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**THIS CIRCULAR IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION**

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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 or registered institution in securities, bank manager, solicitor, professional accountant or other professional adviser.

If you have sold or transferred all your Shares in First Tractor Company Limited\*, you should at once hand this circular to the purchaser(s) or the transferee(s), or to the bank, licensed securities dealer or other agent through whom the sale or the transfer was effected for transmission to the purchaser(s) or the transferee(s).

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**第一拖拉机股份有限公司**  
**FIRST TRACTOR COMPANY LIMITED**\*

*(a joint stock company incorporated in The People's Republic of China with limited liability)*

(Stock Code: 0038)

**REVISION OF 2017 AND 2018 ANNUAL CAPS FOR  
CONTINUING CONNECTED TRANSACTIONS**

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

**VEDA | CAPITAL**  
**智 略 资 本**

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A letter from the Board is set out on pages 1 to 19 of this circular. A letter from the Independent Board Committee is set out on pages 20 to 21 of this circular. A letter from Veda Capital Limited, the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders, containing its advice to the Independent Board Committee and the Independent Shareholders is set out on pages 22 to 55 of this circular.

A notice for convening the annual general meeting (the "AGM") of First Tractor Company Limited\* (the "Company") to be held at 2:15 p.m. on 13 June 2017 (Tuesday) at No. 154 Jianshe Road, Luoyang, Henan Province, the People's Republic of China (the "PRC"), is set out on pages 60 to 65 of this circular.

A form of proxy for use at the AGM was despatched and also published on the website of The Stock Exchange of Hong Kong Limited (<http://www.hkexnews.hk>) on 26 April 2017. Whether or not you are able to attend the meeting in person, you are requested to complete and return the form of proxy in accordance with the instructions printed thereon. The proxy form shall be lodged with the Company's branch share registrar in Hong Kong, Hong Kong Registrars Limited, at Shops 1712–1716, 17/F., Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, or at the registered address and principal place of business of the Company at No. 154 Jianshe Road, Luoyang, Henan Province, the PRC, as soon as possible and in any event not less than 24 hours before the time scheduled for holding the AGM (or any adjourned meeting thereof). Completion and delivery of the form of proxy will not preclude you from attending and voting in person at the AGM or any adjournment if you so desire.

22 May 2017

\* For identification purpose only

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## DEFINITIONS

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*In this circular, unless the context requires otherwise, the following terms shall have the following meanings:*

|   |  |
|---|--|
| “AGM”   | the 2016 annual general meeting of the Company to be held on 13 June 2017 (Tuesday) at 2:15 p.m. for the purposes of, among other things, seeking the Independent Shareholders’ approval for the Proposed Revised Annual Caps;   |
| “Annual Cap(s)”                                       | the maximum aggregate annual value(s) for the continuing connected transactions under the CCT Agreements;  |
| “associate(s)”  | has the same meaning as ascribed to this term under the Listing Rules;   |
| “Board”   | the board of Directors of the Company;   |
| “CCT Agreements”                                      | the Material Procurement Agreement, the Sale of Goods Agreement and the Composite Services Agreement;  |
| “Company”   | First Tractor Company Limited* (第一拖拉機股份有限公司), a joint stock company with limited liability incorporated in the PRC, the H Shares and A Shares of which are listed on the main board of the Stock Exchange (stock code: 0038) and the Shanghai Stock Exchange (stock code: 601038) respectively;  |
| “Composite Services Agreement”                        | the agreement dated 25 August 2015 entered into between YTO, on behalf of YTO, its controlled companies and their associates, as supplier and/or supplying agent, and the Company, on behalf of the Group, as purchaser and/or purchasing agent, pursuant to which YTO, its controlled companies and their associates agreed to provide storage services and transportation services to the Group; |
| “Composite Services Agreement Existing Annual Cap(s)” | the existing Annual Caps for the transactions contemplated under the Composite Services Agreement for the years ending 31 December 2017 and 2018 approved by the then Independent Shareholders at the extraordinary general meeting of the Company on 29 October 2015, which are RMB157,200,000 and RMB167,200,000 respectively;   |

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## DEFINITIONS

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|---|---|
| “Composite Services Agreement Proposed Revised Annual Cap(s)” | the proposed revised Annual Caps for the transactions contemplated under the Composite Services Agreement for the years ending 31 December 2017 and 2018 as approved by the Board on 28 February 2017 subject to the approval of the Independent Shareholders at the AGM, which are RMB215,000,000 and RMB225,000,000 respectively; |
| “connected person(s)”   | has the same meaning as ascribed to this term under the Listing Rules;  |
| “controlling shareholder”                                     | has the same meaning as ascribed to this term under the Listing Rules;  |
| “Director(s)”   | the director(s) of the Company, including the independent non-executive director(s);  |
| “Existing Annual Caps”  | the Material Procurement Agreement Existing Annual Caps, the Sale of Goods Agreement Existing Annual Caps and the Composite Services Agreement Existing Annual Caps;  |
| “Group”   | the Company and its subsidiaries;   |
| “Hong Kong”   | the Hong Kong Special Administrative Region of the PRC;   |
| “Independent Board Committee”                                 | an independent committee of the Board comprising all the independent non-executive Directors;   |
| “Independent Shareholder(s)”                                  | Shareholder(s) other than YTO and its associate(s);   |
| “Latest Practicable Date”                                     | 15 May 2017, being the latest practicable date prior to the printing of this circular for ascertaining certain information contained herein;  |
| “Listing Rules”   | the Rules Governing the Listing of Securities on the Stock Exchange;  |

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## DEFINITIONS

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|---|--|
| “Material Procurement Agreement”                                | the agreement dated 25 August 2015 entered into between YTO, on behalf of YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach, as supplier and/or supplying agent, and the Company, on behalf of the Group, as purchaser and/or purchasing agent, pursuant to which YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach agreed to supply certain materials to the Group; |
| “Material Procurement Agreement Existing Annual Cap(s)”         | the existing Annual Caps for the transactions contemplated under the Material Procurement Agreement for the years ending 31 December 2017 and 2018 approved by the then Independent Shareholders at the extraordinary general meeting of the Company on 29 October 2015, which are both RMB500,000,000;  |
| “Material Procurement Agreement Proposed Revised Annual Cap(s)” | the proposed revised Annual Caps for the transactions contemplated under the Material Procurement Agreement for the years ending 31 December 2017 and 2018 as approved by the Board on 28 February 2017 subject to the approval of the Independent Shareholders at the AGM, which are RMB1,498,000,000 and RMB1,648,000,000 respectively;  |
| “percentage ratio(s)”   | has the same meaning as ascribed to this term under the Listing Rules, as applicable to a transaction;   |
| “PRC”   | The People’s Republic of China which, for the purpose of this circular, excludes Hong Kong, the Macau Special Administrative Region of the PRC and Taiwan;   |
| “Proposed Revised Annual Caps”                                  | the Material Procurement Agreement Proposed Revised Annual Caps, the Sale of Goods Agreement Proposed Revised Annual Caps and the Composite Services Agreement Proposed Revised Annual Caps;   |
| “RMB”   | Renminbi, the lawful currency of the PRC;  |

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## DEFINITIONS

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| “Sale of Goods Agreement”                                | the agreement dated 25 August 2015 entered into between the Company, on behalf of the Group, as supplier and/or supplying agent, and YTO, on behalf of YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach, as purchaser and/or purchasing agent, pursuant to which the Group agreed to supply certain materials to YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach; |
| “Sale of Goods Agreement Existing Annual Cap(s)”         | the existing Annual Caps for the transactions contemplated under the Sale of Goods Agreement for the years ending 31 December 2017 and 2018 approved by the then Independent Shareholders at the extraordinary general meeting of the Company on 29 October 2015, which are RMB200,000,000 and RMB210,000,000 respectively;  |
| “Sale of Goods Agreement Proposed Revised Annual Cap(s)” | the proposed revised Annual Caps for the transactions contemplated under the Sale of Goods Agreement for the years ending 31 December 2017 and 2018 as approved by the Board on 28 February 2017 subject to the approval of the Independent Shareholders at the AGM, which are RMB460,000,000 and RMB488,000,000 respectively;   |
| “SFO”  | the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) as amended from time to time;  |
| “Share(s)”   | share(s) of RMB1.00 each of the Company;   |
| “Shareholder(s)”   | shareholder(s) of the Company;   |
| “Sinomach”   | China National Machinery Industry Corporation* (中國機械工業集團有限公司), a limited liability company incorporated in the PRC and a controlling shareholder of YTO, holding approximately 87.90% equity interest in YTO;  |
| “Stock Exchange”   | The Stock Exchange of Hong Kong Limited;   |
| “subsidiary(ies)”  | has the same meaning as ascribed to this term under the Listing Rules;   |

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## DEFINITIONS

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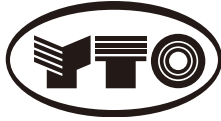
|   |   |
|---|---|
| “Veda Capital” or “Independent Financial Adviser” | Veda Capital Limited, a licensed corporation to carry on Type 6 (advising on corporate finance) regulated activity under the SFO, being the independent financial adviser to the Company to advise the Independent Board Committee and the Independent Shareholders in respect of the Proposed Revised Annual Caps; |
| “YTO”   | YTO Group Corporation* (中國一拖集團有限公司), a limited liability company incorporated in the PRC and the immediate controlling shareholder of the Company, holding approximately 41.24% equity interest in the Company;   |
| “YTO Group”                                       | YTO and its subsidiaries; and   |
| “%”   | per cent.   |

\* *For identification purpose only*

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## LETTER FROM THE BOARD

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**第一拖拉机股份有限公司**  
**FIRST TRACTOR COMPANY LIMITED\***

*(a joint stock company incorporated in The People's Republic of China with limited liability)*

(Stock Code: 0038)

*Board of Directors:*

Mr. Zhao Yanshui (*Chairman*)

Mr. Wang Erlong (*Vice Chairman*)

Mr. Wu Yong

Mr. Li Hepeng

Mr. Xie Donggang

Mr. Li Kai

Mr. Yin Dongfang

Ms. Yang Minli\*\*

Mr. Xing Min\*\*

Mr. Wu Tak Lung\*\*

Mr. Yu Zengbiao\*\*

*Registered and principal office:*

No. 154 Jianshe Road

Luoyang, Henan Province

The PRC

\*\* *Independent non-executive Director*

22 May 2017

*To the Shareholders*

Dear Sir or Madam,

### **REVISION OF 2017 AND 2018 ANNUAL CAPS FOR CONTINUING CONNECTED TRANSACTIONS**

#### **INTRODUCTION**

References are made to (1) the circular of the Company dated 10 October 2015 in respect of, among other things, the continuing connected transactions under the CCT Agreements; and (2) the announcement of the Company dated 28 February 2017. The purpose of this circular is to provide you with further information relating to the CCT Agreements and the Proposed Revised Annual Caps therefor, to enable you to make an informed decision on whether to vote for or against or abstain from voting on the proposed resolutions in relation to the Proposed Revised Annual Caps at the AGM.



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## LETTER FROM THE BOARD

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On 25 August 2015, the Company entered into the CCT Agreements, namely the Material Procurement Agreement, the Sale of Goods Agreement and the Composite Services Agreement, with YTO. The CCT Agreements and the respective Existing Annual Caps were approved by the then Independent Shareholders at the extraordinary general meeting of the Company on 29 October 2015.

Due to operational needs, the Board expects that the Existing Annual Caps of the CCT Agreements will not be sufficient for the expected transaction amounts for the continuing connected transactions contemplated under the CCT Agreements for the years ending 31 December 2017 and 2018. The Board therefore proposes to revise the Existing Annual Caps of the CCT Agreements to the Proposed Revised Annual Caps.

### THE CCT AGREEMENTS

Set out below is a brief summary of the principal terms of each of the CCT Agreements and their corresponding Existing Annual Caps and Proposed Revised Annual Caps:

#### 1. The Material Procurement Agreement

|                             |   |   |
|-----------------------------|---|---|
| <b>Date</b>                 | : | 25 August 2015  |
| <b>Parties</b>              | : | (1) YTO, on behalf of YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach, as supplier and/or supplying agent; and<br><br>(2) The Company, on behalf of the Group, as purchaser and/or purchasing agent.  |
| <b>Goods to be provided</b> | : | Goods required for the production and operation of the Group, including but not limited to raw materials (including steel, pig iron, waste steel, coke, nonferrous metals and lubricating oil), other industrial equipment (including machine tools), components (including clamping apparatus and moulds) and spare parts (including oil injection pumps). |
| <b>Term</b>                 | : | From 1 January 2016 to 31 December 2018.  |

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## LETTER FROM THE BOARD

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**Payment terms** : Shall be principally settled within three months from the date of confirmation of receiving the goods by the purchaser. Subject to negotiations between the parties, prepayments by the purchaser of no more than six months from the estimated date of delivery of the goods are acceptable.

(N.B. These payment terms were usually adopted by the Company in its transactions with independent third parties or YTO. Such terms are on normal commercial terms and not less favourable than those offered to the Company by independent third parties.)

### ***Pricing Standards of the Transactions under the Material Procurement Agreement***

Under the Material Procurement Agreement, the price of the goods to be provided will be:

- (1) the market price of an independent third party obtained through prices quoted on websites for the industry or enquiries in the market (i.e. the price of the same or similar product provided to independent third parties by suppliers other than YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach in the same region during the ordinary course of business on normal commercial terms);
- (2) if there is no market price determined by an independent third party, the transaction price between YTO Group, associates of YTO, Sinomach or the subsidiaries of Sinomach and an independent third party; and
- (3) if none of the above is applicable, costs plus a percentage mark-up (tax-inclusive), which is not more than 30% (i.e. price = cost x (1 + percentage mark-up)), whereas the 30% mark-up is determined based on (i) the average gross profit margin of listed companies engaged in manufacturing of special purpose equipment (this industry classification is according to the “Guidelines for the Industry Classification of Listed Companies (上市公司行業分類指引)” (Revised in 2012) and the industry classification results of listed companies issued by the China Securities Regulatory Commission, and the Company is within this classification) for the three years ended 31 December 2015 and the six months ended 30 June 2016; and (ii) the gross profit margin of the historical transactions of procurement of the same or similar products by the Group from YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach.

YTO undertakes that the applicable price of the goods offered to the Group shall not be less favourable than that offered to independent third party customers of YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach for the same goods.

## LETTER FROM THE BOARD

When adopting the above pricing standards, the Company's:

1. procurement department, in relation to pricing standard (1), shall check one to two price(s) of the same or similar goods (including bulk stock such as steel, nonferrous metals and lubricating oil) quoted on the websites for the industry or in the market for the business department's inquiries and applications. However, the goods with such quoted prices are generally different from the actual goods to be procured by the Company in terms of their quality, specifications and models, and the transaction terms including transportation costs and settlement method may also be different. Therefore, pricing standard (1) is generally not directly applicable and the Company will only use the quoted prices as material pricing references;
2. finance department, in relation to pricing standard (2), shall obtain one to two agreement(s) of YTO providing the same goods to its independent third parties, to ensure that the price of the same goods offered by YTO to the Company shall not be higher than that offered to independent third parties. Meanwhile, finance department shall request YTO to provide cost analysis of goods (including cost breakdown and gross profit margin) to ensure that the prices are fair and reasonable; and
3. finance department, in relation to pricing standard (3), shall obtain cost analysis of goods from YTO and finalise the final price in accordance with the cost analysis and the percentage mark-up which is not more than 30%. The finance department shall also perform quarterly update and review on the average gross profit margin of listed companies engaged in manufacturing of special purpose equipment and the gross profit margin of the historical transactions. The finance department and the office of the Board shall ensure that the percentage mark-up of not more than 30% is fair and reasonable. The Company will not adopt pricing standard (3) and may negotiate with YTO to revise the pricing standards by entering into supplemental agreement in compliance with the requirements of the Listing Rules should it consider such percentage mark-up is no longer fair and reasonable.

### ***Historical Figures, the Existing Annual Caps and the Proposed Revised Annual Caps for the Transactions under the Material Procurement Agreement***

The Company has entered into (i) a material procurement agreement dated 29 October 2012 (details of which were set out in the Company's circular dated 28 November 2012) (the "**2012 Material Procurement Agreement**") and (ii) the Material Procurement Agreement for material procurement in the past. In respect of the 2012 Material Procurement Agreement, the following table sets out the historical transaction amounts for the years ended 31 December 2014 and 2015. The table also sets out the historical transaction amount and the existing Annual Cap for the year ended 31 December 2016, and the existing Annual Caps and the proposed revised Annual Caps for the years ending 31 December 2017 and 2018 under the Material Procurement Agreement:

*(Unit: RMB0'000)*

|                                | Historical transaction amounts<br>for the year ended 31 December |                                |                                | Existing Annual Caps<br>for the year ended/ending 31 December |        |        | Proposed revised<br>Annual Caps for the year<br>ending 31 December |         |
|--------------------------------|--|--------------------------------|--------------------------------|---|--------|--------|--|---------|
|                                | 2014<br><i>(Approximately)</i>                                   | 2015<br><i>(Approximately)</i> | 2016<br><i>(Approximately)</i> | 2016  | 2017   | 2018   | 2017   | 2018    |
| Material Procurement Agreement | 37,616   | 56,848                         | 49,877                         | 50,000  | 50,000 | 50,000 | 149,800  | 164,800 |

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## LETTER FROM THE BOARD

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The historical transaction amount for the year ended 31 December 2016 under the Material Procurement Agreement was approximately RMB498,770,000, representing approximately 99.75% of the existing Annual Cap for the year ended 31 December 2016 under the Material Procurement Agreement.

As at the Latest Practicable Date, the existing Annual Caps for the years ended 31 December 2016 and ending 31 December 2017 under the Material Procurement Agreement have not been exceeded.

