, a Chinese state-owned company overseen by the SASAC of the State Council. As at the Latest Practicable Date, the Concert Group held 1,895,715,000 Shares, representing approximately 34.35% of the total issued share capital of the Company.

None of AVIC HK or parties acting in concert with it had dealt for value in any Shares, convertible securities, warrants or options of the Company or any derivatives in respect of such securities during the Whitewash Relevant Period.

Except for certain Directors who had non-beneficial interests in certain subsidiaries of the Company held for the benefits of the Company, as at the Latest Practicable Date, none of the Directors and chief executive of the Company had an interest or short position in the shares or underlying shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions in which he was deemed or taken to have under such provisions of the SFO), or which were required, pursuant to section 352 of the SFO, to be entered in the register maintained by the Company referred to therein, or which were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers contained in the Listing Rules, to be notified to the Company and the Stock Exchange.

As at the Latest Practicable Date:

(i) there was no benefit given or to be given to any Directors as compensation for loss of office in any member of the Group or otherwise in connection with the Acquisition Agreement (together with the transactions contemplated therein, including the issue of Consideration Shares) and the Whitewash Waiver;

(ii) there was no agreement, arrangement or understanding between AVIC HK or any parties acting in concert with it and any of the Directors, recent Directors, Shareholders or recent Shareholders having any connection with or dependence upon the Acquisition Agreement (together with the transactions contemplated therein, including the issue of the Consideration Shares) and the Whitewash Waiver;

(iii) there was no agreement, arrangement or understanding between any Directors and any other persons which is conditional on or dependent upon the outcome of the Acquisition Agreement (together with the transactions contemplated therein, including the issue of the Consideration Shares) and the Whitewash Waiver; and

(iv) save for the Offering, there was no agreement, arrangement or understanding between AVIC HK or any parties acting in concert with it and other persons in relation to the transfer, charge or pledge of the Shares that may be issued and allotted to AVIC HK or any parties acting in concert with it under the Acquisition Agreement or as a result of any obligation under the Acquisition Agreement.

7. SUBSTANTIAL SHAREHOLDERS

As at the Latest Practicable Date, so far as the Directors and chief executive of the Company were aware, the following persons (other than a director or chief executive of the Company) who had an interest or a short position in the Shares and underlying Shares which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO or which were recorded in the register required to be kept under section 336 of the SFO were as follows:

Long positions in the Shares and underlying Shares:

Name of shareholder	*Notes*	Capacity and nature of interest	Number of ordinary shares held	Approximate percentage of the Company's issued share capital as at the Latest Practicable Date
Tacko International Limited ("Tacko")	*(a)*	Beneficial owner	1,895,559,000	34.34
AVIC HK	*(a)*	Through a controlled corporation	1,895,559,000	34.34
AVIC International	*(a)*	Through a controlled corporation	1,895,559,000	34.34
Aviation Industry	*(a)*	Through a controlled corporation	1,895,559,000	34.34
Cheung Kong (Holdings) Limited ("CKH")	*(b)*	Through controlled corporations	450,000,000	8.15
CK Hutchison Holdings Limited ("CKHH")	*(b)*	Through controlled corporations	450,000,000	8.15

Notes:

(a) Tacko is a wholly-owned subsidiary of AVIC HK, which in turn is a wholly-owned subsidiary of AVIC International. AVIC International is a non-wholly-owned subsidiary of Aviation Industry (62.52% interest controlled by Aviation Industry as at the Latest Practicable Date). Accordingly, each of AVIC HK, AVIC International and Aviation Industry is deemed to be interested in the shares held by Tacko.

(b) According to notices of disclosure of interests filed with the Company, 225,000,000 shares are held by Worsdale Investments Limited ("Worsdale") and 225,000,000 shares are held by Hutchison International Limited ("HIL").

