



23 December 2008

*To the Independent Board Committee and the Independent Shareholders*

Dear Sirs,

**CONNECTED TRANSACTION — SUBSCRIPTION OF SHARES  
BY A CONNECTED PERSON  
AND  
WHITEWASH WAIVER**

**INTRODUCTION**

We refer to our engagement to advise the Independent Board Committee and the Independent Shareholders in respect of the Subscription and the Whitewash Waiver, particulars of which are set out in the letter from the Board (the "Letter from the Board") of the circular to the Shareholders dated 23 December 2008 (the "Circular") and in which this letter is reproduced. Unless the context requires otherwise, capitalised terms used in this letter shall have the same meanings as given to them under the definitions section of the Circular.

As set out in the Letter from the Board, on 1 December 2008, the Company and Huachen, a controlling Shareholder which is interested in approximately 39.41% of the issued share capital of the Company, entered into the Subscription Agreement in relation to the subscription of 1,313,953,488 new Shares at HK\$0.43 each Subscription Share. Immediately following the completion of the Subscription (the "Completion"), Huachen and parties acting in concert with it will be interested in 2,760,074,988 Shares, which represent approximately 55.38% of the issued share capital of the Company as enlarged by the issue of the Subscription Shares. As such, in the absence of the Whitewash Waiver, Huachen would incur an obligation pursuant to Rule 26 of the Takeovers Code to make a mandatory general offer in respect of all the securities of the Company (other than those held by or agreed to be acquired by Huachen and parties acting in concert with it) in accordance with Rule 26 of the Takeovers Code. An application has been made by Huachen to the Executive for the Whitewash Waiver pursuant to the Takeovers Code. The Whitewash Waiver, if granted by the Executive, would be subject to, among other things, the approval of the Independent Shareholders at the SGM by way of poll, which Huachen and parties acting in concert with it will abstain from voting on the relevant resolution. In this regard, Partners Capital International Limited has been appointed as the independent financial adviser to the Independent Board Committee and the Independent Shareholders in relation to the terms of the Subscription and the Whitewash Waiver.

In accordance with Rule 2.1 of the Takeovers Code, the Independent Board Committee, comprising Mr. Xu Bingjin, Mr. Song Jian and Mr. Jiang Bo, was formed to advise the Independent Shareholders in respect of the Subscription and the Whitewash Waiver.

The appointment of Partners Capital International Limited as the independent financial adviser in respect of the Subscription and the Whitewash Waiver has been approved by the Independent Board Committee. In our capacity as the independent financial adviser to the Independent Board Committee and the Independent Shareholders, our role is to provide the Independent Board Committee with an independent opinion as to whether the terms of the Subscription and the grant of the Whitewash Waiver are fair and reasonable so far as the Independent Shareholders are concerned and whether the Subscription and the grant of the Whitewash Waiver are in the interests of the Company and the Shareholders as a whole.

We are not in the same group as the financial or other professional adviser (including a stockbroker) to Huachen or the Company and is not connected with the directors, chief executive and substantial shareholders of the Company and Huachen or any of their respective subsidiaries or their respective associates or their respective party acting, or presumed to be acting, in concert and we had not had, a significant connection, financial or otherwise.



with either Huachen or the Company, or the controlling shareholder(s) of either of them, of a kind reasonably likely to create, or to create the perception of, a conflict of interest or reasonably likely to affect the objectivity of our advice. Therefore, Partners Capital International Limited is considered eligible to give independent advice on the Subscription and the Whitewash Waiver. Apart from normal professional fees payable to us in connection with this appointment, no arrangement exists whereby we will receive any fees or benefits from the Company or the directors, chief executive and substantial shareholders of the Company or any of its subsidiaries or their respective associates.

In formulating our opinion, we have relied on the accuracy of the information and representations contained in the Circular and have assumed that all information and representations made or referred to in the Circular were true, accurate and complete in all material aspects at the time they were made and continue to be true, accurate and complete in all material aspects as at the date of the Circular. We have also relied on our discussion with the management of the Company regarding the Group and the respective terms and conditions of the Subscription, including the information and representations contained in the Circular. We have also assumed that all statements of belief, opinion and intention made by the Directors and the Company in the Circular were reasonably made after due enquiry. We consider that we have reviewed sufficient information to reach an informed view, to justify our reliance on the accuracy of the information contained in the Circular and to provide a reasonable basis for our advice. We have no reason to suspect that any material facts have been omitted or withheld from the information contained or opinions expressed in the Circular nor to doubt the truth, accuracy and completeness of the information and representations provided to us by the Directors. We have not, however, conducted an independent in-depth investigation into the business and affairs of the Group, Huachen and their respective associates nor have we carried out any independent verification of the information supplied.

#### PRINCIPAL FACTORS AND REASONS CONSIDERED

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

##### 1. Review of financial performance

The following is a summary of the financial results of the Group for each of the three years ended 31 December 2007 and the six months ended 30 June 2008:

	Year ended 31 December			Six months ended
	2005	2006	2007	30 June 2008
	(Audited)	(Audited)	(Audited)	(Unaudited)
	RMB'000	RMB'000	RMB'000	RMB'000
Turnover	5,468,990	10,484,754	14,149,149	5,210,123
Profit/(loss) before taxation	(1,156,445)	(656,764)	211,567	244,290
Profit/(loss) attributable to Shareholders	(649,608)	(398,422)	97,086	282,943
Earnings/(loss) per Share (RMB)				
— Basic	(0.1771)	(0.1086)	0.02646	0.07710
Net tangible assets attributable to Shareholders	5,177,466	4,786,652	4,699,482	4,952,256
Net tangible assets attributable to Shareholders per Share (RMB) (Note)	1.411	1.304	1.281	1.349

Source: annual reports of the Company for each of the three years ended 31 December 2007 and interim report of the Company for the six months ended 30 June 2008.

Note: calculated based on the total number of Shares as at the date of the Announcement of 3,669,765,900 Shares.



• *Audited consolidated results for the year ended 31 December 2005*

For the year ended 31 December 2005, the Group recorded a turnover of approximately RMB5,469.0 million, representing a drop of approximately 16.4% as compared with that of the preceding financial year ended 31 December 2004. For the same financial year, the Group recorded a net loss attributable to Shareholders of approximately RMB649.6 million as compared to the net profit attributable to Shareholders of approximately RMB48.6 million for the year ended 31 December 2004.