The Material Procurement Agreement Proposed Revised Annual Caps for the years ending 31 December 2017 and 2018 are RMB1,498,000,000 and RMB1,648,000,000 respectively, which represents an increase of RMB998,000,000 (199.6%) and RMB1,148,000,000 (229.6%) from the Material Procurement Agreement Existing Annual Caps for the years ending 31 December 2017 and 2018 respectively.

### ***Basis for Revision of the Annual Caps under the Material Procurement Agreement***

Taking into account the following factors, the Board expects that the Material Procurement Agreement Existing Annual Caps will not be sufficient, and proposes to revise to the Material Procurement Agreement Proposed Revised Annual Caps:

- (1) the abovementioned approximately 99.75% utilisation rate of the existing Annual Cap for the year ended 31 December 2016 under the Material Procurement Agreement; and
- (2) the Material Procurement Agreement Proposed Revised Annual Caps were determined based on the amounts of the Material Procurement Agreement Existing Annual Caps and the estimated increment (the “**Material Procurement Agreement Annual Caps Increment**”) in transaction amounts contemplated under the Material Procurement Agreement for the years ending 31 December 2017 and 2018, which is attributable to the facts that:
  - (a) In August 2016, YTO increased its shareholding in Luoyang Zhongshou Machinery Equipment Company Limited\* (洛陽中收機械裝備有限公司) (“**Luoyang Zhongshou**”). YTO became the controlling shareholder of Luoyang Zhongshou and Luoyang Zhongshou became the subsidiary of YTO after such increase. Luoyang Zhongshou is principally engaged in research and development, production and sales of wheat, corn and other harvesting machinery products. YTO Group also has the capability for production of certain agricultural machineries.

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## LETTER FROM THE BOARD

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In order to implement the operational idea of the Company of providing customers with the most valuable agricultural equipment whole-set solutions, the Company intends to purchase products including harvesting machinery and agricultural machinery from YTO Group and utilise advantages of the Company for the purpose of providing customers with unit sales and whole-set solutions for agricultural machinery products to meet the needs of the customers for full-process mechanisation in operation. The Company expects to purchase approximately 11,500 units of agricultural machinery and approximately 6,000 units of harvesting machinery from YTO Group in 2017 for the aggregate estimated transaction amounts of approximately RMB742,000,000 for the year ending 31 December 2017, accounting for approximately 74.35% of the Material Procurement Agreement Annual Caps Increment for the year ending 31 December 2017.

- (b) In 2016, the Company completed the transformation of tractor and diesel engine to national III emission standard. Due to the expected increase in the estimated 2017 annual sales volume for diesel engine of the Company by approximately 10% from that in 2016, it is expected that the purchase volume of the Company and its subsidiary, YTO (Luoyang) Diesel Engine Company Limited\* (一拖(洛陽)柴油機有限公司) (“**YTO Diesel Engine Company**”), for products used for production of diesel engine, including (i) the exhaust gas recirculation valve (the “**EGR valve**”) manufactured by Luoyang Tractor Research Company Limited\* (洛陽拖拉機研究所有限公司) (a subsidiary of the Company, and also an associate of YTO due to the fact that YTO holds 49% of its equity interest) (“**Tractor Research Company**”); and (ii) products including electronic control pump and camshaft manufactured by YTO (Luoyang) Fuel Injection Pump Company Limited\* (一拖(洛陽)燃油噴射有限公司) (“**YTO Fuel Injection Pump Company**”) (a subsidiary of the Company, and also an associate of YTO due to the fact that YTO holds 10.57% of its equity interest), will increase to a certain extent. The Company expects that the aggregate estimated increase in transaction amounts for products including the EGR valve, electronic control pump and camshaft, to be purchased by the Company and YTO Diesel Engine Company from Tractor Research Company and YTO Fuel Injection Pump Company will be approximately RMB256,000,000, accounting for approximately 25.65% of the Material Procurement Agreement Annual Caps Increment for the year ending 31 December 2017.
- (c) According to the expected needs in the market of harvesting machinery in 2018 and the plan of the Company, it is expected that the Material Procurement Agreement Proposed Revised Annual Cap for the year ending 31 December 2018 will approximately be 10% higher than that for the year ending 31 December 2017.

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## LETTER FROM THE BOARD

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### 2. The Sale of Goods Agreement

- Date** : 25 August 2015
- Parties** : (1) The Company, on behalf of the Group, as supplier and/or supplying agent; and
- (2) YTO, on behalf of YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach, as purchaser and/or purchasing agent.
- Goods to be provided** : Products to be used in the production and in the ordinary course of business of the purchaser, including but not limited to raw materials, spare parts (including casting parts), components (including semi-finished parts and finished parts) and equipment (including diesel engines and tractors).
- Term** : From 1 January 2016 to 31 December 2018.
- Payment terms** : Shall be principally settled within three months after the date of delivery of goods by the supplier. Subject to negotiations between the parties, prepayments by the purchaser of no more than six months from the estimated date of delivery of the goods are acceptable.
- (N.B. These payment terms were usually adopted by the Company in its transactions with independent third parties or YTO. Such terms are on normal commercial terms and not more favourable than those offered by the Company to independent third parties.)
- Undertaking** : Provided that the Group manufactures such goods, the Group undertakes to give priority to YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach for supply of such goods over other third parties' under the same condition.

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## LETTER FROM THE BOARD

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### *Pricing Standards of the Transactions under the Sale of Goods Agreement*

Under the Sale of Goods Agreement, the applicable price of the goods to be supplied or provided will be:

- (1) the market price of an independent third party obtained through prices quoted on websites for the industry or enquiries in the market (i.e. the price of the same or similar product provided to independent third parties by suppliers other than the Group in the same region during the ordinary course of business on normal commercial terms);
- (2) if there is no market price determined by an independent third party, the transaction price between the Group and an independent third party; and
- (3) if none of the above is applicable, costs plus a percentage mark-up (tax-inclusive), which is not more than 30% (i.e. price = cost x (1 + percentage mark-up)), whereas the 30% mark-up is determined based on (i) the average gross profit margin of listed companies engaged in manufacturing of special purpose equipment (this industry classification is according to the “Guidelines for the Industry Classification of Listed Companies (上市公司行業分類指引)” (Revised in 2012) and the industry classification results of listed companies issued by the China Securities Regulatory Commission, and the Company is within this classification) for the three years ended 31 December 2015 and the six months ended 30 June 2016; and (ii) the gross profit margin of the historical transactions of sales of the same or similar products to the Group by YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach.

In any event, the applicable price of the goods offered to YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach by the Group shall not be more favourable than that offered to independent third party customers of the Group.

When adopting the above pricing standards, the Company’s:

1. sales department, in relation to pricing standard (1), shall obtain prices of the same or similar products in the open market from independent third parties in the ordinary course of business. However, the products with such quoted prices are generally different from the actual products to be sold by the Company in terms of their quality, specifications and models, and the transaction terms including transportation costs and settlement method may also be different. Therefore, pricing standard (1) is generally not directly applicable; and

## LETTER FROM THE BOARD

2. in relation to other pricing standards, finance department shall formulate unified sales prices (the “**Unified Sales Prices**”) of general generic products of the Company according to the Company’s cost and gross profit margin, which will be adopted uniformly in transactions of the Company with the purchaser or with an independent third party. If the purchaser or an independent third party has specific request in relation to technical process and assembly of spare parts, etc. of products of the Company, the Unified Sales Prices will no longer be applicable and the Company will adopt pricing standard (3). But in any event, finance department and sales department are responsible for ensuring that the price of the same products offered by the Company to the purchaser shall not be lower than that offered to independent third parties. The finance department shall also perform quarterly update and review on the average gross profit margin of listed companies engaged in manufacturing of special purpose equipment and the gross profit margin of the historical transactions. The finance department and the office of the Board shall ensure that the percentage mark-up of not more than 30% is fair and reasonable. The Company will not adopt pricing standard (3) and may negotiate with the purchaser to revise the pricing standards by entering into supplemental agreement in compliance with the requirements of the Listing Rules should it consider such percentage mark-up is no longer fair and reasonable.

### ***Historical Figures, the Existing Annual Caps and the Proposed Revised Annual Caps for the Transactions under the Sale of Goods Agreement***

The Company has entered into (i) a sale of goods agreement dated 29 October 2012 (details of which were set out in the Company’s circular dated 28 November 2012) (the “**2012 Sale of Goods Agreement**”) and (ii) the Sale of Goods Agreement for goods sold in the past. In respect of the 2012 Sale of Goods Agreement, the following table sets out the historical transaction amounts for the years ended 31 December 2014 and 2015. The table also sets out the historical transaction amount and the existing Annual Cap for the year ended 31 December 2016, and the existing Annual Caps and the proposed revised Annual Caps for the years ending 31 December 2017 and 2018 under the Sale of Goods Agreement:

*(Unit: RMB0’000)*

|                         | Historical transaction amounts<br>for the year ended 31 December |                        |                        | Existing Annual Caps<br>for the year ended/ending 31 December |        |        | Proposed revised<br>Annual Caps for the year<br>ending 31 December |        |
|-------------------------|--|------------------------|------------------------|---|--------|--------|--|--------|
|                         | 2014   | 2015                   | 2016                   | 2016  | 2017   | 2018   | 2017   | 2018   |
|                         | <i>(Approximately)</i>   | <i>(Approximately)</i> | <i>(Approximately)</i> |   |        |        |  |        |
| Sale of Goods Agreement | 11,345   | 22,420                 | 34,355                 | 35,000  | 20,000 | 21,000 | 46,000   | 48,800 |



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## LETTER FROM THE BOARD

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The historical transaction amount for the year ended 31 December 2016 under the Sale of Goods Agreement was approximately RMB343,550,000, representing approximately 98.16% of the existing Annual Cap for the year ended 31 December 2016 under the Sale of Goods Agreement.

As at the Latest Practicable Date, the existing Annual Caps for the years ended 31 December 2016 and ending 31 December 2017 under the Sale of Goods Agreement have not been exceeded.

The Sale of Goods Agreement Proposed Revised Annual Caps for the years ending 31 December 2017 and 2018 are RMB460,000,000 and RMB488,000,000 respectively, which represents an increase of RMB260,000,000 (130%) and RMB278,000,000 (approximately 132.38%) from the Sale of Goods Agreement Existing Annual Caps for the years ending 31 December 2017 and 2018 respectively.

### *Basis for Revision of the Annual Caps under the Sale of Goods Agreement*

Taking into account the following factors, the Board expects that the Sale of Goods Agreement Existing Annual Caps will not be sufficient, and proposes to revise to the Sale of Goods Agreement Proposed Revised Annual Caps:

- (1) the abovementioned approximately 98.16% utilisation rate of the existing Annual Cap for the year ended 31 December 2016 under the Sale of Goods Agreement; and
- (2) the Sale of Goods Agreement Proposed Revised Annual Caps were determined based on the amounts of the Sale of Goods Agreement Existing Annual Caps and the estimated increment (the “**Sale of Goods Agreement Annual Caps Increment**”) in transaction amounts contemplated under the Sale of Goods Agreement for the years ending 31 December 2017 and 2018, which is attributable to the facts that:
  - (a) According to the production needs of YTO Group in harvesting machinery products and in order to utilise the Company’s core manufacturing capabilities in components including diesel engine, the Company and its subsidiary, YTO Diesel Engine Company, sold and will sell products including diesel engines and spare parts to Luoyang Zhongshou. It is expected that the Company will sell approximately 6,000 units of diesel engines to YTO Group in 2017 and the estimated increase in transaction amounts for sales of raw materials, diesel engines and spare parts to YTO Group for their production of harvesting machinery for the year ending 31 December 2017 will be approximately RMB260,000,000, accounting for 100% of the Sale of Goods Agreement Annual Caps Increment for the year ending 31 December 2017.
  - (b) According to the business plan for harvesting machinery products of Luoyang Zhongshou in 2018, it is expected that the transaction amount for the connected transactions of the sale of goods from the Company to Luoyang Zhongshou in 2018 will increase by approximately 6% from that of 2017.

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## LETTER FROM THE BOARD

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### 3. The Composite Services Agreement

**Date** : 25 August 2015

**Parties** : (1) YTO, on behalf of YTO, its controlled companies and their associates, as supplier and/or supplying agent; and  
(2) The Company, on behalf of the Group, as purchaser and/or purchasing agent.

**Services to be provided** : Storage services and transportation services.

**Term** : From 1 January 2016 to 31 December 2018.

**Payment terms** : Storage services: shall be billed quarterly and paid in the following month.

Transportation services: shall be principally settled within three months after confirmation by the Company (on behalf of the Group) from the date of delivering or receiving the goods.

(N.B. These payment terms were usually adopted by YTO in its transactions with independent third parties or the Company. Such terms are on normal commercial terms and not less favourable than those offered to independent third parties by YTO.)

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## LETTER FROM THE BOARD

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### *Pricing Standards of the Transactions under the Composite Services Agreement*

Under the Composite Services Agreement, the price of the services to be provided thereunder will be:

- (1) the market price of an independent third party obtained through prices quoted on websites for the industry or enquiries in the market (i.e. the price of the same or similar services provided to independent third parties by suppliers other than YTO, its controlled companies and their associates in the same region during the ordinary course of business on normal commercial terms);
- (2) if there is no market price determined by an independent third party, the transaction price between YTO, its controlled companies and their associates and an independent third party; and
- (3) if none of the above is applicable, costs plus a percentage mark-up (tax-inclusive), which is not more than 30% (i.e. price = cost x (1 + percentage mark-up)), whereas the 30% mark-up is determined based on (i) the average gross profit margin of listed companies engaged in storage services and road transportation services (the industry classification is according to the “Guidelines for the Industry Classification of Listed Companies (上市公司行業分類指引)” (Revised in 2012) and the industry classification results of listed companies issued by the China Securities Regulatory Commission) for the three years ended 31 December 2015 and the six months ended 30 June 2016; and (ii) the gross profit margin of the historical transactions of provision of the same or similar service to the Group by YTO, its controlled companies and their associates.

YTO undertakes that the applicable price of the services offered to the Group shall not be less favourable than that offered to independent third party customers of YTO, its controlled companies and their associates for the same services.

When adopting the above pricing standards, the Company’s:

1. operation department, in relation to pricing standard (1), shall check prices of the same or similar services quoted on the websites for the industry every month;
2. finance department, in relation to pricing standard (2), shall obtain cost analysis of services from YTO (including cost breakdown and gross profit margin) supported by one to two agreement(s) of YTO providing the same services to its independent third parties, to ensure that the price of the same services offered by YTO to the Company shall not be higher than that offered to independent third parties; and

## LETTER FROM THE BOARD

3. finance department, in relation to pricing standard (3), shall obtain cost analysis of services from YTO and finalise the final price in accordance with the cost analysis and the percentage mark-up which is not more than 30%. The finance department shall also perform quarterly update and review on the average gross profit margin of listed companies engaged in storage services and road transportation services and the gross profit margin of the historical transactions. The finance department and the office of the Board shall ensure that the percentage mark-up of not more than 30% is fair and reasonable. The Company will not adopt pricing standard (3) and may negotiate with YTO to revise the pricing standards by entering into supplemental agreement in compliance with the requirements of the Listing Rules should it consider such percentage mark-up is no longer fair and reasonable.

### *Historical Figures, the Existing Annual Caps and the Proposed Revised Annual Caps for the Transactions under the Composite Services Agreement*

The Company has entered into (i) a composite services agreement dated 29 October 2012 (details of which were set out in the Company’s circular dated 28 November 2012) (the “**2012 Composite Services Agreement**”) and (ii) the Composite Services Agreement in respect of provision of composite services in the past. In respect of the 2012 Composite Services Agreement, the following table sets out the historical transaction amounts for the years ended 31 December 2014 and 2015. The table also sets out the historical transaction amount and the existing Annual Cap for the year ended 31 December 2016, and the existing Annual Caps and the proposed revised Annual Caps for the years ending 31 December 2017 and 2018 under the Composite Services Agreement:

*(Unit: RMB0’000)*

|                                 | Historical transaction amounts<br>for the year ended 31 December |                        |                        | Existing Annual Caps<br>for the year ended/ending 31 December |        |        | Proposed revised<br>Annual Caps for the year<br>ending 31 December |        |
|---------------------------------|--|------------------------|------------------------|---|--------|--------|--|--------|
|                                 | 2014   | 2015                   | 2016                   | 2016  | 2017   | 2018   | 2017   | 2018   |
|                                 | <i>(Approximately)</i>   | <i>(Approximately)</i> | <i>(Approximately)</i> |   |        |        |  |        |
| Composite Services<br>Agreement | 22,888   | 22,429                 | 14,717                 | 14,720  | 15,720 | 16,720 | 21,500   | 22,500 |

The historical transaction amount for the year ended 31 December 2016 under the Composite Services Agreement was approximately RMB147,170,000, representing approximately 99.98% of the existing Annual Cap for the year ended 31 December 2016 under the Composite Services Agreement.

As at the Latest Practicable Date, the existing Annual Caps for the years ended 31 December 2016 and ending 31 December 2017 under the Composite Services Agreement have not been exceeded.

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## LETTER FROM THE BOARD

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The Composite Services Agreement Proposed Revised Annual Caps for the years ending 31 December 2017 and 2018 are RMB215,000,000 and RMB225,000,000 respectively, which represents an increase of RMB57,800,000 (approximately 36.77%) and RMB57,800,000 (approximately 34.57%) from the Composite Services Agreement Existing Annual Caps for the years ending 31 December 2017 and 2018 respectively.