Worsdale is a wholly-owned subsidiary of Arra International Limited, which in turn is a wholly-owned subsidiary of Cheung Kong Investment Company Limited ("CKIV"). CKIV is a wholly-owned subsidiary of CKH. CKH is deemed to be interested in 225,000,000 shares held by Worsdale. Meanwhile, HIL is a wholly-owned subsidiary of Hutchison Whampoa Limited ("HWL"). HWL is deemed to be interested in 225,000,000 shares held by HIL. CKH is entitled to exercise or control the exercise of more than one-third of the voting power at the general meetings of HWL. Accordingly, CKH is also deemed to be interested in 225,000,000 shares held by HIL. In addition, CKH is a wholly-owned subsidiary of CKHH and accordingly, CKHH is deemed to be interested in the aggregate shares directly held by Worsdale and HIL.

Save as disclosed above, the Directors and chief executive of the Company were not aware of any other persons who, as at the Latest Practicable Date, had an interest or a short position in the Shares and underlying Shares which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or which were recorded in the register required to be kept under section 336 of the SFO.

8. DIRECTOR'S INTERESTS IN ASSETS/CONTRACTS

As at the Latest Practicable Date, none of the Directors had any interest, direct or indirect, in any assets which have since 31 December 2016, being the date to which the latest published audited financial statements of the Company were made up, been acquired or disposed of by or leased to any member of the Enlarged Group or are proposed to be acquired or disposed of by or leased to any member of the Enlarged Group.

As at the Latest Practicable Date, none of the Directors was materially interested in any contract or arrangement subsisting at the Latest Practicable Date and which is significant in relation to the business of the Enlarged Group.

9. DIRECTORS' SERVICE CONTRACTS

As at the Latest Practicable Date, none of the Directors had any existing or proposed service contract with any member of the Enlarged Group or any associated company of the Group: (a) which have been entered into or amended within six months before 19 September 2017, which is the date of the announcement of the Company relating to the Acquisition and Whitewash Waiver; (b) which are continuous contracts with a notice period of 12 months or more; or (c) which are fixed term contracts with more than 12 months to run irrespective of the notice period.

No contracts of significance had been entered into by AVIC HK in which any Director has a material personal interest.

10. MATERIAL CHANGE

Save as disclosed below and in the interim report of the Group for 1H2017 in which an aggregate loss of HK$9.4 million relating to the investments (financial assets, joint venture and associate) held by the Group for 1H2017 has been recorded, the Directors confirm that there has been no material change in the financial or trading position or outlook of the Group since 31 December 2016, being the date to which the latest published audited consolidated financial statements of the Group were made up, up to and including the Latest Practicable Date:

(i) with reference to the latest valuation report on the Group's properties as set out in Appendix V to this circular ("**Latest Valuation**"), the Group expects that a revaluation deficit will be recorded for the year ending 31 December 2017 as the Latest Valuation has already shown a revaluation deficit of approximately HK$109 million, after taken into account the relevant tax impact and adjusting for relevant interests not attributable to the owners of the Company;

(ii) the Group will be engaged in the manufacturing of and providing services to general aviation aircraft piston engines upon Acquisition Completion; and

(iii) the Group's revenue for the ten months ended 31 October 2017 ("**10M2017**"), based on its unaudited consolidated management accounts, amounted to approximately HK$452 million, representing an increase of more than 3 times comparing to the same period in 2016 ("**10M2016**"). However, the Group's gross profit margin in 10M2017 is significantly lower than that in 10M2016, mainly because a substantial portion of the revenue for 10M2017 represents the recognition of sale of properties of Dalian Project pre-sold in 2015 and 2016 when the price was comparatively low due to the then market sentiment.

11. COMPETING INTERESTS

The following Director had interests in the following businesses conducted through the company named below which are considered to compete or be likely to compete, either directly or indirectly, with the business of the Group, as defined in the Listing Rules:

Name of Director	Name of company	Nature of interest	Nature of competing business
Chow Wai Kam	Cheung Kong Property Holdings Limited	Executive director	- property development and investment ("Excluded Businesses")

The Board is of the view that the Group is capable of carrying on its business independently of the Excluded Businesses. When making decisions on the businesses of the Excluded Businesses of the Group, Mr. Chow, in the performance of his duties as Director, has acted and will continue to act in the best interests of the Group.