According to the annual report of the Company for the year ended 31 December 2005, the decrease in sales was primarily due to a decrease in average unit selling prices and volume of Shenyang Automotive's minibuses and Zhonghua sedans in 2005. Shenyang Automotive sold approximately 60,000 minibuses in 2005, representing a decrease of approximately 2.6% from approximately 61,630 minibuses sold in 2004. In addition, Shenyang Automotive sold approximately 9,000 Zhonghua sedans in 2005, representing a decrease of approximately 18.0% from approximately 10,980 sedans sold in 2004.

Cost of sales decreased by approximately 9.5% from approximately RMB5,487.0 million in 2004 to approximately RMB4,964.8 million in 2005. The decrease was primarily due to the decrease in unit sales of minibuses and Zhonghua sedans. Furthermore, the unit production costs of minibuses have decreased as a result of the reduction of materials and component costs in 2005. The overall gross profit margin of the Group decreased from approximately 16.1% in 2004 to approximately 9.2% in 2005.

Other operating expenses increased by approximately 26.2% from approximately RMB70.6 million in 2004 to approximately RMB89.1 million in 2005. The increase was mainly due to the impairment loss of certain fixed assets in two of the subsidiaries. In addition, the Group recognised an impairment loss on goodwill in a subsidiary in the amount of RMB50.0 million in 2005. Moreover, interest expense net of interest income increased by approximately 41.2% from approximately RMB123.7 million in 2004 to approximately RMB174.7 million in 2005. The increase was mainly due to the increase in effective finance expenses from the convertible bonds due 2008 resulting from the adoption of the new Hong Kong Accounting Standard 39 in 2005. As a result, the Group recorded a loss attributable to equity holders of the Company of approximately RMB649.6 million in 2005 as compared to a profit attributable to equity holders of the Company of approximately RMB48.6 million in 2004.

• *Audited consolidated results for the year ended 31 December 2006*

For the year ended 31 December 2006, the Group recorded a turnover of approximately RMB10,484.8 million, representing an increase of approximately 91.7% as compared with that for the year ended 31 December 2005. For the same financial year, the Group recorded a net loss attributable to Shareholders of approximately RMB398.4 million as compared to the net loss attributable to Shareholders of approximately RMB649.6 million for the year ended 31 December 2005.

According to the annual report of the Company for the year ended 31 December 2006, the increase in sales was primarily due to increases in unit sales of Shenyang Automotive's minibuses and, especially, Zhonghua sedans in 2006. Shenyang Automotive sold 66,245 minibuses in 2006, representing an increase of approximately 10.4% from approximately 60,000 minibuses sold in 2005 whilst Shenyang Automotive sold 62,281 Zhonghua sedans in 2006, representing an increase of approximately 592.0% from approximately 9,000 sedans sold in 2005. Despite the increase in sales and decrease in unit costs, the overall gross profit margin of the Group decreased from approximately 9.2% in 2005 to approximately 5.4% in 2006, as a result of the significant increase in sales of Zhonghua sedans which have yet to reach profitability in 2006, as well as a shift in product mix to lower-margin products.



Other revenue increased by approximately 114.3% from approximately RMB135.9 million in 2005 to approximately RMB291.2 million in 2006. The increase was primarily due to the increase in sales of scrap materials. In addition, the Group's share of operating results of associates and jointly controlled entities (excluding an impairment loss on goodwill in a jointly controlled entity) increased by approximately 204.7% from approximately RMB49.0 million in 2005 to approximately RMB149.3 million in 2006. This was mainly attributable to the increased profits contributed by BMW Brilliance Automotive Ltd. ("BMW Brilliance"), the Group's 49.5% indirectly owned jointly controlled entity, and an associate in 2006. The Group also recognised an impairment loss on goodwill in a jointly controlled entity in the amount of approximately RMB73.3 million in 2006 in relation to one of the Group's engine joint ventures. Net profits contributed to the Group by BMW Brilliance increased by approximately 237.7% from approximately RMB31.6 million in 2005 to approximately RMB106.7 million in 2006. The BMW joint venture achieved sales of 23,600 BMW sedans in 2006, an increase of approximately 34.8% as compared to 17,501 BMW sedans in 2005. As a result, the Group's loss attributable to equity holders of the Company decreased by approximately 38.7% from approximately RMB649.6 million in 2005 to approximately RMB398.4 million in 2006.

• *Audited consolidated results for the year ended 31 December 2007*

For the year ended 31 December 2007, the Group recorded a turnover of approximately RMB14,149.1 million, representing an increase of approximately 34.9% as compared with that of the preceding financial year. For the same financial year, the Group recorded a net profit attributable to Shareholders of approximately RMB97.1 million as compared to the net loss attributable to Shareholders of approximately RMB398.4 million for the year ended 31 December 2006.

According to the annual report of the Company for the year ended 31 December 2007, the increase in sales was primarily due to increases in unit sales of Shenyang Automotive's Zhonghua sedans and minibuses in 2007. Shenyang Automotive sold 73,415 minibuses in 2007, representing an increase of approximately 10.8% from 66,245 minibuses sold in 2006 whilst Shenyang Automotive sold 106,770 Zhonghua sedans in 2007, representing an increase of approximately 71.4% from 62,281 sedans sold in 2006.

Cost of sales rose by approximately 30.9% from approximately RMB9.9 billion in 2006 to approximately RMB13.0 billion in 2007. The increase was primarily due to the increase in unit sales of both the Zhonghua sedans and minibuses. The average unit cost for both the Zhonghua sedans and minibuses decreased in 2007, mainly due to improvement in production efficiency together with the decrease in unit cost of components due to economies of scale. As a result, the overall gross profit margin of the Group improved from approximately 5.2% in 2006 to approximately 8.0% in 2007.

Other revenue increased by approximately 26.8% from approximately RMB291.2 million in 2006 to approximately RMB369.2 million in 2007. The increase was primarily due to the increase in sales of scrap materials and incentives provided by the government. General and administrative expenses decreased by approximately 18.5% from approximately RMB632.7 million in 2006 to approximately RMB515.6 million in 2007, mainly as a result of increased capitalization of research and development costs incurred during the year as well as certain bad debt write offs which were recorded in 2006.