### *Basis for Revision of the Annual Caps under the Composite Services Agreement*

Taking into account the following factors, the Board expects that the Composite Services Agreement Existing Annual Caps will not be sufficient, and proposes to revise to the Composite Services Agreement Proposed Revised Annual Caps:

- (1) the abovementioned approximately 99.98% utilisation rate of the existing Annual Cap for the year ended 31 December 2016 under the Composite Services Agreement; and
- (2) the Composite Services Agreement Proposed Revised Annual Caps were determined based on the amounts of the Composite Services Agreement Existing Annual Caps and the estimated increment in transaction amounts contemplated under the Composite Services Agreement for the years ending 31 December 2017 and 2018, which is attributable to the facts that:
  - (a) The Company expects that the Composite Services Agreement Proposed Revised Annual Cap for the year ending 31 December 2017 will increase by 46% from the existing Annual Cap for the year ended 31 December 2016 under the Composite Services Agreement for the reasons that:
    - a. Products of the Company are mainly transported on highway. Under the Composite Services Agreement, YTO shall provide transportation services for the Company's products. In September 2016, the "Administrative Rules on Highway Driving of Overloading Vehicle (超限運輸車輛行駛公路管理規定)" was implemented in the PRC, leading to an increase in the transportation cost for transporting the Company's products.
    - b. in order to make use of the advantages of YTO Group in logistics and transportation, harvesting machinery products sold by the Company in 2017 will be transported by YTO Group. It is expected that the transportation cost of the Company for the year ending 31 December 2017 will increase.
  - (b) The Company expects that the sales volume of harvesting machinery in 2018 will increase. As such, the Composite Services Agreement Proposed Revised Annual Cap for the year ending 31 December 2018 is expected to increase by approximately 5% from the Composite Services Agreement Proposed Revised Annual Cap for the year ending 31 December 2017.

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## LETTER FROM THE BOARD

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### MEASURES OF INTERNAL CONTROL

To ensure the Group's conformity with the pricing policies of the CCT Agreements from time to time, the Group adopts a series of internal control policies for its daily operation. Such internal control policies are conducted and supervised by the finance department, the office of the Board and the independent non-executive Directors:

- (1) the Board, the audit committee of the Board and the independent non-executive Directors have approved the CCT Agreements according to the connected transaction decision policy;
- (2) the Company's management policies for connected transactions clearly stated the principle for determining the prices for connected transactions. When each unit of business enters into contracts in accordance with the framework agreements of the continuing connected transactions, the price must be determined in accordance with the pricing standards as agreed in the CCT Agreements;
- (3) the agreement for procurement together with the negotiation memo (containing types and specifications of products, record of negotiation target, request and undertaking, results of the negotiation and other details) between the specific trained procurement executives of the Company and the suppliers are first delivered to the head of operation department for review and approval. The operation department and the technical department are responsible for assessing the suppliers' products qualities, production capacities, performance capacities and other capacities, based on factors including quality and system certification, characteristics of the main technology and process, annual sales results and main production equipment. Upon obtaining the approval of the head of the operation department, as the products procured by the Company are generally supplied by YTO Group and several independent third parties, the finance department would review and compare the prices and terms of the procurement agreements providing the same product to the Company among two to three suppliers including YTO Group and independent third parties, and would adopt the lowest price under the same terms and conditions, subject to the type, quality and technical requirements of the products to be procured under the Material Procurement Agreement. The finance department would make sure the prices and terms offered by YTO Group are fair and reasonable that they are no less favourable than those offered by independent suppliers. For those products to be procured under the Material Procurement Agreement that there is no independent suppliers, the finance department would request YTO Group to provide the cost breakdown (containing raw materials and manufacturing costs, period costs, gross profit margin and other details) and analysis. The finance department would then evaluate reasonableness of the price charged based on the general gross profit margin in the machinery manufacturing industry. The agreement would then be reviewed and approved by the legal department to ensure legality. The agreement can be executed upon obtaining the approvals from all of the abovementioned departments of the Company;

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## LETTER FROM THE BOARD

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- (4) the agreement for sales together with the negotiation memo between the relevant staff of the sales department of the Company and the purchasers are first delivered to the head of operation department for review and approval. The operation department and the technical department are responsible for assessing the production capacities of the Company based on factors including product specifications, order size and delivery terms and assessing the credibility of the purchasers based on factors including the purchaser's business license, assets, legal representative and previous cooperation with the Company. Upon obtaining the approval of the head of the operation department, the finance department, in relation to the general generic products, would review whether the prices are consistent with the Unified Sales Prices; and the finance department and the sales department, in relation to the specific products, would analyse the cost breakdown of the products and formulate the prices according to the specific request on product technology, technical process and quality, and based on reasonable gross profit margin. The finance department would make sure the prices and terms offered to YTO Group are fair and reasonable that they are no more favourable than those offered to independent third parties. The agreement would then be reviewed and approved by the legal department to ensure legality. The agreement can be executed upon obtaining the approvals from all of the abovementioned departments of the Company; and
- (5) the agreement for the composite services (including storage services and transportation services) together with the negotiation memo between the relevant staff of the operation department of the Company and the counterparties in the transactions are first delivered to the head of operation department for review and approval. The operation department is responsible for assessing transportation abilities or service abilities of the counterparties, etc., based on factors including vehicle loading capacity, organisation and delivery capacity, lifting equipment capacity, delivery qualification rate and on-schedule delivery rate. Upon obtaining the approval of the head of the operation department, the finance department would review and compare the prices and terms of the agreements providing the same service to the Company among two to three counterparties including YTO Group and independent third parties and would adopt the lowest price under the same terms and conditions. The finance department would ensure the prices and terms offered by YTO Group are fair and reasonable that they are no less favourable than those offered by the independent third parties. If there is no market price, the finance department would request YTO Group to provide the cost breakdown (containing fuel costs, toll, labour costs tax and other expenses) and analysis. The finance department would then evaluate reasonableness of the price charged based on the general gross profit margin in the storage and transportation industries. The agreement would then be reviewed and approved by the legal department to ensure legality. The agreement can be executed upon obtaining the approvals from all of the abovementioned departments of the Company.

The Directors are of the view that the above internal control measures can ensure that the transactions under the CCT Agreements are conducted on normal commercial terms and will not be prejudicial to the interests of the Company and the Shareholders.

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## LETTER FROM THE BOARD

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### REASONS AND BENEFITS OF THE CONTINUING CONNECTED TRANSACTIONS UNDER THE CCT AGREEMENTS

The Group and YTO Group have been carrying out transactions with each other to facilitate their productions and operations since 1997. In view of the long-established relationship between the Group and YTO Group, the geographical convenience between the Group and YTO Group (both located in Jianshe Road in Luoyang) provides a reliable supply of raw material and spare parts and provision of services, which are favourable to (i) the Company's effective control over the product performance and quality; and (ii) the after-sales services as it offers fast, convenient and timely communication and coordination between the transaction parties. The entering into of the CCT Agreements can effectively lower the operation risk of both the Group and YTO Group, and is favourable to the Company's daily operation and management of production. The proposed increase in the Annual Caps of the CCT Agreements would satisfy the daily operational needs of the Company and enhance economies of scale of the Company, which is beneficial to the continuing operation of the Company. It is expected that there is no disadvantage to the Group in relation to the proposed revision of the Annual Caps of the CCT Agreements.

The Directors consider that the terms of the CCT Agreements and the Proposed Revised Annual Caps are on normal commercial terms, in the ordinary and usual course of business of the Group, fair and reasonable and in the interests of the Company and the Shareholders as a whole.

### INFORMATION OF THE GROUP, YTO, YTO GROUP AND SINOMACH

The Group is principally engaged in the production and sales of agricultural machineries and power machineries. The principal products include tractors of hi-powered, mid-powered and low-powered, diesel engines and other accessories of tractors, forklift and mining trucks, etc.

As at the Latest Practicable Date, YTO is the immediate controlling shareholder of the Company, holding 410,690,578 A Shares of the Company. YTO Group is principally engaged in the production and sales of transporting machineries, vehicle products, industrial equipments and components.

Sinomach is principally engaged in the business of research and development and manufacturing of machinery equipment, contracting of machineries and engineering projects domestically and internationally, sales of automotive and parts, contracting of international projects and tendering of domestic and international projects, and import and export business.



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## LETTER FROM THE BOARD

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### LISTING RULES IMPLICATIONS

YTO beneficially owns approximately 41.24% equity interest in the Company and is the immediate controlling shareholder of the Company, and therefore is a connected person of the Company under the Listing Rules. Accordingly, the transactions contemplated under the CCT Agreements constitute continuing connected transactions of the Company under Chapter 14A of the Listing Rules.

Pursuant to Rule 14A.54 of the Listing Rules, the Company is required to re-comply with the announcement and Independent Shareholders' approval requirements in respect of the respective Proposed Revised Annual Caps under the CCT Agreements. As the applicable percentage ratios under each of the CCT Agreements are more than 5%, the transactions contemplated under each of the CCT Agreements are subject to the reporting, announcement and Independent Shareholders' approval requirements under Chapter 14A of the Listing Rules. The Company proposes to seek the Independent Shareholders' approval for the Proposed Revised Annual Caps under each of the CCT Agreements at the AGM.

Zhao Yanshui, Wang Erlong, Li Hepeng, Xie Donggang, Li Kai and Yin Dongfang, the Directors of the Company, have abstained from voting to approve the Proposed Revised Annual Caps in the Board meeting due to the fact that they are also directors of YTO and are regarded not independent to make any recommendation to the Board.

### AGM

The AGM will be held at 2:15 p.m. on 13 June 2017 (Tuesday) at No. 154 Jianshe Road, Luoyang, Henan Province, the PRC, at which ordinary resolution(s) will be proposed to, among other things, seek the Independent Shareholders' approval for the Proposed Revised Annual Caps. YTO and its associates, holding approximately 41.24% of the total issued share capital of the Company, will abstain from voting on the ordinary resolution(s) in respect of the Proposed Revised Annual Caps at the AGM. At the AGM, votes will be taken by poll.

The notice of the AGM is set out on pages 60 to 65 of this circular. A form of proxy for use at the AGM was despatched and also published on the website of The Stock Exchange of Hong Kong Limited (<http://www.hkexnews.hk>) on 26 April 2017. Whether or not you are able to attend the meeting in person, you are requested to complete and return the form of proxy in accordance with the instructions printed thereon. The proxy form shall be lodged with the Company's branch share registrar in Hong Kong, Hong Kong Registrars Limited, at Shops 1712–1716, 17/F., Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, or at the registered address and principal place of business of the Company at No. 154 Jianshe Road, Luoyang, Henan Province, the PRC, as soon as possible and in any event not less than 24 hours before the time scheduled for holding the AGM (or any adjourned meeting thereof). Completion and delivery of the form of proxy will not preclude you from attending and voting in person at the AGM or any adjournment if you so desire.

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## LETTER FROM THE BOARD

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### RECOMMENDATION

The Directors are of the view that the terms of the CCT Agreements and the Proposed Revised Annual Caps are fair and reasonable, on normal commercial terms, in the ordinary and usual course of business of the Group and in the interests of the Company and the Shareholders as a whole. Accordingly, the Board recommends the Independent Shareholders to vote in favour of the ordinary resolution(s) with respect to the Proposed Revised Annual Caps to be proposed at the AGM.

The Independent Board Committee, having taken into account the advice of the Independent Financial Adviser, is of the opinion that the terms of the CCT Agreements and the Proposed Revised Annual Caps are fair and reasonable, on normal commercial terms, in the ordinary and usual course of business of the Group and in the interests of the Company and the Shareholders as a whole. Therefore, the Independent Board Committee recommends the Independent Shareholders to vote in favour of the ordinary resolution(s) as set out in the notice of the AGM to approve the Proposed Revised Annual Caps.

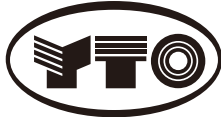
Your attention is drawn to the letter from the Independent Board Committee as set out on pages 20 to 21 of this circular which contains its recommendation to the Independent Shareholders in relation to the Proposed Revised Annual Caps. Your attention is also drawn to the letter of advice from the Independent Financial Adviser as set out on pages 22 to 55 of this circular which contains its advice to the Independent Board Committee and the Independent Shareholders in relation to the Proposed Revised Annual Caps. You are advised to read the said letters from the Independent Board Committee and Independent Financial Adviser before deciding how to vote at the AGM.

### ADDITIONAL INFORMATION

Your attention is drawn to the additional information as set out in the appendix to this circular and the notice of the AGM.

Yours faithfully,  
On behalf of the Board  
**First Tractor Company Limited\***  
**Zhao Yanshui**  
*Chairman*

\* *For identification purpose only*



**第一拖拉机股份有限公司**  
**FIRST TRACTOR COMPANY LIMITED\***

*(a joint stock company incorporated in The People's Republic of China with limited liability)*

(Stock Code: 0038)

22 May 2017

*To the Independent Shareholders*

Dear Sir or Madam,

**REVISION OF 2017 AND 2018 ANNUAL CAPS FOR  
CONTINUING CONNECTED TRANSACTIONS**

We refer to the circular dated 22 May 2017 issued by First Tractor Company Limited\* (the “**Circular**”), of which this letter forms part. Terms defined in the Circular shall have the same meanings herein unless the context otherwise requires.

We have been appointed as members of the Independent Board Committee to consider the Proposed Revised Annual Caps under each of the CCT Agreements, and to advise the Independent Shareholders as to whether, in our opinion, the Proposed Revised Annual Caps under each of the CCT Agreements are fair and reasonable, on normal commercial terms, in the ordinary and usual course of business of the Group and in the interests of the Company and the Shareholders as a whole. Veda Capital has been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in respect of the Proposed Revised Annual Caps under each of the CCT Agreements.

We wish to draw your attention to (i) the “Letter from the Board”; (ii) the “Letter from Veda Capital” to the Independent Board Committee and the Independent Shareholders which contains its advice in respect of the Proposed Revised Annual Caps under each of the CCT Agreements; and (iii) the additional information as set out in the appendix to the Circular.

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## LETTER FROM THE INDEPENDENT BOARD COMMITTEE

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Having considered the Proposed Revised Annual Caps under each of the CCT Agreements and having taken into account the opinion of Veda Capital and, in particular, the factors, reasons and recommendations as set out in the “Letter from Veda Capital” on pages 22 to 55 of the Circular, we consider that the Proposed Revised Annual Caps under each of the CCT Agreements are fair and reasonable, on normal commercial terms, in the ordinary and usual course of business of the Group and in the interests of the Company and the Shareholders as a whole. Accordingly, we recommend the Independent Shareholders to vote in favour of the ordinary resolution(s) which will be proposed at the AGM to approve the Proposed Revised Annual Caps.

Yours faithfully,

For and on behalf of

**Independent Board Committee**

**Ms. Yang Minli**

*Independent*

*non-executive Director*

**Mr. Xing Min**

*Independent*

*non-executive Director*

**Mr. Wu Tak Lung**

*Independent*

*non-executive Director*

**Mr. Yu Zengbiao**

*Independent*

*non-executive Director*

\* *For identification purpose only*

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## LETTER FROM VEDA CAPITAL

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*The following is the text of the letter of advice from Veda Capital, the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders in respect of the Proposed Revised Annual Caps, which has been prepared for the purpose of inclusion in this circular.*

**VEDA | CAPITAL**  
**智 略 資 本**

**Veda Capital Limited**  
Room 1106, 11/F  
Wing On Centre  
111 Connaught Road Central  
Hong Kong

22 May 2017

*To the Independent Board Committee and the Independent Shareholders*

Dear Sirs,

### **REVISION OF 2017 AND 2018 ANNUAL CAPS FOR CONTINUING CONNECTED TRANSACTIONS**

#### **INTRODUCTION**

We refer to our appointment to advise the Independent Board Committee and the Independent Shareholders in respect of the Proposed Revised Annual Caps for the CCT Agreements for the years ending 31 December 2017 and 2018, details of which are set out in the letter from the board (the “**Board Letter**”) contained in the circular to the Shareholders dated 22 May 2017 (the “**Circular**”), of which this letter forms part. Terms used herein have the same meanings as defined elsewhere in the Circular unless the context requires otherwise.

On 25 August 2015, the Company entered into the CCT Agreements, namely the Material Procurement Agreement, the Sale of Goods Agreement and the Composite Services Agreement, with YTO. The CCT Agreements and the respective Existing Annual Caps were approved by the then Independent Shareholders at the EGM of the Company on 29 October 2015.

According to the Board Letter, due to operational needs, the Board expects that the Existing Annual Caps of the CCT Agreements will not be sufficient for the expected transaction amounts for the continuing connected transactions contemplated under the CCT Agreements for the years ending 31 December 2017 and 2018. The Board therefore proposes to revise the Existing Annual Caps of the CCT Agreements to the Proposed Revised Annual Caps.

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## LETTER FROM VEDA CAPITAL

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As at the Latest Practicable Date, YTO beneficially owns approximately 41.24% equity interest in the Company and is the immediate controlling shareholder of the Company, and therefore is a connected person of the Company under the Listing Rules. Accordingly, the transactions contemplated under the CCT Agreements constitute continuing connected transactions of the Company under Chapter 14A of the Listing Rules.

The Independent Board Committee comprising all the independent non-executive Directors (namely Ms. Yang Minli, Mr. Xing Min, Mr. Wu Tak Lung and Mr. Yu Zengbiao) has been formed to consider the Proposed Revised Annual Caps amounts under the CCT agreements for the years ending 31 December 2017 and 2018 are on normal commercial terms, fair and reasonable and in the interests of the Company and the Shareholders as a whole. We, Veda Capital, have been appointed to advise the Independent Board Committee and the Independent Shareholders in these regards.