So far as the Directors were aware, save as abovementioned, as at the Latest Practicable Date, none of the Directors or their respective associates had any interest in any business which competed or was likely to compete with the business of the Group (as would be required to be disclosed under Rule 8.10 of the Listing Rules if each of them were a controlling shareholder).

12. EXPERTS AND CONSENTS

The following sets out the qualifications of the experts who have been named in this circular:

Name	Qualifications
Anglo Chinese	Anglo Chinese Corporate Finance, Limited, a corporation licensed to carry out type 1 (dealing in securities), type 4 (advising on securities), type 6 (advising on corporate finance) and type 9 (asset management) regulated activities under the SFO
Conyers Dill & Pearman	BVI and Bermuda legal counsel to the Company
Ernst & Young	Certified public accountants
Euromonitor	Independent market research consultant
Freshfields Bruckhaus Deringer	Germany legal counsel to the Company
Jia Yuan Law Offices	PRC legal counsel to the Company
JLL	Independent professional surveyor
Maynard, Cooper & Gale, P.C.	US legal counsel to the Company
Somerley	Somerley Capital Limited, a corporation licensed to carry out type 1 (dealing in securities) and type 6 (advising on corporate finance) regulated activities under the SFO and the independent financial adviser to the Independent Board Committees and the Independent Shareholders in respect of the Acquisition, Whitewash Waiver and the Sale Framework Agreement

Each of the above experts has given and has not withdrawn its written consent to the issue of this circular with the inclusion herein of its letter and references to its name, in the form and context in which they respectively appear.

As at the Latest Practicable Date, none of the above experts had any shareholding, directly or indirectly, in any member of the Enlarged Group or the right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for shares in any member of the Enlarged Group.

As at the Latest Practicable Date, none of the above experts had any interest, direct or indirect, in any assets which since 31 December 2016, the date to which the latest published audited financial statements of the Company were made up, had been acquired or disposed of by or leased to any member of the Enlarged Group, or are proposed to be acquired or disposed of by or leased to any member of the Enlarged Group.

13. MATERIAL CONTRACTS

The following contracts (not being contracts entered into in the ordinary course of business) were entered into by the members of the Enlarged Group within two years immediately preceding the issue of this circular and are or might be material:

(a) the Acquisition Agreement; and

(b) the sales and purchase agreement dated 29 June 2016 entered into between (i) 上海瑞爾通投資顧問有限公司(Shanghai RET Investment Consulting Company Limited*) ("**RET**"), an indirect wholly-owned subsidiary of the Company, (ii) 浙江東陽金牛針織製衣有限公司 (Zhejiang Dongyang Jinniu Knitting and Garment Company Limited*) ("**Jinniu**"), which was then a 51%-owned subsidiary of RET, (iii) Mr. Fu Yuqun, an independent third party, and (iv) Mr. Wu Xiaogang, who owned 49% equity interest in Jinniu, in relation to, among other things, the disposal of the 51% equity interest in Jinniu by RET to Mr. Fu Yuqun at a cash consideration of RMB5,000,000.

* English translation is for identification only.

14. LITIGATION

As at the Latest Practicable Date, the Enlarged Group was not engaged in any litigation or claims of material importance and there was no litigation or claims of material importance known to the Directors to be pending or threatened by or against the Enlarged Group.

15. MISCELLANEOUS

(a) The company secretary of the Company is Ms. Tsui Choi Yee, Connie, a member of the Hong Kong Institute of Certified Public Accountants and a CPA member of CPA Australia.

(b) The registered office of the Company is at Canon's Court, 22 Victoria Street, Hamilton, HM 12, Bermuda. The head office and principal place of business of the Company is at Unit B, 15th Floor, United Centre, 95 Queensway, Hong Kong.

(c) The share registrar and transfer office of the Company in Bermuda is MUFG Fund Services (Bermuda) Limited at The Belvedere Building, 69 Pitts Bay Road, Pembroke HM 08, Bermuda.