Net finance costs decreased by approximately 38.7% from approximately RMB201.3 million in 2006 to approximately RMB123.3 million in 2007 due to reduced short-term borrowing in 2007 as well as higher foreign exchange gains realized from our U.S. dollar denominated Convertible Bonds. The Group's share of operating results of associates and jointly controlled entities increased by approximately 28.8% from approximately RMB149.3 million in 2006 (excluding an impairment loss on goodwill in a jointly controlled entity) to approximately RMB192.3 million in 2007. This was mainly attributable to the increased profits contributed by BMW Brilliance. As a result, the Group recorded a profit before taxation amounting to approximately RMB211.6 million in 2007 and recorded a net profit attributable to Shareholders of approximately RMB97.1 million as compared to the net loss attributable to Shareholders of approximately RMB398.4 million for the year ended 31 December 2006.



- *Unaudited consolidated results for the six months ended 30 June 2008*

For the six months ended 30 June 2008, the turnover of the Group dropped by 32.7% to approximately RMB5,210.1 million when compared with that of the preceding corresponding period. During the same period, the Group recorded a net profit attributable to Shareholders of approximately RMB282.9 million as compared to the net loss attributable to Shareholders of approximately RMB125.7 million for the six months ended 30 June 2007.

According to the interim report of the Company for the six months ended 30 June 2008, the decrease in turnover was primarily due to a decrease in unit sales of Shenyang Automotive's Zhonghua sedans during the period in 2008. Shenyang Automotive sold 33,520 minibuses in the first half of 2008, representing a decrease of approximately 4.3% from 35,038 units sold during the same period in 2007 whilst Shenyang Automotive sold 33,221 Zhonghua sedans in the first half of 2008, representing a decrease of approximately 44.9% from 60,287 units sold during the corresponding period last year. The overall unaudited gross profit margin of the Group decreased to approximately 5.6% for the first half of 2008 from approximately 7.3% in the same period in 2007. The Zhonghua sales volume fell below its breakeven level in the first half of 2008, resulting in a loss for that segment and a lower gross margin overall.

Unaudited other revenue decreased by approximately 37.9% from approximately RMB169.6 million in the first six months of 2007 to approximately RMB105.3 million for the same period in 2008. The decrease was primarily due to the decrease in sales of scrap materials and subsidy income recognised during the period. The Group's unaudited share of operating results of associates and jointly controlled entities increased by approximately 42.9% from approximately RMB90.4 million in the first half of 2007 to approximately RMB129.2 million for the same period in 2008. This was mainly attributable to the increased profits contributed by BMW Brilliance in the first half of 2008. Unaudited net profits contributed to the Group by BMW Brilliance increased by approximately 106.8% from approximately RMB53.0 million in the first half of 2007 to approximately RMB109.6 million for the same period this year. The BMW joint venture achieved sales of 16,543 BMW sedans in the first six months of 2008, an increase of approximately 1.7% as compared to 16,260 BMW sedans for the same period in 2007. The higher net profits contributed to the Group in the first half of 2008 was mainly a result of reduced tariffs on imported components and reduced expenses incurred for component localisation.

In the first half of 2008, the Group recognised a gain of RMB215.0 million on the change in fair value of the embedded conversion option of the convertible bonds in accordance with Hong Kong Financial Reporting Standards. This compares to a loss of RMB282.5 million recorded in the first half of 2007. The gain resulted from the change in fair value during the period was primarily due to a drop in the Company's share price between 31 December 2007 and 30 June 2008. As a result, the Group recorded an unaudited profit attributable to equity holders of the Company of approximately RMB282.9 million for the first half of 2008 as compared to the net loss attributable to Shareholders of approximately RMB125.7 million for the six months ended 30 June 2007.

- *Further analysis*

As set out in the Letter from the Board, the Group is engaged in the manufacture and sale of minibuses and automotive components and sedans. As advised by the Company, the Group intended to extend its auto business chain downstream into the aftermarket sector in 2008. The Group suffered significant losses during the two financial years ended 31 December 2005 and 31 December 2006 but achieved a turnaround since 2007.

According to the statistics from the China Association of Automobile Manufacturers (中國汽車工業協會) of the PRC, the total number of sedans sold for the nine months ended 30 September 2008 amounted to approximately 3.8 million vehicles, representing an increase of approximately 10.2% from that of the corresponding period in year 2007. During the same period, the total number of automobiles



exported from the PRC amounted to approximately 557,500 vehicles representing an increase of approximately 34.7% from that of the corresponding period in year 2007. In addition, the monthly sales and production of automobile of the PRC in October 2008 amounted to approximately 0.72 million vehicles and approximately 0.70 million vehicles respectively, representing an increase of approximately 3.37% and a reduction of approximately 1.15% as compared to those of the corresponding period in year 2007 respectively.

On the other hand, according to Autodata, a leading publisher and supplier of technical information for automotive professionals, the monthly retail sales of light vehicles of United States of America in November 2008 amounted to 746,789 vehicles, representing a significant decrease of approximately 36.7% as compared to that of the corresponding period in year 2007. Besides, according to the statistics from Japan Automobile Dealers Association, the monthly sales of new automobile in Japan in November 2008 amounted to 215,783 vehicles, representing a decrease of approximately 27.3% as compared to that of the corresponding period in year 2007. Such level of November sales volume was the lowest since 1969. Furthermore, according to the Committee of French Automobile Manufacturers, the new cars registration in France amounted to 145,918 vehicles, representing a decline of approximately 14% as compared to that of the corresponding period in year 2007. Based on the above, we consider that the automobile markets worldwide showed signs of slowing down and even recession. Based on our discussion with the Company, the Directors expect that market conditions will remain challenging in the near future as a result of credit tightening and slower economic growth.

Based on the above, we concur with the Directors' view that the automobile market in the PRC will be highly likely to remain challenging and we consider that there is an uncertainty as to whether the Group can sustain its profitability in future given the current market conditions.