As at the Latest Practicable Date, we were not aware of any relationships or interest between Veda Capital and the Company or any other parties that could be reasonably be regarded as hindrance to Veda Capital's independence as defined under Rule 13.84 of the Listing Rules to act as the independent financial adviser to the Independent Board Committee and the Independent Shareholders in respect of the undertaking and the transactions contemplated thereunder. We are not associated with the Company, its subsidiaries, its associates or their respective substantial shareholders or associates, and accordingly, are eligible to give independent advice and recommendations on the terms of the undertaking and the transactions contemplated thereunder. In the last two years prior to the date of submission of our declaration relating to independence to the Stock Exchange, we have acted as an independent financial adviser to the Independent Board Committee and the Independent Shareholders in relation to one occasion as detailed in the circular of the Company dated 10 October 2015, which is related to continuing connected transactions. Given (i) our independent role in the above engagement; and (ii) our fees, which did not involve any contingent fee or conditional fee arrangement on the successful of the transactions, for the above engagement represented an insignificant percentage of our revenue, we consider the above engagement would not affect our independence to form our opinion in respect of the transactions contemplated under the Circular.

### **BASIS OF OUR OPINION**

In formulating our opinion and advice, we have relied upon accuracy of the information and representations contained in the Circular and information provided to us by the Company, the Directors and the management of the Company. We have assumed that all statements, information and representations made or referred to in the Circular and all information and representations which have been provided by the Company, the Directors and the management of the Company, for which they are solely and wholly responsible, were true at the time they were made and continue to be true as at the Latest Practicable Date. We have also assumed that all statements of belief, opinion and intention made by the Directors in the Circular were reasonably made after due and careful enquiry and were based on honestly-held opinions.

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## LETTER FROM VEDA CAPITAL

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The Directors have collectively and individually accepted full responsibility for the accuracy of the information contained in the Circular and have confirmed, having made all reasonable enquiries that, to the best of their knowledge and belief, there are no other facts the omission of which would make any statements in the Circular misleading. We have no reason to believe that any information and representations relied on by us in forming our opinion is untrue, inaccurate or misleading, nor are we aware of any material facts the omission of which would render the information provided and the representations made to us untrue, inaccurate or misleading. We have not, however, conducted any independent in-depth investigation into the business affairs, financial position or future prospects of the Group, nor have we carried out any independent verification of the information provided by the Directors and management of the Company.

### **PRINCIPAL FACTORS AND REASONS CONSIDERED**

In giving our recommendation to the Independent Board Committee and the Independent Shareholders in respect of the Proposed Revised Annual Caps, we have taken into consideration the following principal factors and reasons:

#### **1. Background of and reasons for revising the Annual Caps**

The Group is principally engaged in the production and sale of agricultural machinery and power machinery. The principal products include tractors of hi-powered, mid-powered and low-powered, diesel engine machinery and other accessories of tractors, forklifts and mining trucks etc.

Sinomach is a limited liability company incorporated in the PRC and a controlling shareholder of YTO having 87.90% shareholding interest in YTO. It is principally engaged in the business of research and development and manufacturing of machinery equipment, heavy machinery and engineering projects domestically and internationally, sales of automotive and parts, contracting of international projects and tendering of domestic and international projects, and import and export business. YTO Group is principally engaged in the production of transporting machinery, vehicles products, industrial equipment and components.

As noted from the Board Letter, the Group and YTO Group have been carrying out transactions with each other to facilitate their productions and operations since 1997. In view of the long-established relationship between the Group and YTO Group, the geographical convenience between the Group and YTO Group provides a reliable supply of raw material and spare parts and provision of services, which are favourable to (i) the Company's effective control over the product performance and quality; and (ii) the after-sales services as it offers fast, convenient and timely communication and coordination between the transaction parties. The entering into of the CCT Agreements can effectively lower the operation risk of both the Group and YTO Group, and is favourable to the Company's daily operation and management of production.

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## LETTER FROM VEDA CAPITAL

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As further noted from the Board Letter, the utilisation rate of the Existing Annual Cap for the year ended 31 December 2016 under the Material Procurement Agreement, the Sale of Good Agreement and the Composite Services Agreement are 99.75%, 98.16% and 99.98% respectively.

As noted from the website of YTO Group ([www.yto-en.com](http://www.yto-en.com)) (the “**YTO website**”), the line of products of YTO Group (other than the Group) consist of special vehicles, agricultural machinery and tools, tobacco machinery and intelligent equipment, etc. Also noted from YTO website, YTO Group has over sixty years of production experience and is committed to provide customers with high quality products. YTO Group implements a thorough quality control system which monitors each phase of manufacturing, from raw material selection, through production, to the delivery to its customers and it is one of their practices to purchase raw materials and spare parts in large quantities in order to purchase products at the most economical prices. The accessories sales network of YTO Group is well-developed and has numerous distributors. A subsidiary of YTO controls up to a number of branches across different channels of logistic services including automobiles and railway, warehouses for distribution and equipment for lifting services. Besides, the logistic network of YTO Group becomes well-developed and enjoys the advantages from economics of scales given its location in Jianxi, which is conveniently located in the center of the industrialised zone in Luoyang.

As advised by the Company, the major production capacity of the Group is allocated for the production of agricultural machinery (such as tractors) and power machinery (such as diesel engine machinery) and their important components. Therefore, it is more cost and time effective for the Group to mainly procure products including certain raw materials required for production from external vendors instead of producing them by the Company itself.

Having considered the wide sales network and the well-developed logistics and storage facilities of YTO Group, the Sale of Goods Agreement provides a channel for the Company to distribute the spare parts manufactured by the Company while the Composite Services Agreement allows the Company to enjoy the geographical advantages of YTO Group by saving the transportation costs.

Having considered (i) the principal business of the Company and YTO Group; (ii) the abovementioned benefits to the Company for entering the CCT Agreements; (iii) the long-established relationship between the Group and YTO; and (iv) the Existing Annual Caps under the CCT Agreements are almost fully utilised, the Proposed Revised Annual Caps provides the flexibility for the Company to continue the transactions under the CCT Agreements without adversely affecting the business operations of the Company and thus we are of the view that the Proposed Revised Annual Caps are in the interest of the Company and the Independent Shareholders as a whole.



### 2. Principal terms of the CCT Agreements

We have enquired with the management of the Company and are given to understand that save for the Proposed Revised Annual Caps, there is no change in the terms of the CCT Agreements including but not limited to the pricing standards. We are given to understand that all the factors contributing to the Proposed Revised Annual Caps are newly noticed by the Company after the Existing Annual Caps were approved by the Independent Shareholders on the EGM held on 29 October 2015. In order to assess the fairness and reasonableness of the Proposed Revised Annual Caps, we have performed the following analysis:

#### (A) *The Material Procurement Agreement*

Pursuant to the Material Procurement Agreement, YTO, on behalf of YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach will, as supplier and/or supplying agent, provide to the Group, products required in the production and operation of the Group (the “**Required Products**”), including but not limited to, raw materials (including steel, pig iron, waste steel, coke, nonferrous metals and lubricating oil), other industrial equipment (including machine tools), components (including clamping apparatus and moulds) and spare parts (including oil injection pumps). Given the principal business of the Group as mentioned above, major production capacity of the Group is allocated for the production of agricultural machinery and power machinery. Therefore, it is more cost and time effective for the Group to procure the Required Products instead of producing them by the Company itself.

As set out in the Board Letter, payment terms under the Material Procurement Agreement shall be principally settled within three months from the date of confirmation of receiving the goods by the purchaser. Subject to negotiations between the parties, prepayments by the purchaser of no more than six months from the estimated date of delivery of the goods are acceptable.

We have enquired with the management of the Company and are given to understand that the Group normally adopted the three months settlement payment term in its transactions with both independent third parties (within the meaning of the Listing Rules) (the “**Independent Third Parties**”) and YTO Group while we are advised that the Group has only entered into the transactions with the Independent Third Parties which adopted the prepayment term. As further noted from the management of the Company, such prepayment term is only acceptable and subject to the negotiations between the parties which will take into account of the factors, including but not limited to, the market condition, the demand and supply of the relevant goods in the market, the production capacities and the inventory. In these regards, we have obtained and reviewed ten randomly selected sample procurement contracts for each of the transactions entered into (i) between the Group and YTO Group; and (ii)

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between the Group and the Independent Third Parties (including the transactions with the prepayment term adopted), we observed that the above payment terms offered by YTO Group to the Group is not less favourable to the Group than that offered by the Independent Third Parties as the three months settlement payment term is available to the transactions entered into between the Group and YTO Group and between the Group and the Independent Third Parties, and the prepayment term can be adopted in the transactions entering with both YTO Group and the Independent Third Parties upon negotiations.

Therefore, we consider that the payment terms under the Material Procurement agreement are on normal commercial terms and not less favourable to the Group than those offered to the Group by the Independent Third Parties

### *Pricing standards of the transactions under the Material Procurement Agreement*

The price of goods to be supplied or provided will be determined based on the following price basis:

- (1) the market price of an independent third party obtained through prices quoted on websites for the industry or enquiries in the market (i.e. the price of the same or similar product provided to the Independent Third Parties by suppliers other than YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach in the same region during the ordinary course of business on normal commercial terms);
- (2) if there is no market price determined by an independent third party, the transaction price between YTO Group, associates of YTO, Sinomach or the subsidiaries of Sinomach and an independent third party; and
- (3) if none of the above is applicable, costs plus a percentage mark-up (tax-inclusive), which is not more than 30% (i.e. price = cost x (1 + percentage mark-up)), whereas the 30% markup is determined based on (i) the average gross profit margin of listed companies engaged in manufacturing of special purpose equipment (this industry classification is according to the “Guidelines for the Industry Classification of Listed Companies (上市公司行業分類指引)” (Revised in 2012) and the industry classification results of listed companies issued by the China Securities Regulatory Commission (“CSRC”), and the Company is within this classification) for the three years ended 31 December 2015 and the six months ended 30 June 2016; and (ii) the gross profit margin of the historical transactions of procurement of the same or similar products by the Group from YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach.

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YTO undertakes that the applicable price of the goods offered to the Group shall not be less favourable than that offered to independent third party customers of YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach for the same goods.

We are given to understand that the procurement department of the Company will check one to two price(s) of same or similar goods (including bulk stock such as steel, nonferrous metals and lubricating oil) quoted on the websites for the industry or market (such as China Commodity Marketplace ([www.chinaccm.com](http://www.chinaccm.com)), 中國聯合鋼鐵網 ([www.custeel.com](http://www.custeel.com)), and 卓創資訊網 ([www.sci99.com](http://www.sci99.com)), etc.) for the business department's inquiry and application. We have discussed with the management of the Company and reviewed the prices quoted on the websites for the industry and market, and noted that there is no direct relationship between the quoted price and the price of the Required Products offered by YTO Group and the Independent Third Parties. We are advised that the Company will only use the quoted prices as material pricing references due to the quoted prices are generally different from the actual goods to be procured by the Company in terms of their quality, specifications and models, and the transaction terms including transportation costs and settlement method may also be different. Therefore, the pricing standard (1) is generally not directly applicable.

Given that the pricing standard (1) is only used as material pricing references instead of directly applied in determining the price, we concur that the pricing standard (1) is effective in providing a source of reference for the Company only.

In the view of the pricing standard (2), we are given to understand that the finance department of the Company will obtain one to two agreement(s) of YTO Group providing the same goods to the Independent Third Parties, to ensure that the price of the same goods offered by YTO Group to the Company shall not be higher than that offered to independent third parties. Meanwhile, finance department shall request YTO Group to provide cost analysis of goods (including cost breakdown and gross profit margin) to ensure that the prices are fair and reasonable.

We have obtained and reviewed ten randomly selected sets of sample invoices and/or contracts for each of the transactions entered into (i) between the Group and YTO Group; (ii) between the Group and the Independent Third Parties; and (iii) between YTO Group and the Independent Third Parties during the same period, where price comparison of similar type of Required Products is available. We observed that the price charged by YTO Group to the Group is not less favourable to the Group than that charged by the Independent Third Parties.

In the view of the pricing standard (3), we are advised that the finance department of the Company will obtain cost analysis of goods from YTO and finalise the final price in accordance with the cost analysis and the percentage mark-up which is not more than 30%. The finance department shall also perform quarterly update and review on the average gross

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profit margin of listed companies engaged in manufacturing of special purpose equipment and the gross profit margin of the historical transactions. The finance department and the office of the Board shall ensure that the percentage mark-up of not more than 30% is fair and reasonable. The Company will not adopt pricing standard (3) and may negotiate with YTO to revise the pricing standards by entering into supplemental agreement in compliance with the requirements of the Listing Rules should it consider such percentage mark-up is no longer fair and reasonable. Having considered the above, we are of the view that the review mechanism performed by the finance department of the Company and the office of the Board is fair and reasonable.

We have also obtained and reviewed four cost analysis samples of the procurement transaction, which YTO Group was the only supplier to the Group. We noted that the gross profit margins of these sample transactions are within 30% and the price charged by YTO Group to the Group is not less favourable to the Group than the market average gross profit margin as the analysis below.

In order to further assessing the fairness and reasonableness of the mark-up of 30%, we have searched on the website of CSRC (<http://www.csrc.gov.cn>) and we noted that the Company is classed into manufacturing industry noted as special purpose equipment with an industry code 35 under the classification of the company industry by the CSRC. We also noted that, in the fourth quarter of 2016, there are 172 listed companies, the shares of them are listed on the Shenzhen Stock Exchange and Shanghai Stock Exchange, are under the same industry code of special purpose equipment industry. According to the available information from Bloomberg, the average gross profit margin of these listed companies for each of the years ended 31 December 2013, 2014 and 2015 and the six months ended 30 June 2016 is 32.27%, 32.51%, 31.42% and 32.08% respectively. Thus, the mark-up percentage of not more than 30% under the Material Procurement Agreement is in line with the market and we are of the view that the mark-up percentage of not more than 30% is fair and reasonable.

In order to ensure the effectiveness of the internal control procedures in approving each of the agreements, we have reviewed the “Management Policies for Connected Transactions” formulate by the Company and enquired with the management of the Company for the internal control procedures in relation to the approval of agreements, and to ensure that the abovementioned pricing standards are properly followed and the relevant Annual Caps would not be exceeded. We noted that different levels of management of the Company participate in the review of the transactions under the Material Procurement Agreement to ensure that it is in compliance with the with the terms and conditions as stated in the agreement and the relevant pricing standards are properly followed. The agreement for procurement together with the negotiation memo (containing types and specifications of products, record of negotiation target, request and undertaking, results of the negotiation and other details) between the specific trained procurement executives of the Company and the suppliers are first delivered to the head of operation department for review and approval. The operation department and technical department are responsible for assessing the suppliers’ products

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qualities, production capacities, performance capacities and other capacities, based on factors including quality and system certification, characteristics of the main technology and process, annual sales results and main production equipment. Upon obtaining the approval of the head of the operation department, as the products procured by the Company are generally supplied by YTO Group and several Independent Third Parties, the finance department would review and compare the prices and terms of the procurements agreement providing the same product to the Company among two to three suppliers including YTO Group and Independent Third Parties and would adopt the lowest price under the same terms and conditions, subject to the type, quality and technical requirements of the Required Products. The finance department would make sure the prices and terms offered by YTO Group are fair and reasonable that no less favourable than those offered by independent suppliers. For those Required Products that there are no independent suppliers, the finance department would request YTO Group to provide the cost breakdown (containing raw materials and manufacturing costs, period costs, gross profit margin and other details) and analysis. The finance department would then evaluate the reasonableness of the price charged based on the general gross profit margin in the machinery manufacturing industry with reference to the listed companies engaged in manufacturing of special purpose equipment which classified under the industry classification (industry code: 35) of the CSRC. The finance department would compare the relevant gross profit margin from the cost breakdown of the Required Products provided by YTO Group with the general gross profit margin of the industry in order to ensure the price charged by YTO Group to the Group is not less favourable to the Group than the general gross profit margin of the industry. The agreement would then be reviewed and approved by the legal department to ensure the legality. The agreement can be executed upon obtaining the approvals from all the abovementioned departments of the Company.

We have obtained and reviewed ten sample agreement approval forms for approving the agreement for the purchase of the Required Products from YTO Group and from the Independent Third Parties respectively. We have considered the result of samples reviewed and noted that each of the department head of the abovementioned departments of the Company was required to comment and sign on the approval forms for both the transactions entered into between (i) the Group and YTO Group; and (ii) the Group and the Independent Third Parties, and the abovementioned pricing standards are properly followed. We have further noted from “Management Policies for Connected Transactions” that the Company has assigned its financial department to monitor the usage of the Annual Caps and report to the office of the Board quarterly in order to ensure that the transactions amount would not exceed the relevant Annual Caps. The finance department will inform the Board for a transaction which is expected to exceed the relevant Annual Caps.

Having considered (i) the result of the samples reviewed; (ii) different levels of the management of the Company participate in the review of the transactions; (iii) the pricing standards are properly followed; and (iv) the Company has adopted internal policy to monitor the usage of the Annual Caps, we are of the view that appropriate internal control measures

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are in place by the Company to ensure that the Material Procurement Agreement will be conducted on normal commercial terms and to safeguard the interests of the Independent Shareholders and of the Company as a whole.

Given that (i) the transactions under the abovementioned samples were transacted during the term of the Material Procurement Agreement and thus are relevant samples; and (ii) the samples represent the transactions which covered different types of the Required Products where price comparison with the Independent Third Parties is available, we consider the samples reviewed are fair and representative.

Having considered that (i) there is no change on the Material Procurement Agreement in material aspects including but not limited to the pricing standards; (ii) YTO undertakes that the applicable price of the goods offered to the Group shall not be less favourable than that offered to independent third party customers of YTO Group associates of YTO Sinomach and the subsidiaries of Sinomach for the same goods and (iii) the Company has adopted certain internal control policies to ensure the compliance of the pricing standards and monitor the usage of the Annual Caps as set out in the section headed “Measures of Internal Control” in the Board Letter and the procedures for approving the procurement agreements as mentioned above, we are of the view that the terms of the Material Procurement Agreement, including but not limited to the pricing standards, are on normal commercial terms, fair and reasonable and in the interests of the Company and the Independent Shareholders as a whole.