(d) The branch share registrar and transfer office of the Company in Hong Kong is Computershare Hong Kong Investor Services Limited at Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong.

(e) The English text of this circular and the enclosed proxy form shall prevail over the Chinese text.

(f) The registered office of AVIC HK is 20/F, Tower II, Admiralty Centre, 18 Harcourt Road, Admiralty, Hong Kong.

(g) The registered office of Anglo Chinese is 40th Floor, Two Exchange Square, 8 Connaught Place, Central, Hong Kong.

(h) The registered office of Somerley is 20th Floor, China Building, 29 Queen's Road Central, Hong Kong.

16. DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents will be available for inspection during normal business hours at (i) the office of the Company at Unit B, 15/F., United Centre, 95 Queensway, Hong Kong; (ii) the website of the Company at www.avic.com.hk; and (iii) the website of SFC at http://www.sfc.hk from the Latest Practicable Date up to and including the date of the SGM:

(a) the Bye-laws of the Company;

(b) the letter from the Board, the text of which is set out on pages 8 to 31 of this circular;

(c) the letter from the Code IBC, the text of which is set out on pages 32 to 33 of this circular;

(d) the letter from the LR IBC, the text of which is set out on pages 34 to 35 of this circular;

(e) the letter from Somerley, the text of which is set out on pages 36 to 83 of this circular;

(f) the annual reports and interim report of the Company for each of FY2014, FY2015, FY2016 and 1H2017 ;

(g) the accountants' report on the Target Company prepared by Ernst & Young, the text of which is set out in Appendix III to this circular;

(h) the accountants' report on the compilation of unaudited pro forma financial information of the Enlarged Group issued by Ernst & Young, the text of which is set out in Appendix IV to this circular;

(i) the valuation report issued by JLL;

(j) a copy of each of the material contracts as set out in the section headed "Material Contracts" in this Appendix;

(k) the written consents referred to in the section headed "Experts and Consents" in this Appendix; and

(l) this circular.

AVIC International Holding (HK) Limited
中國航空工業國際控股(香港)有限公司

(Incorporated in Bermuda with limited liability)

(Stock Code: 232)

NOTICE OF SPECIAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that a special general meeting of the shareholders of AVIC International Holding (HK) Limited (the "**Company**") will be held at Monaco Room, Basement 1, Regal Hongkong Hotel, 88 Yee Wo Street, Causeway Bay, Hong Kong on Tuesday, 23 January 2018 at 3:00 p.m. (the "**SGM**") for the purposes of considering and, if thought fit, passing, with or without amendments, the following resolutions as ordinary resolutions of the Company:

ORDINARY RESOLUTIONS

1. **"THAT:**

a. the Acquisition Agreement (as defined in the circular of the Company dated 29 December 2017 (the "**Circular**"), a copy of which is marked ''A'' and initialed by the chairman of the meeting for the purpose of identification) dated 19 September 2017 entered into between the Company, AVIC International (HK) Group Limited ("**AVIC HK**") and AVIC International Holding Corporation relating to the acquisition of the entire issued share capital of Motto Investment Limited ("**Target Company**") and the shareholder's loan note(s) owing by the Target Company to AVIC HK as at the Acquisition Completion (as defined in the Circular) and the transactions contemplated thereunder be and are hereby approved, confirmed and ratified;

b. the directors of the Company (the "**Directors**") be and are hereby granted a specific mandate ("**Specific Mandate**") to exercise the powers of the Company to allot and issue the Consideration Shares (as defined in the Circular) pursuant to the terms and conditions of the Acquisition Agreement. Such Consideration Shares shall rank equally in all respects among themselves and with all fully paid ordinary shares of the Company in issue as at the date of allotment and issue. The Specific Mandate is in addition to, and shall not prejudice nor revoke any general or special mandate(s) which has/have been granted or may from time to time be granted to the Directors prior to the passing of this resolution;