## **2. Background of and reasons for the Subscription**

As set out in the Letter from the Board, the Group is engaged in the manufacture and sale of minibuses and automotive components and sedans. The Group would like to raise funds to reduce debt and increase working capital to improve its liquidity and cash flow position. The price of the Shares has been adversely impacted by the current financial turmoil and negative market sentiment. Huachen is prepared to subscribe for the Subscription Shares at a premium to the trading price of the Shares and inject cash to further support the business of the Group. The Subscription will provide the Group with additional cash to strengthen its financial position and to better equip the Group in weathering through the current economic downturn.

As such, by entering into the Subscription Agreement with Huachen to raise net proceeds in the amount of approximately RMB490 million (equivalent to approximately HK\$553.7 million) which will be used to reduce the outstanding indebtedness of the Group and for working capital of Shenyang Automotive, we consider that it represents a valuable opportunity for the Group to raise additional funding and is beneficial to the Company and Shareholders as a whole.

As set out in the interim report of the Company for the six months ended 30 June 2008, on 7 June 2006, the Group, through a wholly-owned subsidiary, Brilliance China Finance Limited ("BCF"), issued the Convertible Bonds with principal amount of US\$182,678,000 (equivalent to approximately RMB1,461 million based on the applicable exchange rate at the time of issue). The Convertible Bonds are listed on the Singapore Exchange Securities Trading Limited. The Convertible Bonds are convertible into fully paid ordinary shares at par value of US\$0.01 each of the Company at an initial conversion price of HK\$1.93 per share, subject to adjustment in certain events, at any time on or after 6 July 2006, and up to and including 8 May 2011, unless the Convertible Bonds have previously been redeemed or previously have matured. Pursuant to the terms of the Convertible Bonds, the initial conversion price of HK\$1.93 was adjusted to HK\$1.53 with effect from 10 March 2008. The Convertible Bonds will mature on 7 June 2011. All but not some of the aggregate outstanding principal amount of the Convertible Bonds is redeemable at the option of BCF at the early redemption amount (calculated at principal amount of the Convertible Bonds plus a yield at 7% per annum, compounded semi-annually) if certain event(s) occurred.



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On the other hand, the Convertible Bonds may be redeemed in whole but not in part at the option of the relevant holders on 7 June 2009 at 122.926% of their respective principal amount. To exercise such right, the holders of the Convertible Bonds must complete, sign and deposit at the specified office of any paying agent a duly completed and signed notice of redemption, in the then current form obtainable from the specified office of any paying agent together with the certificate evidencing the Convertible Bonds to be redeemed not earlier than 60 days and not later than 30 days prior to 7 June 2009. In addition, the Convertible Bonds may also be redeemed in whole but not in part at the option of the holders at the early redemption amount on the occurrence of a change of control of the Company, or if the Shares cease to be listed or admitted to trading in the Stock Exchange.

In view of the current economic condition, the current outlook of the automobile market in 2009 and the expected stock market sentiment in 2009, the Company expects that it is unlikely that the price of the Shares would stay above the conversion price of HK\$1.53, which represents a premium of 292.3% over the closing price of HK\$0.39 per Share for the morning trading session on 1 December 2008, the date of the Subscription Agreement, by 7 June 2009 and the holders of the Convertible Bonds would highly likely exercise their options to request for redemption (the "Forced Redemption") by the Company. As at 30 June 2008, the Group had cash and cash equivalents and short-term bank deposits in the amount of approximately RMB1,634.4 million (equivalent to approximately HK\$1,846.9 million) and capital commitment contracted for but not provided for in the amount of RMB615.8 million (equivalent to approximately HK\$695.9 million) respectively. In the event that all of the holders of the Convertible Bonds exercise their options to request for redemption by the Company, the Company expects that there would be a substantial drawing of cash of the Company by that time in the amount of approximately RMB1,527.0 million (which was calculated based on the rate of the Forced Redemption at 122.926% and the principal of amount of US\$182,678,000 (equivalent to approximately RMB1,242.2 million based on the applicable exchange rate of approximately RMB6.8 to US\$1 as at the Latest Practicable Date)). Based on the aggregate cash and cash equivalents available of approximately RMB1,634.4 million as at 30 June 2008, but without taking into account any further movement in the cash balance subsequent to 30 June 2008, and assuming all the holders of the Convertible Bonds opt for the Forced Redemption, the Group may be short of working capital as a result of the Forced Redemption. Therefore, the Directors are taking a proactive step to secure additional funding to prepare for the possible Forced Redemption by way of the Subscription. The aggregate of the proceeds of RMB500 million from the Subscription and the aggregate cash balance of approximately RMB1,634.4 million as at 30 June 2008 would be sufficient to settle the cash required for the possible Forced Redemption but the Company may be unable to fulfill its other payment obligations if there were not enough cash inflow from operations and/or other means before 7 June 2009. Nevertheless, the completion of the Subscription would improve the Company's potential cash flow problem.

On the other hand, we were advised by the Directors that they had considered various financing alternatives for raising additional fund, including arrangement of new bank loans, placing of new shares, rights issue and etc. However, taking on additional bank borrowings may increase the Group's current gearing ratio and it is difficult to obtain facilities from banks in light of the current financial turmoil and negative market sentiment. On the other hand, rights issue may incur substantial costs to the Company in the form of underwriting commission, as a typical rights issue or open offer would involve engagement of underwriter. The substantial cost may not be favourable to the Company and the Independent Shareholders and it is also difficult to find an underwriter under the current market conditions. In addition, we observed that rights issue often involve a discount in the subscription price, which may have an adverse impact on the Shares. Furthermore, the Company has endeavoured to procure for independent investors for the Company from time to time but in light of the current market conditions, no investment plan could materialise with the independent investors. In light of the above and in view that the issue of the Subscription Shares will enlarge and strengthen the capital base of the Company, the Directors consider that the Subscription is the best financing alternative available to the Company at the moment to finance the reduction of the outstanding indebtedness of the Group and increase the working capital of Shenyang Automotive.



We concur with the Directors' view and consider that the Subscription represents the best available option to obtain additional funding and working capital in light of the current financial turmoil and negative market sentiment and we consider that the Subscription serves as an acceptable means to furnish the Group with additional funding for the possible Forced Redemption and is beneficial to the Company and Shareholders as a whole.