### *Historical Figures, the Existing Annual Caps and the Proposed Annual Caps for the Transactions under the Material Procurement Agreement*

In respect of the Material Procurement Agreement, the following table sets out the historical transaction amounts for the years ended 31 December 2014, 2015 and 2016. The table also sets out the Material Procurement Agreement Existing Annual Cap for the year ended 31 December 2016, and the Material Procurement Agreement Existing Annual Caps and the Material Procurement Agreement Proposed Revised Annual Caps for the years ending 31 December 2017 and 2018:

*(Unit: RMB in million)*

|                                   | Historical transaction amounts for<br>the year ended 31 December |                                |                                | Existing Annual Caps for<br>the year ending 31 December |        |        | Proposed revised Annual<br>Caps for the year ending<br>31 December |          |
|-----------------------------------|--|--------------------------------|--------------------------------|---|--------|--------|--|----------|
|                                   | 2014<br><i>(Approximately)</i>                                   | 2015<br><i>(Approximately)</i> | 2016<br><i>(Approximately)</i> | 2016  | 2017   | 2018   | 2017   | 2018     |
| Material Procurement<br>Agreement | 376.16   | 568.48                         | 498.77                         | 500.00  | 500.00 | 500.00 | 1,498.00   | 1,648.00 |

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The historical transaction amount for the year ended 31 December 2016 under the Material Procurement Agreement was approximately RMB498.77 million, representing approximately 99.75% of the Material Procurement Agreement Existing Annual Cap for the year ended 31 December 2016.

As at the Latest Practicable Date, the Material Procurement Agreement Existing Annual Caps for the years ended 31 December 2016 and ending 31 December 2017 have not been exceeded.

The Material Procurement Agreement Proposed Revised Annual Caps for the years ending 31 December 2017 and 2018 are RMB1,498.00 million and RMB1,648.00 million respectively, which represent an increase of RMB998.00 million (approximately 199.60%) and RMB1,148.00 million (approximately 229.60%) from the Material Procurement Agreement Existing Annual Caps for the years ending 31 December 2017 and 2018 respectively.

*Basis for Revision of the Annual Caps under the Material Procurement Agreement*

As set out in the Board Letter, taking into account the following factors, the Board expects that the Material Procurement Agreement Existing Annual Caps will not be sufficient, and proposes to revise to the Material Procurement Agreement Proposed Revised Annual Caps:

- (1) the abovementioned approximately 99.75% utilisation rate of the Existing Annual Cap for the year ended 31 December 2016 under the Material Procurement Agreement; and
- (2) the Material Procurement Agreement Proposed Revised Annual Caps were determined based on the amounts of the Material Procurement Agreement Existing Annual Caps and the estimated increment (the “**Material Procurement Agreement Annual Caps Increment**”) in transaction amounts contemplated under the Material Procurement Agreement for the years ending 31 December 2017 and 2018, which is attributable to the facts that:
  - (a) In August 2016, YTO increased its shareholdings and became a controlling shareholder in Luoyang Zhongshou, which has become a subsidiary of YTO after such increase. Luoyang Zhongshou is principally engaged in research and development, production and sales of wheat, corn and other harvesting machinery products. YTO Group also has the capacity for production of certain agricultural machinery.



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In order to implement the operational idea of the Company of providing customers with the most valuable agricultural equipment whole-set solutions, the Company intends to purchase products including harvesting machinery and agricultural machinery from YTO Group and utilise advantages of the Company, for the purpose of providing customers with unit sales and whole-sets of solutions for agricultural mechanisation to meet the needs of the customers for full-process mechanisation in operation.

The Company expects to purchase approximately 6,000 units of harvesting machinery and approximately 11,500 units of agricultural machinery from YTO Group in 2017 for the aggregate estimated transaction amounts of approximately RMB742 million or the year ending 31 December 2017, accounting for approximately 74.35% of the Material Procurement Agreement Annual Caps Increment for the year ending 31 December 2017.

- (b) In 2016, the Company completed the transformation of tractor and diesel engine machinery to national III emission standard. Due to an expected increase in the estimated 2017 annual sales volume for diesel engine machinery of the Company by approximately 10% from that in 2016, it is expected that the purchase volume of the Company and its subsidiary, YTO (Luoyang) Diesel Engine Company Limited\* (一拖 (洛陽) 柴油機有限公司) (“**YTO Diesel Engine Company**”), for products used for production of diesel engine machinery, including (i) the exhaust gas recirculation valve (the “**EGR valve**”) manufactured by Luoyang Tractor Research Company Limited\* (洛陽拖拉機研究所有限公司) (a subsidiary of the Company, and also an associate of YTO due to the fact that YTO holds 49% of its equity interest) (“**Tractor Research Company**”); and (ii) products including electronic control pump and camshaft manufactured by YTO (Luoyang) Fuel Injection Pump Company Limited\* (一拖 (洛陽) 燃油噴射有限公司) (“**YTO Fuel Injection Pump Company**”) (a subsidiary of the Company, and also an associate of YTO due to the fact that YTO holds 10.57% of its equity interest), will increase significantly. The Company expects that the aggregate estimated increase transaction amounts for products including the EGR valve, electronic control pump and camshaft, to be purchased by the Company and YTO Diesel Engine Company from Tractor Research Company and YTO Fuel Injection Pump Company will be approximately RMB256 million, accounting for approximately 25.65% of the Material Procurement Agreement Annual Caps Increment for the year ending 31 December 2017.



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- (c) According to the expected demand in the market for harvesting machinery and the Company's plan, it is expected that the Material Procurement Agreement Proposed Revised Annual Cap for the year ending 31 December 2018 will approximately 10% higher than that for the year ending 31 December 2017.

YTO is a large-scale equipment manufacturing conglomerate in China, with extensive experience in research and development and sales of machinery products and core manufacturing capability. Upon acquisition of Luoyang Zhongshou by YTO and YTO became a controlling shareholder in Luoyang Zhongshou, the production and operating capability of Luoyang Zhongshou will be improved and the quality level of its products will be enhanced, which in turn will further expand the market competitiveness of its products.

According to the statistics prepared by the Company, in 2016, the total unit sale of grain harvesting machinery and corn harvesting machinery of the industry in the PRC was 90,084 units and the sale of the said products of Luoyang Zhongshou was 5,460 units which accounted for 6.06% in 2016 (2015: 4.90%). As advised by the management of the Company, in 2017, with the support from YTO Group, Luoyang Zhongshou will propose to improve its existing products and introduce certain competitive new products, so as to improve the sales volume of its products. Luoyang Zhongshou currently has more than 300 dealers while the Company has extensive and established distribution network, with approximately more than 1,000 dealers in total. By virtue of sharing of distribution networks and unit sales, the sales volume of harvesting machinery is expected to increase.

The Company expects to purchase harvesting machinery and agricultural machinery from YTO Group for estimated transaction amounts of approximately RMB742 million, accounting for approximately 74.35% of the Material Procurement Agreement Annual Caps Increment, for the year ending 31 December 2017. As advised by the Company, the Company has no historical transaction record with YTO in relation to the purchase of harvesting machinery and agricultural machinery. We have obtained and reviewed the market demand analysis provided by the Company and after enquired the management of the Company in relation to the Company's plan, we noted that the Company targets to purchase approximately 11,500 units of agriculture machinery and approximately 6,000 units of harvesting machinery from YTO Group. The estimated total amount for the purchasing of the agricultural machinery and the harvesting machinery from YTO Group in 2017 accounts for approximately 74.35% of the Material Procurement Agreement Annual Caps Increment for the year ending 31 December 2017.

According to the "2016中國農業機械化發展白皮書 (2016 White Paper on the Development of Agricultural Mechanisation in the PRC\*)" issued by the China Agricultural Mechanisation Association, with the dual drivers of policies under the "Thirteenth-Five Year" Plan and the demands in the market, a growth of 2.4% was recorded for the total power of agricultural machineries, reaching 1.144 billion kilowatts, in 2016. The inventory volume of large

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and medium-scale tractors and combine harvesters recorded a year-on-year increase of approximately 7.4% and 8.2%, respectively. The consolidated mechanisation for the cultivation, planting and harvesting of main crops reached 65%–66% nationwide in the PRC, representing an increase of 2%–3% as compared with the ending period under the “Twelfth-Five Year” Plan. In light of such growth, by the end of the “Thirteenth-Five Year” Plan, the country will be able to meet the target of 70% for consolidated mechanisation for the cultivation, planting and harvesting of main crops as proposed under the plan.

Although the PRC economy was influenced by the downward pressure, the total revenue generated from the main businesses of agricultural machinery enterprises, which above designated size nationwide, amounted to RMB451.639 billion in 2016, representing an increase of approximately 5.8% as compared with the same period of last year, while total profit recorded by agricultural machinery enterprises above designated size amounted to RMB25.524 billion, representing an increase of approximately 1.39%. The government has been providing greater financial support to the agricultural machinery industry, the budget for the industry is amounted to approximately RMB977 million, which represented a year-on-year increase of approximately 51.37%.

We also noted from the “2016 White Paper on the Development of Agricultural Mechanisation in the PRC” that the unit price of agricultural machinery products increased from the bottom of RMB6,800/unit in 2013 to RMB28,000/unit in 2016. 60% of agricultural machinery products were consumed by 20% of new agricultural management entities.

In 2016, the Ministry of Finance of the PRC and the National Development and Reform Commission jointly issued the “關於擴大18項行政事業性收費免徵範圍的通知 (Notice on Expanding the Exemption Scope of 18 Administrative Charge Items\*)”, which requires the exemption of five administrative charge items on the safety supervision over agricultural machinery since 1 May 2016, which includes the charges for the number plate, operating license, registration certificate, driving license and safety technology inspection for tractors. The exemption amount was nearly RMB1 billion.

In 2016, the subsidy for the acquisition of agricultural machinery financed by the PRC government amounted to approximately RMB23.65 billion and there were approximately 2.63 million units of agricultural machinery acquired with the government subsidy, which benefited over 2.30 million of agricultural households and attracted over RMB50.0 billion of investment from agricultural households.

Given that (i) the Board expects that the Material Procurement Agreement Existing Annual Caps will not be sufficient as 99.75% of the Existing Annual Cap for the year ended 31 December 2016 under the Material Procurement Agreement has been utilised; (ii) the management of the Company expects to have a significant sales amount from the harvesting machinery through the sales channel of the Company and due to the control of Luoyang

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Zhongshou by YTO; (iii) the Material Procurement Agreement Existing Annual Caps limited the Company to capture the revenue generated from the sales of harvesting machinery which will be purchased from Luoyang Zhongshou; (iv) the abovementioned policies implemented by the PRC government would have a significant impact to boost up to the market demand for the agricultural machinery and harvesting machinery, the Company is in need to revised the Material Procurement Agreement Existing Annual Caps in order to capture this opportunity to increase its revenue from the sales of the agricultural machinery and harvesting machinery.

We are given to understand that the Company is of the view that by purchasing the harvesting machinery and agricultural machinery from YTO Group, the Company is able to gradually achieve the object of providing customers with whole-sets of “plowing, planting and harvesting” for agricultural mechanisation. This is not only meeting the needs of customers for full-process mechanisation in operation, but also cost-effective to sell this new product by utilising the Company’s brand influence, marketing channels and after-sale service system. We noted that the Company provides customers with whole-sets of solutions for agricultural mechanisation through purchase of harvesting machinery and agricultural machinery in accordance with the Material Procurement Agreement, and therefore we are of the view that the estimated transaction amounts of approximately RMB742 million is justifiable.

On the other hand, according to the “關於實施國家第三階段非道路移動機械用柴油機排氣污染物排放標準的公告 (Announcement on the Implementation of National III Emission Standard for the Emission Standard of Air Pollutants of Diesel Engines for Non-road Mobile Machinery\*)” announced by the Ministry of Environmental Protection of the PRC, since 1 December, 2016, no diesel engines that fail to meet the national III emission standard shall be installed for all agricultural machineries manufactured, imported and sold. As stated in the “2016 White Paper on the Development of Agricultural Mechanisation in the PRC”, for manufacturers of agricultural machinery and equipment, the shifting to national III emission standard has offered the industry a great opportunity to pursue industrial adjustment and enterprise upgrade in order to assist enterprises in reducing overcapacity, adjusting industry structure, enhancing product technology, improving sale and marketing services and fulfilling other new requirements.

As noted from the Group’s annual result for the year ended 31 December 2016, there is a further promotion of structural reforms on the agricultural supply side in the PRC laid a policy foundation for the development of agricultural machinery industry. The agricultural machinery and equipment manufacturing industry has been listed as the ten key development fields in “Made in China 2025”. The development of high-end agricultural equipment, such as large tractors, and the key core spare parts will be accelerated. The promulgation of the “Action Plan on Agricultural Equipment Development (2016–2025)” of the PRC provides an exceptional strategic opportunity for the transformation and upgrade of enterprises. The good market performance of power-shift products and machinery products with national III standard provides the Company with the first mover advantage in industry competition and transformation and upgrade.

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As the Company completed the transformation of tractor and diesel engine machinery to national III emission standard. It is expected that the purchase volume of the Company of the EGR valve manufactured by Luoyang Tractor Research Company Limited and the electronic control pump and camshaft manufactured by YTO Fuel Injection Pump Company will increase significantly. The Company expects that the aggregate estimated newly increased transaction amounts for the EGR valve, electronic control pump, camshaft to be purchased by YTO Diesel Engine Company from Tractor Research Company and YTO Fuel Injection Pump Company, respectively will be approximately RMB256 million, accounting for approximately 25.65% of the Material Procurement Agreement Annual Caps Increment for the year ending 31 December 2017.

Furthermore, as advised by the Company, the total annual sales of diesel engine machinery in 2017 aims to have an increase of approximately 10% as compared to that in 2016. The Company targets to sell approximately 150,000 units of the diesel engine machinery in 2017. The estimated increase in sales of the diesel engine machinery addressed the increased demand for the EGR valve, electronic control pump and camshaft which are used for the production of the diesel engine machinery. The estimated total amount for the EGR valve, electronic control pump, camshaft to be purchased by YTO Diesel Engine Company from Tractor Research Company and YTO Fuel Injection Pump Company in 2017 accounts for approximately 25.65% of the Material Procurement Agreement Annual Caps Increment for the year ending 31 December 2017.

In order to adapt the changing market and customer's needs, it is important for the Company to fully make use of its advantages including research and development, manufacturing and sales, to boost high-end products to the market, control product costs effectively and increase market share of the products. By selling the harvesting machinery and agricultural machinery to provide customers with whole-sets of "plowing, planting and harvesting" agricultural machinery and harvesting machinery, the Company aims at fulfilling customers' need and expectation and provide extra by faster speed, better products and services.

Having considered (i) the Company intends to purchase harvesting machinery and agricultural machinery from YTO Group; (ii) the Material Procurement Agreement Existing Annual Caps limited the Company to capture the revenue generated from the sales of harvesting machinery which will be purchased from Luoyang Zhongshou; and (iii) the mass production of national III series of diesel engine machinery, the 2017 sales volume for the diesel engine machinery is expected to increase by approximately 10% as compared to that with 2016 and newly increased transaction amounts for the EGR valve, electronic control pump, camshaft to be purchased by the Company from Tractor Research Company and YTO Fuel Injection Pump Company, we are of the view that the Material Procurement Agreement Proposed Revised Annual Cap for the year ending 31 December 2017 is fair and reasonable so far as the Independent Shareholders are concerned.

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The Material Procurement Agreement Proposed Revised Annual Caps for the year ending 31 December 2018 is approximately 10% higher than the Material Procurement Agreement Proposed Revised Annual for the year ending 31 December 2017. In order to address the reasonableness of the 10% increment, we have analysed the historical transaction trend under the Material Procurement Agreement for three years ended 31 December 2016 and referenced to the expected gross domestic products (“GDP”) growth of the PRC in 2017, which is 6.50% forecasted by the International Monetary Fund (“IMF”). Having considered (i) the 6.50% expected GDP growth of the PRC forecasted by the IMF; and (ii) as advised by the Company, such increase is mainly due to the expected increase of harvesting machinery, agriculture machinery and the Required Products which will be purchased by the Company from YTO Group during the corresponding period in 2018, we are of the view that the Material Procurement Agreement, including but not limited to the pricing standards, Proposed Revised Annual Cap for the year ending 31 December 2018 is fair and reasonable so far as the Independent Shareholders are concerned.

Given the abovementioned, we are of the view that the Material Procurement Agreement Proposed Revised Annual Caps are fair and reasonable so far as the Independent Shareholders are concerned.

**(B) Sale of Goods Agreement**

Pursuant to the Sale of Goods Agreement, the Company will, on behalf of the Group, as a supplier and/or supplying agent, provide to the members of YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach, products to be used in the production and in the ordinary course of business of the purchaser (the “Sales Products”), including but not limited to, raw materials, spare parts (including casting parts and wheels), components (including semi-finished parts and finished parts) and equipment (including diesel engine machinery and tractors). Having considered the wide sales network and the well-developed logistics and storage facilities of YTO Group, the Sale of Goods Agreement provides a channel for the Company to distribute the products manufactured by the Company.

As set out in the Board Letter, the payment terms under the Sales of Goods Agreement shall be principally settled within three months after the delivery of goods by the supplier. Subject to negotiations between the parties, prepayments by the purchaser of no more than six months from the estimated date of delivery of the goods are acceptable.