c. subject to the Executive (as defined in the Circular) granting the Whitewash Waiver (as defined in the Circular) to AVIC HK and the satisfaction of any conditions attached to the Whitewash Waiver granted, the waiver pursuant to Note 1 on the dispensations from Rule 26 of the Hong Kong Code on Takeovers and Mergers waiving any obligation on the part of AVIC HK to make a mandatory general offer for all of the shares of the Company not already owned or agreed to be acquired by the Concert Group (as defined in the Circular) as a result of the allotment and issuance of the Consideration Shares to AVIC HK be and is hereby approved; and

d. any one director of the Company be and is hereby authorised to do all acts and things and to execute all such documents (including the affixation of the common seal of the Company where execution under seal is required) and take all steps which, in his/her opinion deem necessary, are desirable or expedient to carry out or to give effect to any matters relating to or in connection with the Acquisition Agreement and Whitewash Waiver."

2. "**THAT**:

a. the Sale Framework Agreement (as defined in the Circular, a copy of which is marked "B" and initialed by the chairman of the meeting for the purpose of identification), the transaction contemplated thereunder, the proposed annual caps thereunder and all other transactions in connection therewith and any other ancillary documents, be and are hereby confirmed, approved and ratified, subject to such addition or amendment as any Director(s) may consider necessary, desirable or appropriate; and

b. any one director of the Company be and is hereby authorised to do all acts and things and to execute all such documents (including the affixation of the common seal of the Company where execution under seal is required) and take all steps which, in his/her opinion deem necessary, are desirable or expedient to carry out or to give effect to any matters relating to or in connection with the Sale Framework Agreement."

3. "**THAT**:

to re-elect Mr. Zhang Ping as an independent non-executive director of the Company (the "**INED**") and to authorise the board of directors of the Company to fix the INED's remuneration."

By order of the Board
AVIC International Holding (HK) Limited
Liu Hongde
Chairman

Hong Kong, 29 December 2017

NOTICE OF SPECIAL GENERAL MEETING

Registered office:
Canon's Court
22 Victoria Street
Hamilton, HM 12
Bermuda

Head office and principal place of business in Hong Kong:
Unit B, 15th Floor
United Centre
95 Queensway
Hong Kong

Notes:

1. A member of the Company entitled to attend and vote at the SGM is entitled to appoint a proxy to attend and vote instead of him. A proxy need not be a member of the Company. A member who is the holder of two or more shares of the Company may appoint more than one proxy to represent him to attend and vote on his behalf. If more than one proxy is so appointed, the appointment shall specify the number and class of shares in respect of which each such proxy is so appointed.

2. To be valid, the proxy form, together with any power of attorney or other authority (if any) under which it is signed, or a notarially certified copy thereof, must be lodged with the Company's Hong Kong branch share registrar and transfer office, Computershare Hong Kong Investor Services Limited at 17M Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong as soon as possible and in any event not less than 48 hours before the time appointed for holding the meeting or any adjournment thereof. Completion and return of the form of proxy will not preclude a member from attending and voting at the meeting if the member so desires.

3. Where there are joint registered holders of any share(s), any one of such persons may vote at the meeting, either personally or by proxy, in respect of such share(s) as if he were solely entitled thereto; but if more than one of such joint holders be present at the meeting personally or by proxy, that one of the said persons so present whose name stands first on the register of members of the Company in respect of such share(s) shall alone be entitled to vote in respect thereof.

4. The voting on the above resolutions at the SGM will be conducted by way of a poll.

5. The register of members of the Company will be closed from Thursday, 18 January 2018 to Tuesday, 23 January 2018, both days inclusive, during which period no transfer of Shares will be registered, in order to determine the entitlement to attend and vote at the SGM. In order to be entitled to attend and vote at the SGM, unregistered holders of Shares should ensure that all transfers of Shares accompanied by the relevant share certificates and properly completed transfer forms must be lodged for registration with the Hong Kong branch share registrar and transfer office, Computershare Hong Kong Investor Services Limited at Rooms 1712-1716, 17th Floor, Hopewell centre, 183 Queen's Road East, Wan Chai, Hong Kong no later than 4:30 p.m. on Wednesday, 17 January 2018.