### 3. Terms of the Subscription

#### (i) *Share price performance and trading liquidity*

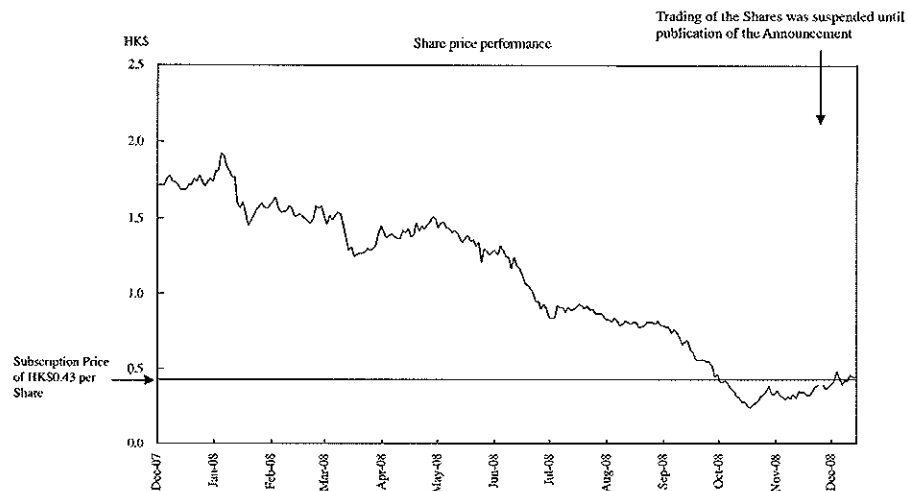
Pursuant to the Subscription Agreement, the Subscription Price of HK\$0.43 each Subscription Share was determined after arm's length negotiations between the Company and Huachen. The net price of each Subscription Share is HK\$0.42. The Subscription Monies in the total amount of approximately RMB500 million (equivalent to approximately HK\$565 million) is to be settled in cash by Huachen by not later than the date of completion of the Subscription. We note that the Subscription Price represents:

- (a) a premium of approximately 10.3% over the closing price of HK\$0.39 per Share for the morning trading session on 1 December 2008, the date of the Subscription Agreement;
- (b) a premium of approximately 13.2% over the closing price of HK\$0.38 per Share as quoted on the Stock Exchange on the Last Trading Day;
- (c) a premium of approximately 24.6% over the average closing price of HK\$0.345 per Share as quoted on the Stock Exchange for the 5 consecutive trading days up to and including the Last Trading Day;
- (d) a premium of approximately 28.0% over the average closing price of HK\$0.336 per Share as quoted on the Stock Exchange for the 10 consecutive trading days up to and including the Last Trading Day;
- (e) a premium of approximately 35.2% over the average closing price of approximately HK\$0.318 per Share as quoted on the Stock Exchange for the 30 consecutive trading days up to and including the Last Trading Day;
- (f) a discount of approximately 70.3% to the audited consolidated net tangible asset value per Share of approximately RMB1.281 per Share (equivalent to approximately HK\$1.448 per Share) as at 31 December 2007 as announced by the Company;
- (g) a discount of approximately 71.8% to the unaudited consolidated net tangible asset value per Share of approximately RMB1.349 per Share (equivalent to approximately HK\$1.524 per Share) as at 30 June 2008 as announced by the Company; and
- (h) a discount of approximately 3.4% to the closing price of HK\$0.445 per Share as quoted on the Stock Exchange on the Latest Practicable Date.



- *Share price performance*

In view that the 12-month benchmarking period is a commonly used tenure for analysis purpose, we consider that it is relevant to review the closing price level of the Shares traded on the Stock Exchange during the 12 month period from 1 December 2007 to 28 November 2008 (being the Last Trading Day) and further up to the Latest Practicable Date (the "Review Period") as follows:



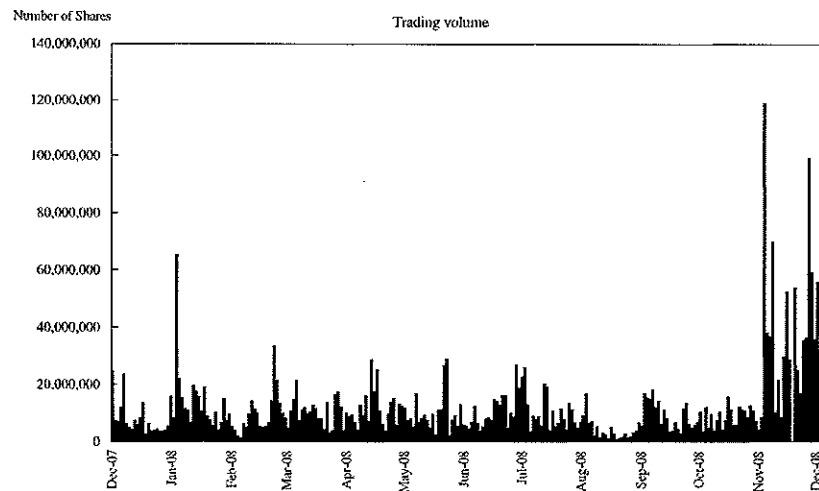
Source: Infocast

During the Review Period, the lowest closing price was HK\$0.242 per Share recorded on 27 October 2008 and the highest closing price was HK\$1.92 per Share recorded on 8 January 2008. The Shares had been traded above the Subscription Price of HK\$0.43 per Share during the first ten months of the Review Period from December 2007 to early October 2008, with a range from approximately HK\$0.45 to HK\$1.92 per Share. The share price was generally declining during the Review Period and the share price reached a bottom of HK\$0.242 on 27 October 2008. Thereafter, the share price started to rebound. The trading of the Shares was suspended with effect from 2:30 pm on 1 December 2008 pending the publication of the Announcement and the trading of the Shares resumed on 3 December 2008. The Subscription Price represents a premium of approximately 77.7% over the lowest closing price per Share and a discount of approximately 77.6% to the highest closing price per share during the Review Period. The Subscription Price also represents a discount of approximately 3.4% to the closing price of the Shares of HK\$0.445 on the Latest Practicable Date.