We have enquired with the management of the Company and are given to understand that the Group normally adopted the three months settlement payment term in its transactions with the Independent Third Parties and YTO Group while we are advised that the Group has not entered into any transactions with the Independent Third Parties nor YTO Group which adopted the prepayment term. As further noted from the management of the Company, such

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## LETTER FROM VEDA CAPITAL

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prepayment term is only acceptable and subject to the negotiations between the parties which will take into account of the factors, including but not limited to, the market condition, the demand and supply of the relevant goods in the market, the production capacities and the inventory. Although the Group has not entered into any transactions with the Independent Third Parties nor YTO Group which has adopted prepayment term, the prepayment term is considered as favourable to the Company as receiving part of the payment in advance under special occasions and upon negotiations with the purchaser in order to safeguard the interests of the Company. In these regards, we have obtained and reviewed ten randomly selected sample sales contracts for each of the transactions entered into (i) between the Group and YTO Group and (ii) between the Group and the Independent Third Parties, we observed that the above payment terms offered by the Group to YTO Group is not more favourable to YTO Group than that offered to the Independent Third Parties as the three months settlement payment term is available to the transactions entered into between the Group and YTO Group and between the Group and the Independent Third Parties, and the prepayment term can be adopted in the transactions entering with both YTO Group and the Independent Third Parties upon negotiations.

Therefore, we consider that the payment terms under the Sale of Goods Agreement are on normal commercial terms and not more favourable to YTO Group than those offered by the Company to the Independent Third Parties.

### *Pricing standards of the Transactions under the Sale of Goods Agreement*

The price of goods to be supplied or provided will be determined based on the following price basis:

- (1) the market price of an independent third party obtained through prices quoted on websites for the industry or enquiries in the market (i.e. the price of the same or similar product provided to the Independent Third Parties by suppliers other than YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach in the same region during the ordinary course of business on normal commercial terms);
- (2) if there is no market price determined by an independent third party, the transaction price between the Group and an independent third party; and
- (3) if none of the above is applicable, costs plus a percentage mark-up (tax-inclusive), which is not more than 30% (i.e. price = cost × (1 + percentage mark-up)), whereas the 30% markup is determined based on (i) the average gross profit margin of listed companies engaged in manufacturing of special purpose equipment (this industry classification is according to the “Guidelines for the Industry Classification of

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## LETTER FROM VEDA CAPITAL

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Listed Companies (上市公司行業分類指引)” (Revised in 2012) and the industry classification results of listed companies issued by the CSRC, and the Company is within this classification) for the three years ended 31 December 2015 and the six months ended 30 June 2016; and (ii) the gross profit margin of the same or similar products of YTO Group; and (iii) the gross profit margin of the historical transactions of sales of the same or similar products to the Group by YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach.

As noted in the Board Letter, in any event, the applicable price of the goods offered to YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach by the Group shall not be more favourable than that offered to the Independent Third Party customers of the Group.

We are also given to understand that, in relation to the pricing standard (1), the sale department of the Company will obtain prices of the same or similar products in the open market from the Independent Third Parties in the ordinary course of business. However, the products with such quoted prices are generally different from the actual products to be sold by the Company in terms of their quality, specifications and models, and the transaction terms including transportation costs and settlement method may also be different. Therefore, pricing standard (1) is generally not directly applicable.

In relation to other pricing standards, we are advised by the Company, the finance department of the Company will formulate unified sales prices (the “**Unified Sales Prices**”) of general generic products of the Company according to the Company’s cost and gross profit margin, which will be adopted uniformly in transactions of the Company with the purchaser or with the Independent Third Party. If the purchaser or an Independent Third Party has specific request in relation to technical process and assembly of spare parts, etc. of products of the Company, the Unified Sales Prices will no longer be applicable and the Company will adopt pricing standard (3). But in any event, finance department and sales department are responsible for ensuring that the price of the same products offered by the Company to the purchaser shall not be lower than that offered to the Independent Third Parties. The finance department shall also perform quarterly update and review on the average gross profit margin of listed companies engaged in manufacturing of special purpose equipment and the gross profit margin of the historical transactions. The finance department and the office of the Board shall ensure that the percentage mark-up of not more than 30% is fair and reasonable. The Company will not adopt pricing standard (3) and may negotiate with the purchaser to revise the pricing standards by entering into supplemental agreement in compliance with the requirements of the Listing Rules should it consider such percentage mark-up is no longer fair and reasonable. Having considered the above, we are of the view that the review mechanism performed by the finance department of the Company and the office of the Board is fair and reasonable.



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## LETTER FROM VEDA CAPITAL

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We have obtained and reviewed ten sample sales orders and/or contracts for the Sales Products entered into (i) between the Group and YTO Group; and (ii) between the Group and the Independent Third Parties, where price comparison of similar type of Sales Products is available. We observed that the price charged by the Group to YTO Group is not more favourable to YTO Group than that charged to the Independent Third Parties.

Also, in order to further assessing the fairness and reasonableness of the mark-up of 30%, we have searched on the website of CSRC (<http://www.csrc.gov.cn>) and we noted that the Company is classed into manufacturing industry noted as special purpose equipment with an industry code 35 under the classification of the company industry by the CSRC. We also noted that, in the fourth quarter of 2016, there are 172 listed companies, the shares of them are listed on the Shenzhen Stock Exchange and Shanghai Stock Exchange, are under the same industry code of special purpose equipment industry. According to the available information from Bloomberg, the average gross profit margin of these listed companies for each of the years ended 31 December 2013, 2014 and 2015 and the six months ended 30 June 2016 is 32.27%, 32.51%, 31.42% and 32.08% respectively. Thus, the mark-up percentage of not more than 30% under the Material Procurement Agreement is in line with the market and we are of the view that the mark-up percentage of not more than 30% is fair and reasonable.

We have also obtained and reviewed ten cost analysis samples of the Sales Products provided by the Company, which the Sales Products were sold by the Company to YTO Group. We noted that the gross profit margins of these sample transactions are within 30% and the price charged by the Group to YTO Group is not more favourable to YTO Group than the market average gross profit margin.

In order to ensure the effectiveness of the internal control procedures in approving each of the agreements, we have reviewed the “Management Policies for Connected Transactions” formulated by the Company and enquired with the management of the Company for the internal control procedures in relation to the approval of agreements, and to ensure that the abovementioned pricing standards are properly followed and the relevant Annual Caps would not be exceeded. We noted that different levels of management of the Company participate in the review of the transactions under the Sale of Goods Agreement to ensure that it is in compliance with the with the terms and conditions as stated in the agreement and the relevant pricing standards are properly followed. We have obtained and reviewed the price list of the Company for the Sales Products and are given to understand from the Company that same price would be applied to both YTO Group and the Independent Third Parties for same type of Sales Products unless different raw materials or components for the Sales Products are specially requested by the purchaser and the price difference would be the difference in costs. The agreement for sales together with the negotiation memo between the relevant staff of the sales department of the Company and the purchasers are first delivered to the head of



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## LETTER FROM VEDA CAPITAL

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operation department for review and approval. The operation department and the technical department are responsible for assessing the production capacities of the Company based on factors including products specification, order size and delivery terms and assessing the credibility of the purchaser based on factors including the purchaser's business license, assets, legal representative and previous cooperation with the Company. Upon obtaining the approval of the head of the operation department, the finance department, in relation to the general generic products, would review whether the prices are consistent with the Unified Sales Prices; and the finance department and the sales department, in relation to the specific products, would analyse the cost breakdown of the products and formulate the prices according to the specific request on product technology, technical process and quality, and based on reasonable gross profit margin. The finance department would make sure the prices and terms offered to YTO Group are fair and reasonable that no more favourable to YTO Group than those offered to the Independent Third Parties. The agreement would then be reviewed and approved by the legal department to ensure the legality. The agreement can be executed upon obtaining the approvals from all the abovementioned departments of the Company.

We have obtained and reviewed ten sample agreement approval forms for approving the agreement for the sales of Sales Products from the Company to YTO Group and the Independent Third Parties respectively. We have considered the result of sample reviewed and noted that each of the department head of the abovementioned departments of the Company was required to comment and sign on the approval forms for both the transactions entered into between (i) the Group and YTO Group; and (ii) the Group and the Independent Third Parties, and the abovementioned pricing standards are properly followed. We have also further noted from the "Management Policies for Connected Transactions" that the Company has assigned its financial department to monitor the usage of the Annual Caps and report to the office of the Board quarterly in order to ensure that the transactions amount would not exceed the relevant Annual Caps. The finance department will inform the Board for a transaction which is expected to exceed the relevant Annual Caps.

Having considered (i) the result of the samples reviewed; (ii) different levels of the management of the Company participate in the review of the transactions; (iii) the pricing standards are properly followed; and (iv) the Company has adopted internal policy to monitor the usage of the Annual Caps, we are of the view that appropriate internal control measures are in place by the Company to ensure that the Sales of Goods Agreement will be conducted on normal commercial terms and to safeguard the interests of the Independent Shareholders and of the Company as a whole.

## LETTER FROM VEDA CAPITAL

Given that (i) the transactions under the abovementioned samples were transacted during the term of the Sale of Goods Agreement and thus are relevant samples; and (ii) the samples represent the transactions which covered different types of the Sale Products where price comparison with the Independent Third Parties is available, we consider the samples reviewed are fair and representative.

Having considered that (i) there is no change on the Sales of Goods Agreement in material aspects including but not limited to the pricing standards; (ii) in any event, the applicable price of the goods offered to YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach by the Group shall not be more favourable than that offered to independent third party customers of the Group; and (iii) the Company has adopted certain internal control policies to ensure the compliance of the pricing standards and monitor the usage of the Annual Caps as set out in the section headed “Measures of Internal Control” in the Board Letter and the procedures for approving the sales agreements as mentioned above, we are of the view that the terms of the Sales of Goods Agreement, including but not limited to the pricing standards, are on normal commercial terms, fair and reasonable and in the interests of the Company and the Independent Shareholders as a whole.

### *Historical Figures, the Existing Annual Caps and the Proposed Annual Caps for the Transactions under the Sale of Goods Agreement*

The Company has entered into (i) a sale of goods agreement dated 29 October 2012 (details of which were set out in the Company’s circular dated 28 November 2012) (the “**2012 Sale of Goods Agreement**”) and (ii) the Sale of Goods Agreement for goods sale in the past. In respect of the 2012 Sale of Goods Agreement, the following table sets out the historical transaction amounts for the years ended 31 December 2014 and 2015. The table also sets out the historical transaction amount and the Sale of Goods Agreement Existing Annual Cap for the year ended 31 December 2016, and the Sale of Goods Agreement Existing Annual Caps and the Sale of Goods Agreement Proposed Revised Annual Caps for the years ending 31 December 2017 and 2018:

*(Unit: RMB in million)*

|                            | Historical transaction amounts for<br>the year ended 31 December |                        |                        | Existing Annual Caps for<br>the year ending 31 December |        |        | Proposed revised Annual<br>Caps for the year ending<br>31 December |        |
|----------------------------|--|------------------------|------------------------|---|--------|--------|--|--------|
|                            | 2014   | 2015                   | 2016                   | 2016  | 2017   | 2018   | 2017   | 2018   |
|                            | <i>(Approximately)</i>   | <i>(Approximately)</i> | <i>(Approximately)</i> |   |        |        |  |        |
| Sale of Goods<br>Agreement | 113.45   | 224.20                 | 343.55                 | 350.00  | 200.00 | 210.00 | 460.00   | 488.00 |

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## LETTER FROM VEDA CAPITAL

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The historical transaction amount for the year ended 31 December 2016 under the Sale of Goods Agreement was approximately RMB343.55 million, representing approximately 98.16% of the Sale of Goods Agreement Existing Annual Cap for the year ended 31 December 2016.

As at the Latest Practicable Date, the Sale of Goods Agreement Existing Annual Caps for the years ended 31 December 2016 and ending 31 December 2017 have not been exceeded.

The Sale of Goods Agreement Proposed Revised Annual Caps for the years ending 31 December 2017 and 2018 are RMB460 million and RMB488 million respectively, which represents an increase of approximately RMB260 million (approximately 130%) and RMB278 million (approximately 132.38%) from the Sale of Goods Agreement Existing Annual Caps for the years ending 31 December 2017 and 2018 respectively.

### *Basis for Revision of the Annual Caps under the Sale of Goods Agreement*

As noted from the Board Letter, taking into account the following factors, the Board expects that the Sale of Goods Agreement Existing Annual Caps will not be sufficient, and proposes to revise to the Sale of Goods Agreement Proposed Revised Annual Caps:

- (1) the abovementioned approximately 98.16% utilisation rate of the Sale of Goods Agreement Existing Annual Cap for the year ended 31 December 2016; and
- (2) the Sale of Goods Agreement Proposed Revised Annual Caps were determined based on the amounts of the Sale of Goods Agreement Existing Annual Caps and the estimated increment (the “**Sale of Goods Agreement Annual Caps Increment**”) in transaction amounts contemplated under the Sale of Goods Agreement for the years ending 31 December 2017 and 2018, which is attributable to the facts that:
  - (a) According to the production needs of YTO Group in harvesting machinery and in order to utilise the Company’s core manufacturing capabilities in components including diesel engine, the Company and its subsidiary YTO Diesel Engine Company have sold and shall sell products including diesel engine machinery and spare parts to Luoyang Zhongshou. It is expected that the Company will sell approximately 6,000 units of diesel engines to YTO Group in 2017 and the estimated newly increased transaction amounts for sales of raw materials, diesel engines and spare parts to YTO Group for their production of harvesting machinery for the year ending 31 December 2017 will be approximately RMB260 million, accounting for 100% of the Sale of Goods Agreement Annual Caps Increment for the year ending 31 December 2017.

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## LETTER FROM VEDA CAPITAL

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- (b) According to the business plan for harvesting machinery of Luoyang Zhongshou, it is expected that the transaction amount for the connected transactions of the sale of goods from the Company to Luoyang Zhongshou in 2018 will increase by approximately 6% from that of 2017.

The Company expects that the newly increased transaction amounts will be approximately RMB260 million, accounting for 100% of the Sale of Goods Agreement Annual Caps Increment for the year ending 31 December 2017. We have enquired with the management of the Company regarding the basis of the newly increased transaction amount. During the year of 2017, the Company will sell raw materials, diesel engine machinery and spare parts to Luoyang Zhongshou under the Sale of Goods Agreement for their production of the harvesting machinery which the Company will be purchased under the Material Procurement Agreement. As advised by the management of the Company, the Company sold approximately 1,300 units of the diesel engine machinery to YTO Group in 2016. The Company targets to sell approximately 6,000 units of the diesel engine machinery to YTO Group in 2017 under the Sale of Goods Agreement, which represents an increase of approximately 3.6 times comparing to that in 2016.

Having considered that (i) in order to fully utilise the Company's core manufacturing capabilities and improve production capacity utilisation rate, the Company will sell the required raw materials, diesel engine machinery and spare parts to Luoyang Zhongshou for them to produce the harvesting machinery; and (ii) most of the harvesting machinery produce by Luoyang Zhongshou would eventually be purchased and sold by the Company in order to provide customer with whole-sets of solutions for agricultural mechanisation, we are of the view that the Sale of Goods Agreement Proposed Revised Annual Cap for the year ending 31 December 2017 is fair and reasonable so far as the Independent Shareholders are concerned.

Furthermore, the Sale of Goods Agreement Proposed Revised Annual Caps for the year ending 31 December 2018 is approximately 6% higher than the Sale of Goods Agreement Proposed Revised Annual Caps for the year ending 31 December 2017. In order to address the reasonableness of the 6% increment, we have referenced to the expected GDP growth of the PRC in 2017, which is 6.50% forecasted by the IMF. We noted that the approximately 6% increment in the Sale of Goods Agreement Proposed Revised Annual Caps from 2017 to 2018 is lower than the 6.50% expected GDP growth of the PRC in 2017. Having considered (i) the approximately 6% increment in the Sale of Goods Agreement Proposed Revised Annual Caps from 2017 to 2018 is lower than the expected GDP growth of the PRC in 2017, which is 6.50% forecasted by the IMF; and (ii) the Company expects the sale of diesel engine machinery and spare parts to YTO Group in 2018 will be increased due to the expected increase of harvesting machinery and agriculture machinery which will be purchased by the

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## LETTER FROM VEDA CAPITAL

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Company from YTO Group during the corresponding period in 2018, we are of the view that the Sale of Goods Agreement Proposed Revised Annual Cap for the year ending 2018 is fair and reasonable so far as the Independent Shareholders are concerned.

Given the abovementioned, we are of the view that the Sale of Goods Agreement Proposed Revised Annual Caps are fair and reasonable so far as the Independent Shareholders are concerned.

**(C) *The Composite Services Agreement***

Pursuant to the Composite Services Agreement, YTO, on behalf of YTO Group, its controlled companies and their associates as supplier and/or supplying agent, provide to the Company with storage services and transportation services. For storage services, YTO will provide the Group with qualified warehouses and cargo lifting, handling, custody, maintenance and related warehousing services. For transportation services, the Group required transportation of goods at specific required time and location and services delivered at required standard.

As set out in the Board Letter, the payment terms under the Composite Services Agreement are as follows:

- (1) Storage services: shall be billed quarterly and paid in the following month.
- (2) Transportation services: shall be principally settled within three months after confirmation by the Company (on behalf of the Group) from the date of delivering or receiving the goods.

The payment terms were usually adopted by YTO in its transactions with the Company. We have obtained and reviewed ten randomly selected sample contracts relating to transportation services for each of the transactions entered into (i) between the Group and YTO Group and (ii) between YTO Group and the Independent Third Parties. Due to the Independent Third Parties has accepted the same payment terms which offered by YTO Group according to the reviewed sample contracts, we believe that the payment terms offered by the Company to YTO Group is in line with the industry practice.