• *Liquidity*

For the purpose of assessing the trading liquidity of the Shares, the following chart shows the daily trading volume of the Shares during the Review Period:



Source: Infocast

Month	Highest daily turnover (in number of Shares)	Lowest daily turnover (in number of Shares)	Average daily turnover (in number of Shares)	Number of trading days with no turnover (in days)	Percentage of average daily turnover over total number of Shares in issue (note 1) (%)	Percentage of average daily turnover over total number of Shares held by the Independent Shareholders (note 2) (%)
<b>2007</b>						
December	24,734,894	2,828,000	8,117,127	0	0.221%	0.365%
<b>2008</b>						
January	65,506,000	3,956,000	13,989,009	0	0.381%	0.629%
February	33,712,000	1,312,000	9,392,302	0	0.256%	0.422%
March	21,507,500	3,274,000	10,305,231	0	0.281%	0.463%
April	28,722,744	3,771,490	11,436,294	0	0.312%	0.514%
May	26,782,000	2,544,000	10,394,637	0	0.283%	0.467%
June	28,984,750	2,134,000	9,211,885	0	0.251%	0.414%
July	26,996,298	3,652,000	12,592,767	0	0.343%	0.566%
August	16,826,480	1,316,000	6,239,918	0	0.170%	0.281%
September	18,282,000	938,000	7,319,432	0	0.199%	0.329%
October	15,726,000	2,922,000	7,761,332	0	0.211%	0.349%
November	119,312,000	4,216,000	24,276,985	0	0.662%	1.092%
December (1 December morning trading session and 3 December to the Latest Practicable Date)	99,420,000	16,932,700	47,943,637	0	1.306%	2.156%

Source: Infocast

Notes:

1. Based on the total number of issued Shares of 3,669,765,900 Shares as at the date of the Announcement.



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2. Based on the total number of Shares held by the Independent Shareholders of 2,223,644,400 Shares as at the Latest Practicable Date.

During the Review Period, save for the period during the afternoon trading session on 1 December 2008 to 2 December 2008, there was trading of the Shares on every trading day on the Stock Exchange. However, as illustrated in the table above, the trading volume of the Shares during the Review Period has been generally thin. During the period from January 2008 to July 2008, the daily average trading volume amounted to roughly 10 million Shares, representing approximately 0.27% of the total number of issued Shares and approximately 0.45% of the total number of Shares held by the Independent Shareholders respectively. During the period from August 2008 to October 2008, the highest daily average trading volume amounted to 7.7 million Shares recorded in October 2008, only representing approximately 0.21% of the total number of issued Shares and approximately 0.35% of the total number of Shares held by the Independent Shareholders respectively. Despite the relatively higher trading volume in November 2008 (especially on 18, 21 and 28 November 2008) and after publication of the Announcement, we consider the liquidity of the Shares was generally thin during most of the time in the Review Period.

(ii) *Comparison of Subscription Price with comparables*

• *Price/earnings multiple*

As the Group is engaged in the manufacture and sale of minibuses and automotive components and sedans, reference to price/earnings multiple is the most common approach adopted by the investment community in valuing such kind of revenue-generating entities. For the purpose of assessing the reasonableness of the Subscription Price by reference to the price/earnings multiple, we have identified (to the best of our knowledge) eight companies listed on the Main Board of the Stock Exchange which are principally engaged in the manufacture and sales of automobile in the PRC (the "Comparables") and such list of Comparables represents an exhaustive list and the businesses of the Comparables are closely comparable to that of the Company. The details of the Comparables are set out below:

Company name	Year end date	Closing share price as at 28 November 2008 (HK\$)	Approximate Market Capitalisation (HK\$ million)	Latest published earnings per share (HK\$)	Price/earnings multiple (times)
AviChina Industry & Technology Company Limited	31 December	0.630	2,925.5	(0.250)	N/A
Denway Motors Limited	31 December	2.000	15,037.4	0.326	6.13
Dongfeng Motor Group Company Limited	31 December	1.760	15,164.4	0.494	3.56
Geely Automobile Holdings Limited	31 December	0.485	2,522.5	0.064	7.58
Great Wall Motor Company Limited	31 December	2.230	2,442.5	1.026	2.17
Qingling Motors Company Limited	31 December	0.710	1,762.4	0.072	9.86
Sinotruk (Hong Kong) Limited	31 December	4.540	10,329.4	0.801	5.67
Weichai Power Company Limited	31 December	13.100	6,820.6	3.079	4.25
				Mean	5.60
				Median	5.67
<i>The Company</i>	<i>31 December</i>	<i>0.38</i>	<i>1,394.5</i>	<i>0.030</i>	<i>12.67</i>
<i>Subscription Price (HK\$)</i>		<i>0.43</i>		<i>0.030</i>	<i>14.33</i>

Source: [www.hkex.com.hk](http://www.hkex.com.hk) and Infocast



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

Upon comparison, we note that the price/earnings multiple represented by the Subscription Price of 14.33 times lies well above the range of the price/earnings multiples of the Comparables from 2.17 times to 9.86 times and lies well above the mean and median of those of the Comparables, which were calculated with reference to the respective closing price of the shares of the Comparables as at 28 November 2008, being the last full trading day prior to the signing of the Subscription Agreement.

For further comparison, we set out below the price/earnings multiples of the Comparables calculated with reference to the respective average closing share price of the Comparables for the 180 consecutive trading days up to and including 28 November 2008:

Company name	Year end date	Average closing share price as quoted on the Stock Exchange for the 180 consecutive trading days up to and including 28 November 2008 (HK\$)	Approximate Market Capitalisation based on average closing price (HK\$ million)	Latest published earnings per share (HK\$)	Price/earnings multiple (times)
AviChina Industry & Technology Company Limited	31 December	1.16	5,386.6	(0.250)	N/A
Denway Motors Limited	31 December	2.90	21,804.2	0.326	8.90
Dongfeng Motor Group Company Limited	31 December	3.18	27,399.3	0.494	6.44
Geely Automobile Holdings Limited	31 December	0.74	3,848.8	0.064	11.56
Great Wall Motor Company Limited	31 December	5.41	5,925.4	1.026	5.27
Qingling Motors Company Limited	31 December	1.15	2,854.6	0.072	15.97
Sinotruk (Hong Kong) Limited	31 December	7.15	16,267.7	0.801	8.93
Weichai Power Company Limited	31 December	20.06	10,444.3	3.079	6.52
				Mean	9.08
				Median	8.90
<i>The Company</i>	<i>31 December</i>	<i>0.93</i>	<i>3,412.9</i>	<i>0.030</i>	<i>31.00</i>
<i>Subscription Price (HK\$)</i>		<i>0.43</i>		<i>0.030</i>	<i>14.33</i>