On the other hand, we are advised by the management of the Company that the Group has not received any storage services from YTO Group in 2016 and up to the Latest Practicable Date. However, having considered the payment terms of the storage services are not less favourable to the Group than those for the previous storage service transactions between the Company and YTO and for the other transactions between the Company and YTO Group.

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## LETTER FROM VEDA CAPITAL

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Therefore, we consider that the payment terms under the Composite Services Agreement are on normal commercial terms and not less favourable to the Group than those offered to the Independent Third Parties.

*Pricing standards of the transactions under the Composite Services Agreement*

The price of services to be supplied or provided will be determined based on the following price basis:

- (1) the market price of an independent third party obtained through prices quoted on websites for the industry or enquiries in the market (i.e. the price of the same or similar product provided to the Independent Third Parties by suppliers other than YTO Group, associates of YTO, Sinomach and the subsidiaries of Sinomach in the same region during the ordinary course of business on normal commercial terms);
- (2) if there is no market price determined by an independent third party, the transaction price between YTO, its controlled companies and their associates and an independent third party; and
- (3) if none of the above is applicable, costs plus a percentage mark-up (tax-inclusive), which is not more than 30% (i.e. price = cost × (1 + percentage mark-up)), whereas the 30% markup is determined based on (i) the average gross profit margin of listed companies engaged in storage and road transportation services (this industry classification is according to the “Guidelines for the Industry Classification of Listed Companies (上市公司行業分類指引)” (Revised in 2012) and the industry classification results of listed companies issued by the CSRC, and the Company is within this classification) for the three years ended 31 December 2015 and the six months ended 30 June 2016; and (ii) the gross profit margin of the historical transactions of provision of the same and similar service to the Group by YTO, its controlled companies and their associates.

YTO undertakes that the applicable price of the services offered to the Group shall not be less favourable to the Group than that offered to independent third party customers of YTO, its controlled companies and their associates for the same services.

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## LETTER FROM VEDA CAPITAL

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We have attempted to obtain and review the sample orders and/or contracts for similar types of storage and transportation services entered into (i) between the Group and YTO Group and (ii) between the Group and the Independent Third Parties; and (iii) between YTO Group and the Independent Third Parties. However, as advised by the management of the Company, the Group has not entered any transportation services contracts with any Independent Third Parties and the price comparison of similar type of composite service between the (i) between the Group and YTO Group; and (ii) between YTO Group and the Independent Third Parties is not available as the different specific conditions (i.e. goods being transported, weight of the goods and transportation distance) of transportation services provided by YTO Group to the Group and to the Independent Third Parties are different. Furthermore, we are given to understand that the Group has not entered any storage services contracts with YTO Group and the Independent Third Parties during the financial year of 2016 and up to the Latest Practicable Date under the Composite Services Agreement. Therefore, we are not able to make price comparison through obtaining the sample contracts.

The management of the Company has advised that in determining the service fees under the Composite Services Agreement, the Company is currently using the pricing standard (3) only. We are given to understand that the finance department of the Company will obtain cost analysis of services from YTO Group and finalise the final price in accordance with the cost analysis and the percentage mark-up which is not more than 30%. The finance department shall also perform quarterly update and review on the average gross profit margin of listed companies engaged in storage services and road transportation services and the gross profit margin of the historical transactions. The finance department and the office of the Board shall ensure that the percentage mark-up of not more than 30% is fair and reasonable. The Company will not adopt pricing standard (3) and may negotiate with YTO to revise the pricing standards by entering into supplemental agreement in compliance with the requirements of the Listing Rules should it consider such percentage mark-up is no longer fair and reasonable. Having considered the above, we are of the view that the review mechanism performed by the finance department of the Company and the office of the Board is fair and reasonable.

We have also obtained and reviewed ten cost analysis samples of the transportation services provided by the Company, which the transportation services were provided by YTO Group to the Group. We noted that the gross profit margins of these sample transactions are within 30% and the price charged by YTO Group to the Group is not less favourable to the Group than the market average gross profit margin as the analysis below.

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## LETTER FROM VEDA CAPITAL

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In order to further assessing the fairness and reasonableness of the mark-up of 30%, we have searched on the website of CSRC (<http://www.csrc.gov.cn>) and we noted that the Company has referenced to the storage and road transportation services industries with an industry code 54 and 59 under the classification of the company industry by the CSRC. We also noted that, in the fourth quarter of 2016, there are 41 listed companies, the shares of them are listed on the Shenzhen Stock Exchange and Shanghai Stock Exchange, are under the industry classifications of storage and road transportation services industries. According to the available information from Bloomberg, the average gross profit margin of these listed companies for each of the years ended 31 December 2013, 2014 and 2015 and the six months ended 30 June 2016 is 38.24%, 35.87%, 34.41% and 38.78% respectively. Thus, the mark-up percentage of not more than 30% under the Material Procurement Agreement is in line with the market and we are of the view that the mark-up percentage of not more than 30% is fair and reasonable.

In order to ensure the effectiveness of the internal control procedures in approving each of the agreements, we have reviewed the “Management Policies for Connected Transactions” formulated by the Company and enquired with the management of the Company for the internal control procedures in relation to the approval of agreements, and to ensure that the abovementioned pricing standards are properly followed and the relevant Annual Caps would not be exceeded. We noted that different levels of management of the Company participate in the review of the transactions under the Composite Services Agreement to ensure that it is in compliance with the with the terms and conditions as stated in the agreement and the relevant pricing standards are properly followed. The agreement for the composite services (including storage services and transportation services) together with the negotiation memo between the relevant staff of the operation department of the Company and the counterparties in the transactions are first delivered to the head of operation department for review and approval. The operation department is responsible for assessing transportation capacities or service abilities of the counterparties, etc., based on factors including vehicle loading capacity, organisation and delivery capacity, lifting equipment capacity, delivery qualification rate and on-schedule delivery rate. Upon obtaining the approval of the head of the operation department, the finance department would review and compare the prices and terms of the agreements providing the same service to the Company among two to three counterparties including YTO Group and Independent Third Parties and would adopt the lowest price under the same terms and conditions. The finance department would ensure the prices and terms offered by YTO Group are fair and reasonable that they are no less favourable than those offered by the Independent Third Parties. If there is no market price, the finance department would request YTO Group to provide the cost breakdown (containing fuel costs, toll, labor cost tax and other expenses) and analysis. The finance department would then evaluate reasonableness of the price charged based on the general gross profit margin in the storage and transportation industries with reference to the listed companies engaged in storage and



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## LETTER FROM VEDA CAPITAL

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road transportation services which classified under the industry classification (industry code 54 and 59) of the CSRC. The finance department would compare the relevant gross profit margin from the cost breakdown of the storage and transportation services provided by YTO Group with the general gross profit margin of the industry in order to ensure the price charged by YTO Group to the Group is not less favourable to the Group than the general gross profit margin of the industry. The agreement would then be reviewed and approved by the legal department to ensure legality. The agreement can be executed upon obtaining the approvals from all of the abovementioned departments of the Company.

We have obtained five sample agreement approval forms for approving the agreement for the composite services from the Company to show compliance of the abovementioned procedure for the Composite Services Agreement. We have considered the result of samples reviewed and noted that each of the department head of the abovementioned departments of the Company was required to comment and sign on the approval forms for the transactions entered into between the Group and YTO Group, and abovementioned pricing standards are properly followed. We have also further noted from the “Management Policies for Connected Transactions” that the Company has assigned its financial department to monitor the usage of the Annual Caps and report to the office of the Board quarterly in order to ensure that the transactions amount would not exceed the relevant Annual Caps. The finance department will inform the Board for a transaction which is expected to exceed the relevant Annual Caps.

Having considered (i) the result of the samples reviewed; (ii) different levels of the management of the Company participate in the review of the transactions; (iii) the pricing standards are properly followed; and (iv) the Company has adopted internal policy to monitor the usage of the Annual Caps, we are of the view that appropriate internal control measures are in place by the Company to ensure that the Composite Services Agreement will be conducted on normal commercial terms and to safeguard the interests of the Independent Shareholders and of the Company as a whole.

Given that (i) the transactions under the abovementioned samples were transacted during the term of the Composite Services Agreement and thus are relevant samples; and (ii) the samples represent the transactions which covered different types of the services where price comparison with the Independent Third Parties is available, we consider the samples reviewed are fair and representative.

Having considered that (i) there is no change on the Composite Services Agreement in material aspects including but not limited to the pricing standards; (ii) YTO undertakes that the applicable price of the services offered to the Group shall not be less favourable than that offered to independent third party customers of YTO, its controlled companies and their associates for the same services; and (iii) the Company has adopted certain internal control policies to ensure the compliance of the pricing standards and monitor the usage of the

## LETTER FROM VEDA CAPITAL

Annual Caps as set out in the section headed “Measures of Internal Control” in the Board Letter and the procedures for approving the agreement for the composite services, we are of the view that the terms of the Composite Services Agreement, including but not limited to the pricing standards, are on normal commercial terms, fair and reasonable and in the interests of the Company and the Independent Shareholders as a whole.

### *Historical Figures, the Existing Annual Caps and the Proposed Annual Caps for the Transactions under the Composite Services Agreement*

The Company has entered into (i) a composite services agreement dated 29 October 2012 (details of which were set out in the Company’s circular dated 28 November 2012) (the “**2012 Composite Services Agreement**”); and (ii) the Composite Services Agreement in respect of provision of composite services in the past. In respect of the 2012 Composite Services Agreement, the following table sets out the historical transaction amounts for the years ended 31 December 2014 and 2015. The table also sets out the historical transaction amount and the Composite Services Agreement Existing Annual Cap for the year ended 31 December 2016, and the Composite Services Agreement Existing Annual Caps and the Composite Services Agreement Proposed Revised Annual Caps for the years ending 31 December 2017 and 2018:

*(Unit: RMB in million)*

|                                 | Historical transaction amounts for<br>the year ended 31 December |                        |                        | Existing Annual Caps for<br>the year ending 31 December |        |        | Proposed revised Annual<br>Caps for the year ending<br>31 December |        |
|---------------------------------|--|------------------------|------------------------|---|--------|--------|--|--------|
|                                 | 2014   | 2015                   | 2016                   | 2016  | 2017   | 2018   | 2017   | 2018   |
|                                 | <i>(Approximately)</i>   | <i>(Approximately)</i> | <i>(Approximately)</i> |   |        |        |  |        |
| Composite Services<br>Agreement | 228.88   | 224.29                 | 147.17                 | 147.20  | 157.20 | 167.20 | 215.00   | 225.00 |

The historical transaction amount for the year ended 31 December 2016 under the Composite Services Agreement was RMB147,170,000, representing approximately 99.98% of the Composite Services Agreement Existing Annual Cap for the year ended 31 December 2016.

As at the Latest Practicable Date, the Composite Services Agreement Existing Annual Caps for the years ended 31 December 2016 and ending 31 December 2017 have not been exceeded.

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## LETTER FROM VEDA CAPITAL

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The Composite Services Agreement Proposed Revised Annual Caps for the years ending 31 December 2017 and 2018 are RMB215,000,000 and RMB225,000,000 respectively, which represents an increase of RMB57,800,000 (approximately 36.77%) and RMB57,800,000 (approximately 34.57%) from the Composite Services Agreement Existing Annual Caps for the years ending 31 December 2017 and 2018 respectively.

*Basis for Revision of the Annual Caps under the Composite Services Agreement*

As noted from the Board Letter, taking into account the following factors, the Board expects that the Composite Services Agreement Existing Annual Caps will not be sufficient, and proposes to revise to the Composite Services Agreement Proposed Revised Annual Caps:

- (1) the abovementioned approximately 99.98% utilisation rate of the Composite Services Agreement Existing Annual Caps for the year ended 31 December 2016; and
- (2) the Composite Services Agreement Proposed Revised Annual Caps were determined based on the amounts of the Composite Services Agreement Existing Annual Caps and the estimated increment (the “**Composite Services Agreement Annual Caps Increment**”) in transaction amounts contemplated under the Composite Services Agreement for the years ending 31 December 2017 and 2018, which is attributable to the facts that:
  - (a) The Company expects that the Composite Services Agreement Proposed Revised Annual Caps for the year ending 31 December 2017 will increase by 46% from the Composite Services Agreement Existing Annual Caps for the year ended 31 December 2016 for the reasons that:
    - a. products of the Company are mainly transported on highway. Under the Composite Services Agreement, YTO shall provide transportation services for the Company’s products. In September 2016, the “**超限運輸車輛行駛公路管理規定 (Administrative Rules on Highway Driving of Overloading Vehicle\*)**” was implemented in the PRC, leading to an increase in the transportation cost for transporting the Company’s products;
    - b. in order to utilise the advantage of YTO Group in logistics and transportation, sales of harvesting machinery by the Company in 2017 will be transported by YTO Group. It is expected that the transportation cost of the Company for the year ending 31 December 2017 will increase.

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## LETTER FROM VEDA CAPITAL

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- (b) The Company expects that the sales volume of harvesting machinery in 2018 will increase. As such, the Composite Services Agreement Proposed Revised Annual Caps for the year ending 31 December 2018 is expected to increase by approximately 5% from the Composite Services Agreement Proposed Revised Annual Cap for the year ending 31 December 2017.

According to the “超限運輸車輛行駛公路管理規定 (Administrative Rules on Highway Driving of Overloading Vehicle\*)”, a vehicle’s allowed maximum loading weights decreased. Pursuant to the information provided by the Company, a truck could carry 16 to 18 units of 40 horsepower (or below) mid-powered wheeled tractor products before the “超限運輸車輛行駛公路管理規定 (Administrative Rules on Highway Driving of Overloading Vehicle\*)” implemented in September 2016, the number of same type products a truck is allowed to carry dropped to 10 to 11 units since the rules became effective. As the number of Company’s hi-powered and mid-powered wheeled tractor products can be transported by each truck per trip decreased accordingly, it is unavoidable the transportation cost would be increased.

We have also reviewed a number of sample invoices issued by Luoyang YTO Logistics Co. Limited to YTO Group, which showed the transportation cost for same type of hi-powered and mid-powered wheeled tractor products before and after the “超限運輸車輛行駛公路管理規定 (Administrative Rules on Highway Driving of Overloading Vehicle\*)” was implemented. We noticed that the transportation cost has increased by an average of approximately 46% from the samples we have reviewed.

Moreover, according to the Board Letter, the Company intends to buy the harvesting machinery from YTO Group under the Material Procurement Agreement in 2017 and 2018. As advised by the management of the Company, in order to make use of the advantage of YTO Group in logistics, the harvesting machinery will be transported by YTO Group. It is expected that the transportation cost for transporting the Company’s harvesting machinery will be increased due to the increase of their quantity.

Luoyang YTO Logistics Co. Limited (一拖 (洛陽) 物流有限公司), a subsidiary of YTO, has become an integrated logistics enterprise providing road transport, railway transport, warehousing and distribution, installation and repair of motor vehicles, driver training and freight information services. It obtained the “國家二級道路運輸企業資質 (National Secondary Road Transport Enterprise Qualification\*)” and the qualification of “洛陽市一類機動車維修企業資質 (First Class of Motor Vehicle Maintenance Enterprises in Luoyang\*)”. Having considered that YTO Logistics Co. Limited has a strong integrated logistics services and industry competitiveness, the Group can enhance the cost and time effectiveness in the logistics and storage aspects.

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## LETTER FROM VEDA CAPITAL

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Having considered that (i) the implementation of the “超限運輸車輛行駛公路管理規定 (Administrative Rules on Highway Driving of Overloading Vehicle\*)”; (ii) the reviewed samples show an average increase of approximately 46% on the transportation cost after the “超限運輸車輛行駛公路管理規定 (Administrative Rules on Highway Driving of Overloading Vehicle\*)” being effective, which is same as the proposed 46% increment in the annual caps under the Composite Services Agreement for the year ending 31 December 2017 from the Composite Services Agreement Existing Annual Cap for the year ended 31 December 2016; and (iii) the increase of the Company’s target harvesting machinery sale in 2017 comparing to that in 2016, we are of the view that the Composite Services Agreement Proposed Revised Annual Cap for the year ending 31 December 2017 is fair and reasonable and in the interests of the Company and the Independent Shareholders as a whole.

The Composite Services Agreement Proposed Revised Annual Caps for the year ending 31 December 2018 is approximately 5% higher than the Composite Services Agreement Proposed Revised Annual Caps for the year ending 31 December 2017. In order to address the reasonableness of the 5% increment, we have referenced to the expected GDP growth of the PRC in 2017, which is 6.50% forecasted by the IMF. We noted that the approximately 5% increment in the Composite Services Agreement Proposed Revised Annual Caps from 2017 to 2018 is lower than the 6.50% expected GDP growth of the PRC in 2017.

Having considered (i) the 5% increment in the Composite Services Agreement Proposed Revised Annual Caps from 2017 to 2018 is lower than the expected GDP growth of the PRC in 2017, which is 6.50% forecasted by the IMF; and (ii) the Company expects that the sales volume of harvesting machinery for 2018 will increase from 2017 which will further increase the need of transportation services, we are of the view that the Composite Services Agreement Proposed Revised Annual Cap for the year ending 31 December 2018 is fair and reasonable so far as the Independent Shareholders are concerned.

Given the abovementioned, we are of the view that the Composite Services Agreement Proposed Revised Annual Caps are fair and reasonable so far as the Independent Shareholders are concerned.

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## LETTER FROM VEDA CAPITAL

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### RECOMMENDATION

Having considered the abovementioned principal factors and reasons, we consider (i) the Proposed Revised Annual Caps are on normal commercial terms and are fair and reasonable so far as the Independent Shareholders are concerned; and (ii) the Proposed Revised Annual Caps are in the interests of the Company and the Independent Shareholders as a whole. We would therefore recommend the Independent Shareholders and advise the Independent Board Committee to recommend the Independent Shareholders to vote in favour of the resolutions to approve the proposed Annual Cap amount to be proposed at the AGM.