Source: [www.hkex.com.hk](http://www.hkex.com.hk) and Infocast

Upon comparison, we note that the price/earnings multiple represented by the Subscription Price of 14.33 times lies within the range of the price/earnings multiples of the Comparables from 5.27 times to 15.97 times and lies well above the mean and median of those of the Comparables, which were calculated with reference to the respective average closing share price of the Comparables as quoted on the Stock Exchange for the 180 consecutive trading days up to and including 28 November 2008, being the last full trading day prior to the signing of the Subscription Agreement.



• *Net asset value*

In addition to price/earnings multiple, we also assess the Subscription Price by reference to the net asset value as it is also common in the investment community to value a company by reference to its net asset value. However, we consider that Independent Shareholders should focus on the profitability and/or earning potential of a company principally engaged in manufacturing due to its recurring revenue generating nature. Besides, the size of the net asset value may not have direct linkage to the profitability and/or earning potential of such company. Although it may not be most relevant to value a company principally engaged in manufacturing by reference to its net assets in general, we consider that it provides another angle for analysis and we have reviewed and tabulated below the premium/(discounts) of the closing share prices of the Comparables as at 28 November 2008 over/(to) their respective net tangible asset value as reported in their latest published financial reports:

Company name	Year end date	Closing share price as at 28 November 2008 (HK\$)	Latest published net tangible asset value per share (HK\$)	Premium/(discount) of the closing share price on 28 November 2008 over/(to) the latest published net tangible asset value per share
AviChina Industry & Technology Company Limited	31 December	0.630	0.66	(4.58)%
Denway Motors Limited	31 December	2.000	1.69	18.17%
Dongfeng Motor Group Company Limited	31 December	1.760	2.33	(24.49)%
Geely Automobile Holdings Limited	31 December	0.485	0.52	(7.32)%
Great Wall Motor Company Limited	31 December	2.230	6.84	(67.39)%
Qingling Motors Company Limited	31 December	0.710	3.09	(77.06)%
Sinotruk (Hong Kong) Limited	31 December	4.540	5.76	(21.21)%
Weichai Power Company Limited	31 December	13.100	14.98	(12.52)%
			Mean	(24.55)%
			Median	(16.87)%
<i>The Company</i>	<i>31 December</i>	<i>0.38</i>	<i>1.52</i>	<i>(75.08)%</i>
<i>Subscription Price (HK\$)</i>		<i>0.43</i>	<i>1.52</i>	<i>(71.71)%</i>

Source: [www.hkex.com.hk](http://www.hkex.com.hk) and Infocast

The premium/(discounts) of the closing share prices as at 28 November 2008, being the last full trading day prior to the signing of the Subscription Agreement, over/(to) the net tangible asset value per share of the Comparables range from a discount of approximately 77.06% to a premium of approximately 18.17%. We note that the shares of the majority of the Comparables have been trading at discounts to their respective net tangible asset value per share and the Shares have been also trading at discount to net tangible asset value per Share.

Upon comparison, we note that the discount of the Subscription Price to the unaudited consolidated net tangible asset value per Share as at 30 June 2008 of approximately 71.71% lies at the low end of the range of those of the Comparables and falls below the median of those of the Comparables. We also note that the discounts of share price to the respective consolidated net tangible asset value per share of half of the Comparables fall below the median of those of the Comparables.



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

For further comparison, we set out below the premium/(discounts) of the respective average closing share price of the Comparables for the 180 consecutive trading days up to and including 28 November 2008 of the Comparables over/(to) their respective net tangible asset value as reported in their latest published financial reports

Company name	Year end date	Average closing share price as quoted on the Stock Exchange for the 180 consecutive trading days up to and including 28 November 2008 (HK\$)	Latest published net tangible asset value per share (HK\$)	Premium/(discount) of the average closing share price as quoted on the Stock Exchange for the 180 consecutive trading days up to and including 28 November 2008 over/(to) the latest published net tangible asset value per share
AviChina Industry & Technology Company Limited	31 December	1.16	0.66	75.69%
Denway Motors Limited	31 December	2.90	1.69	71.35%
Dongfeng Motor Group Company Limited	31 December	3.18	2.33	36.43%
Geely Automobile Holdings Limited	31 December	0.74	0.52	25.14%
Great Wall Motor Company Limited	31 December	5.41	6.84	(20.90)%
Qingling Motors Company Limited	31 December	1.15	3.09	(62.84)%
Sinotruk (Hong Kong) Limited	31 December	7.15	5.76	24.08%
Weichai Power Company Limited	31 December	20.06	14.98	33.95%
			Mean	22.86%
			Median	29.55%
<i>The Company</i>	<i>31 December</i>	<i>0.93</i>	<i>1.52</i>	<i>(39.01)%</i>
<i>Subscription Price (HK\$)</i>		<i>0.43</i>	<i>1.52</i>	<i>(71.71)%</i>

Source: [www.hkex.com.hk](http://www.hkex.com.hk) and Infocast

The premia/(discounts) of the average closing share price as quoted on the Stock Exchange for the 180 consecutive trading days up to and including 28 November 2008, being the last full trading day prior to the signing of the Subscription Agreement, over/(to) the net tangible asset value per share of the Comparables range from a discount of approximately 62.84% to a premium of approximately 75.69%.

Upon comparison, we note that the discount of the average closing share price for the 180 consecutive trading days up to and including 28 November 2008 of the Shares to the unaudited consolidated net tangible asset value per Share as at 30 June 2008 of approximately 39.01% lies within the range of the Comparables but falls below the median of those of the Comparables. We further note that the discount of the Subscription Price to the unaudited consolidated net tangible asset value per Share as at 30 June 2008 of approximately 71.71% falls below the range and the median of those of the Comparables.