Yours faithfully,  
For and on behalf of  
**Veda Capital Limited**  
**Julisa Fong**  
*Managing Director*

*Ms. Julisa Fong is a responsible officer under the SFO to engage in Type 6 (advising on corporate finance) regulated activity and has over 20 years of experience in investment banking and corporate finance.*

*\* For identification purpose only*

## 1. RESPONSIBILITY STATEMENT

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

## 2. DISCLOSURE OF INTERESTS

### (i) Interests of Directors, supervisors and chief executive of the Company

Save as disclosed below, as at the Latest Practicable Date, none of the Directors, supervisors or chief executive of the Company had any interest or short position in any Shares, underlying Shares and debentures (as the case may be) of the Company or any associated corporations (within the meaning of Part XV of the SFO) which was required to be (i) 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 which the Directors, supervisors or chief executive of the Company was taken or deemed to have under such provisions of the SFO); or (ii) entered into the register kept by the Company pursuant to section 352 of the SFO; or (iii) notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers as contained in Appendix 10 to the Listing Rules:

| Name        | The Company/<br>associated<br>corporation | Nature of<br>interests | Number of<br>Shares held  | Total number of<br>Shares interested | Percentage of<br>the relevant<br>issued class of<br>share capital<br>(%) | Percentage of<br>the total issued<br>share capital of<br>the Company<br>(%) | Type of<br>Share |
|-------------|---|------------------------|---------------------------|--------------------------------------|--|---|------------------|
| Wu Tak Lung | The Company                               | Beneficial owner       | 10,000<br>(Long position) | 10,000<br>(Long position)            | 0.0025   | 0.0010  | H Share          |

**(ii) Interests of substantial Shareholders and other persons**

Save as disclosed below, as at the Latest Practicable Date, the Directors were not aware of any person (other than the Directors, supervisors or chief executive of the Company) who had any interest or short position in the Shares or underlying Shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who was, directly or indirectly, interested in 10 per cent. (10%) or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of the Group:

| Name             | Capacity         | Number of Shares held <sup>1</sup> | Number of underlying Shares held under equity derivatives <sup>1</sup> | Total number of Shares interested <sup>1</sup> | Percentage of                              | Percentage of                                 | Type of Share |
|------------------|------------------|------------------------------------|--|--|--|---|---------------|
|                  |                  |                                    |  |  | the relevant issued class of share capital | the total issued share capital of the Company |               |
|                  |                  |                                    |  |  | (%)  | (%)   |               |
| YTO <sup>2</sup> | Beneficial owner | 410,690,578 (L)                    | /  | 410,690,578 (L)                                | 69.15 (L)                                  | 41.24 (L)                                     | A Share       |

*Note 1:* (L) – Long position

*Note 2:* Sinomach is the controlling shareholder of YTO. Sinomach is deemed to have the same interest in the Company as those owned by YTO by virtue of the SFO, holding 410,690,578 A Shares of the Company.

Save as disclosed above, there are no other persons (other than the Directors, supervisors or chief executive of the Company) who, as at Latest Practicable Date, had any interest or short position in the Shares or underlying Shares of the Company as recorded in the register required to be kept by the Company under section 336 of the SFO.

**(iii) Directors', supervisors' or chief executive's rights to acquire interests or short positions in Shares and debentures**

As at the Latest Practicable Date, none of the Directors, supervisors or chief executive of the Company or their respective spouse or minor children were granted any rights to acquire benefits by means of acquisition of the Shares in or debentures of the Company or any other body corporate; nor was the Company, its subsidiaries or holding company or any of its subsidiaries a party to any arrangement to enable the Directors, supervisors or chief executive of the Company to acquire such rights in the Company or any other body corporate.



**3. DISCLOSURE OF OTHER INTERESTS****(i) Interests in contract or arrangement**

As at the Latest Practicable Date, none of the Directors or supervisors of the Company was materially interested in any contract or arrangement subsisting at the Latest Practicable Date which was significant in relation to the business of the Group.

**(ii) Interests in assets**

As at the Latest Practicable Date, none of the Directors or supervisors had any direct or indirect interest in any assets which had been acquired or disposed of by, or leased to, or which were proposed to be acquired or disposed of by, or leased to, any member of the Group since 31 December 2016, being the date to which the latest published audited accounts of the Group were made up.

**(iii) Interests in competing business**

As at the Latest Practicable Date, none of the Directors or supervisors or any of their respective close associates was interested in any business apart from the Company's business which competed or was likely to compete, either directly or indirectly, with the Company's business.

**4. DIRECTORS' AND SUPERVISORS' SERVICE CONTRACTS**

As at the Latest Practicable Date, none of the Directors or supervisors of the Company had entered, or proposed to enter, into a service contract with any member of the Group (excluding contracts expiring or determinable by relevant member of the Group within one year without payment of compensation, other than statutory compensation).

**5. MATERIAL ADVERSE CHANGE**

As at the Latest Practicable Date, the Directors were not aware of any material adverse change in the financial or trading position of the Group since 31 December 2016 the date to which the latest published audited consolidated financial statements of the Group were made up.

**6. EXPERT AND CONSENT**

The following is the qualification of the expert who had given opinion or advice which is contained in this circular:

| <b>Name</b>  | <b>Qualification</b>   |
|--------------|--|
| Veda Capital | a licensed corporation to carry on Type 6 (advising on corporate finance) regulated activities under the SFO |

Veda Capital has given and has not withdrawn its written consent to the issue of this circular with the inclusion of its letter and references to its name in the form and context in which it is included.

As at the Latest Practicable Date, Veda Capital did not have any direct or indirect interest in any assets which had since 31 December 2016 (being the date which the latest published audited financial statement of the Group was made up) been acquired or disposed of by, or leased to, or were proposed to be acquired or disposed of by, or leased to, any member of the Group.

As at the Latest Practicable Date, Veda Capital was not beneficially interested in the share capital of any member of the Group nor had any right, whether legally enforceable or not, to subscribe for or to nominate persons to subscribe for securities in any member of the Group.

The letter given by Veda Capital is given as at the date of this circular for incorporation herein.

**7. DOCUMENTS FOR INSPECTION**

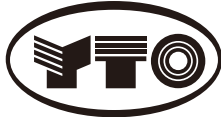
Copies of the following documents will be available for inspection at the office of Messrs. Li & Partners at 22nd Floor, World-Wide House, Central, Hong Kong during normal business hours on any weekday (except public holidays) for a period of 14 days from the date hereof:

- (i) the CCT Agreements;
- (ii) the letter from the Independent Board Committee, the text of which is set out on pages 20 to 21 of this circular;
- (iii) the letter from Veda Capital, the text of which is set out on pages 22 to 55 of this circular;
- (iv) the written consent referred to in the paragraph headed “Expert and Consent” in this Appendix; and
- (v) this circular.

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## NOTICE OF AGM

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# 第一拖拉机股份有限公司\*

## FIRST TRACTOR COMPANY LIMITED\*

*(a joint stock company incorporated in The People's Republic of China with limited liability)*

(Stock Code: 0038)

### NOTICE OF ANNUAL GENERAL MEETING

**NOTICE IS HEREBY GIVEN THAT** the 2016 annual general meeting (the “**AGM**”) of First Tractor Company Limited\* (the “**Company**”) will be held at 2:15 p.m. on 13 June 2017 (Tuesday) at No. 154 Jianshe Road, Luoyang, Henan Province, The People’s Republic of China (the “**PRC**”) for the purpose of considering and, if thought fit, passing the following resolutions:

#### ORDINARY RESOLUTIONS

1. To consider and approve the report of the board (the “**Board**”) of directors (the “**Directors**”) of the Company for the year 2016.
2. To consider and approve the report of the supervisory committee of the Company for the year 2016.
3. To consider and approve the audited financial report of the Company for the year 2016.
4. To consider and approve the dividend distribution proposal of the Company for the year ended 31 December 2016.

The Board recommends the following dividend distribution proposal for 2016: a cash dividend of RMB0.57 (tax inclusive) for every ten shares on the basis of the total share capital of the Company as at the record date for dividend distribution.

5. To consider and approve the re-appointment of ShineWing Certified Public Accountants as the auditor of the Company’s financial report and the internal control auditor for the year 2017, and to authorise the Board of the Company to decide its remuneration with reference to the 2016 remuneration standard.

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## NOTICE OF AGM

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6. To consider and approve the resolution in relation to provision of guarantees for the financial business for the Company's products.

(Provided that the relevant requirements of the Rules Governing the Listing of Stocks on Shanghai Stock Exchange, relevant requirements of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "Listing Rules") (including but not limited to Chapters 14 and 14A) and other relevant requirements are complied with, the Company be hereby approved to provide guarantees for dealers and users which purchase agricultural machinery products from the Company under finance lease, buyer's credit and "Dong Fanghong" commercial loan business and the amount of guarantees actually provided by the Company shall not exceed RMB480 million at any time during the validity period of the guarantees. The proposed guarantees will be available for use on a revolving basis, and the general manager of the Company be hereby authorised to determine the guarantee proposal(s) and to sign relevant documents. The validity period of the aforesaid guarantees is from 13 June 2017 to the date of convening the 2017 annual general meeting of the Company.)

7. To consider and approve the resolution in relation to provision of guarantees by the Company for its subsidiaries, YTO (France) Agricultural Equipment Company Limited\* and Luoyang Changxing Agricultural Machinery Company Limited\*.

(Provided that the relevant requirements of the Rules Governing the Listing of Stocks on Shanghai Stock Exchange, relevant requirements of the Listing Rules (including but not limited to Chapters 14 and 14A) and other relevant requirements are complied with, the Company be hereby approved to provide guarantees for its subsidiaries, YTO (France) Agricultural Equipment Company Limited\* and Luoyang Changxing Agricultural Machinery Company Limited\* and the amount of guarantees actually provided by the Company shall not exceed RMB612.50 million at any time during the validity period of the guarantees. The proposed guarantees will be available for use on a revolving basis. The validity period of the aforesaid guarantees is from 13 June 2017 to the date of convening the 2017 annual general meeting of the Company.)

8. To consider and approve the resolution of the Company in relation to purchase of wealth management products with internal idle funds.

(Provided that the relevant requirements of the Rules Governing the Listing of Stocks on Shanghai Stock Exchange, relevant requirements of the Listing Rules (including but not limited to Chapters 14 and 14A) and other relevant requirements are complied with, the Company be hereby approved that the total amount of wealth management products purchased by using internal idle funds and held by the Company at any time shall be no more than RMB1.8 billion and the total amount of wealth management products purchased from a financial institution and held by the Company at any time shall be no more than RMB800 million. Such caps will be revolving in nature, and the general manager of the Company be hereby authorised to determine the wealth management proposal(s) and to sign relevant documents. The validity period of the aforesaid caps of purchase of wealth management products is from 13 June 2017 to the date of convening the 2017 annual general meeting of the Company.)

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## NOTICE OF AGM

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9. To consider and approve the increase in 2017 and 2018 annual cap amounts of the Material Procurement Agreement of the Company.
10. To consider and approve the increase in 2017 and 2018 annual cap amounts of the Sale of Goods Agreement of the Company.
11. To consider and approve the increase in 2017 and 2018 annual cap amounts of the Composite Services Agreement of the Company.

### SPECIAL RESOLUTIONS

1. To consider and approve the merger and absorption by the Company of its wholly-owned subsidiary, YTO (Luoyang) Drive Axle Company Limited\*.
2. To authorise the Board of the Company to repurchase H shares of the Company (the “**H Shares**”) subject to the following conditions:
  - (a) subject to paragraphs (b), (c) and (d) below, during the Relevant Period (as defined in paragraph (e) below), the Board may exercise all the powers of the Company to repurchase H Shares in issue on The Stock Exchange of Hong Kong Limited (the “**Stock Exchange**”), subject to and in accordance with all applicable laws, rules and regulations and/or requirements of the governmental or regulatory body of securities in the PRC, the Stock Exchange or of any other governmental or regulatory body be and is approved;
  - (b) the authorisation to the Board in respect of the repurchase of H Shares includes but not limited to:
    - (i) formulate and implement specific repurchase proposal, including but not limited to the repurchase price and repurchase amount, and decide the timing of repurchase and time limit;
    - (ii) notify the creditor(s) of the Company and publish announcement(s) in accordance with the Company Law of the PRC and the Articles of Association of the Company;
    - (iii) open offshore securities account and attend relevant registration procedures for foreign exchange;
    - (iv) implement the relevant approval procedures pursuant to the requirements of the regulatory authorities and the listing places, and report to the China Securities Regulatory Commission;

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## NOTICE OF AGM

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- (v) attend the cancellation matters in respect of the repurchased shares, reduce the registered capital, amend the Articles of Association of the Company in relation to the total share capital amount and shareholding structure, and attend the relevant required domestic and overseas registration and reporting procedures; and
  - (vi) execute and handle all other relevant documents and matters in relation to the share repurchase;
- (c) the aggregate nominal value of H Shares authorized to be repurchased pursuant to the approval in paragraph (a) above during the Relevant Period shall not exceed 10 per cent of the aggregate nominal value of H Shares in issue and having not been repurchased as at the date of the passing of this resolution;
- (d) the approval in paragraph (a) above shall be conditional upon:
  - (i) the passing of a special resolution in the same terms as the resolution set out in this paragraph (except for this sub-paragraph (d)(i)) at the class meeting for holders of H Shares of the Company to be held on 13 June 2017 (or on such adjourned date as may be applicable) and at the class meeting for holders of A shares of the Company to be held on 13 June 2017 (or on such adjourned date as may be applicable); and
  - (ii) the approval of the State Administration of Foreign Exchange of the PRC and/or any other regulatory authorities as may be required by the laws, rules and regulations of the PRC being obtained by the Company, if appropriate;
- (e) for the purpose of this special resolution, “Relevant Period” means the period from the passing of this special resolution until whichever is the earlier of:
  - (i) the conclusion of the next annual general meeting following the passing of this special resolution;
  - (ii) the expiry of a period of twelve months following the passing of this special resolution; or
  - (iii) the date on which the authority set out in this special resolution is revoked or varied by a special resolution of the shareholders of the Company in any general meeting or by a special resolution of holders of H Shares or holders of A shares of the Company at their respective class meetings.

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## NOTICE OF AGM

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(For details of the above resolutions, please refer to the announcements of the Company dated 28 February 2017 and 28 March 2017 and the circular of the Company dated 26 April 2017.)

By Order of the Board  
**FIRST TRACTOR COMPANY LIMITED\***  
**YU Lina**  
*Company Secretary*

Luoyang, the PRC  
26 April 2017

*As at the date of this notice, the Board comprises Mr. Zhao Yanshui (Chairman), Mr. Wang Erlong (vice Chairman) and Mr. Wu Yong as executive Directors; Mr. Li Hepeng, Mr. Xie Donggang, Mr. Li Kai and Mr. Yin Dongfang as non-executive Directors; and Ms. Yang Minli, Mr. Xing Min, Mr. Wu Tak Lung and Mr. Yu Zengbiao as independent non-executive Directors.*

*Notes:*

1. The register of members of the Company will be temporarily closed from 13 May 2017 to 12 June 2017 (both days inclusive) during which no transfer of shares of the Company (the “**Shares**”) will be registered in order to determine the list of shareholders of the Company (the “**Shareholders**”) for attending the AGM. The last lodgment for the transfer of the H Shares of the Company should be made on 12 May 2017 at Hong Kong Registrars Limited by or before 4:00 p.m. The Shareholders or their proxies being registered before the close of business on 12 May 2017 are entitled to attend the AGM by presenting their identity documents. The address of Hong Kong Registrars Limited, the H Shares registrar of the Company, is Shops 1712–1716, 17/F., Hopewell Centre, 183 Queen’s Road East, Wanchai, Hong Kong.
2. Each Shareholder having the rights to attend and vote at the AGM is entitled to appoint one or more proxies (whether a Shareholder or not) to attend and vote on his behalf. Should more than one proxy be appointed by one Shareholder, such proxy shall only exercise his voting rights on a poll.
3. Shareholders can appoint a proxy by an instrument in writing (i.e. by using the Proxy Form enclosed). The Proxy Form shall be signed by the person appointing the proxy or an attorney authorised by such person in writing. If the Proxy Form is signed by an attorney, the power of attorney or other documents of authorisation shall be notarially certified. To be valid, the Proxy Form and the notarially certified power of attorney or other documents of authorisation must be delivered to the Company’s registered address at No. 154 Jianshe Road, Luoyang, Henan Province, the PRC, or the Company’s H Shares registrar, Hong Kong Registrars Limited at Shops 1712–1716, 17/F., Hopewell Centre, 183 Queen’s Road East, Wanchai, Hong Kong in not less than 24 hours before the time scheduled for the holding of the AGM or any adjournment thereof.
4. Shareholders who intend to attend the AGM are requested to deliver the duly completed and signed reply slip for attendance to the Company’s registered and principal office in person, by post or by facsimile on or before 4:00 p.m., 23 May 2017.
5. Shareholders or their proxies shall present proofs of their identities upon attending the AGM. Should a proxy be appointed, the proxy shall also present the proxy form.

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## NOTICE OF AGM

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6. The AGM is expected to last for less than one day. The Shareholders and proxies attending the AGM shall be responsible for their own travelling and accommodation expenses.

7. The Company's registered address:

No. 154 Jianshe Road, Luoyang, Henan Province, the PRC

Postal code: 471004

Telephone: (86379) 6496 7038

Facsimile: (86379) 6496 7438

Email: msc0038@ytogroup.com

\* *For identification purposes only*