Notwithstanding the significant discount of the Subscription Price to the unaudited consolidated net tangible asset value per Share as at 30 June 2008 as compared to those of the Comparables, we note that the Shares have been trading at significant discount to the Comparables in general historically as indicated by both the discounts represented by the closing price of the Share as at the Last Trading Day and the average closing share price as quoted on the Stock Exchange for the 180 consecutive trading days up to and including 28 November 2008 respectively. Thus, even though the Subscription Price represents a premium of approximately 13.2% over the closing price of HK\$0.38 per Share as quoted on the Stock Exchange on the Last Trading Day and a premium of approximately 35.2% over the average closing price of approximately HK\$0.318 per Share as quoted on the Stock Exchange for the 30 consecutive trading days up to and including the Last Trading Day respectively, we note that the Subscription Price still represents a significant discount to the unaudited consolidated net tangible asset value per Share as at 30 June 2008 as compared to those of the Comparables. However, in view of the fact that it may not be most relevant to value a company principally engaged in manufacturing by reference to its net assets in general, we consider that the Independent Shareholders should also take into account the result from the price-earnings multiple approach when making references to the Comparables instead of considering the net asset value approach on a standalone basis in order to reach an informed view.

As each of the Comparables may not be entirely comparable to the Group in terms of the scale of operations, market capitalisation, track record, asset base, future prospects and other relevant criteria and all of these factors may affect the valuation of a company as illustrated by the various results in our comparison, the above comparison is for illustrative purposes only. Accordingly, in forming our opinion, we have considered the findings of the above comparison together with other factors stated in this letter as a whole.

Based on the above analysis and from the sole perspective assessment of the Subscription Price with reference to the Comparables in terms of price/earnings multiple and the net asset value as a whole, we consider that the Subscription Price is acceptable so far as the Independent Shareholders are concerned.

#### 4. Financial effects of the Subscription on the Group

- *Cashflow*

According to the interim report of the Company for the six months ended 30 June 2008, the Group had cash and cash equivalents, short-term bank deposits and pledged short-term bank deposits of approximately RMB3,671.9 million as at 30 June 2008. Upon completion of the Subscription, the liquidity and cash position of the Group will be improved as the Subscription will facilitate the Company to raise net proceeds of approximately RMB490 million (equivalent to approximately HK\$553.7 million). Accordingly, the cash position, net current assets and current ratio of the Company are expected to be improved upon completion of the Subscription.



- *Earnings*

Save for the expenses relating to the Subscription, the completion of the Subscription will not have any immediate material impact on the earnings of the Company. Hence, immediately upon completion of the Subscription, there will be no effect on the earnings of the Company. As set out in the Letter from the Board, the net proceeds from the Subscription in the amount of approximately RMB490 million (equivalent to approximately HK\$553.7 million) will be used to reduce the outstanding indebtedness of the Group and for working capital of Shenyang Automotive. Accordingly, upon reduction of the indebtedness of the Group, it is expected that the interest expenses of the Group will be reduced which would result in improvement in the earning position of the Company.

- *Net Asset Value*

According to the interim report of the Company for the six months ended 30 June 2008, the unaudited consolidated net asset value of the Group as at 30 June 2008 was RMB6,517.8 million. Upon completion of the Subscription, the net asset value of the Company will be improved as the Subscription would increase the share capital of the Company. Accordingly, the completion of the Subscription will have a positive impact on the net asset value of the Group.

- *Gearing*

According to the interim report of the Company for the six months ended 30 June 2008, the gearing ratio of the Group as at 30 June 2008 was approximately 0.82 time, as derived by dividing the total interest-bearing liabilities of the Group as at 30 June 2008 of approximately RMB5,335.2 million by the net assets of approximately RMB6,517.8 million as at 30 June 2008.

Upon completion of the Subscription, the net asset value of the Group would be increased as a result of the Subscription whilst the interest-bearing liabilities of the Group would remain the same. Thus, the gearing level of the Group will be improved upon completion of the Subscription.

Based on the above, the Subscription would have an overall positive effect on the financial position of the Group in terms of cashflow, net asset value, and gearing upon Completion. Meanwhile, the Subscription will not have any material impact on earnings of the Group. On such basis, we are of the view that the Subscription is in the interests of the Company and the Shareholders as a whole.

##### **5. Potential dilution effect on the shareholding of the Company**

As set out in the tables showing the shareholdings changes of the Company under the section headed "Shareholding structure" as contained in the Letter from the Board, the shareholding of the existing public Shareholders as at the Latest Practicable Date was approximately 46.48%. Pursuant to the Subscription Agreement, 1,313,953,488 new Shares, representing approximately 35.8% of the existing share capital of the Company and 26.4% of the share capital of the Company as enlarged by the issue of the Subscription Shares, will be issued to Huachen. On such basis, the shareholdings of the existing public Shareholders will be diluted from approximately 46.48% to 34.23% upon completion of the Subscription.



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

We were advised by the Directors that they had considered various financing alternatives for raising additional fund. Due to the reasons stated in details in the section headed "Background of and reasons for the Subscription" above, the Directors consider that the Subscription is the best financing alternative available to the Company at the moment to finance the reduction of the outstanding indebtedness of the Group, in particular, the Convertible Bonds which may be redeemable by the Group at the options of the holders of Convertible Bonds at 122.926% of the principal amount on 7 June 2009, and increase the working capital of the Company.

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

- (a) the current financial turmoil and negative market sentiment;
- (b) the issue of the Subscription Shares will enlarge and strengthen the capital base of the Company as well as greatly enhance the net asset position and gearing position of the Group; and
- (c) the Directors consider that the Subscription is the best financing alternative available to the Company at the moment to raise funding for the Company;

we are of the opinion that the Subscription is an acceptable means of fund raising by the Company and the shareholding dilution to the Independent Shareholders is acceptable so far as the Independent Shareholders are concerned.

**6. The Whitewash Waiver**

**(a) Background**

As at the Latest Practicable Date, Huachen and parties acting in concert with it are beneficially interested in 1,446,121,500 Shares, representing approximately 39.41% of the existing issued share capital of the Company. Immediately following the Completion, Huachen and parties acting in concert with it will be interested in 2,760,074,988 Shares, representing approximately 55.38% of the issued share capital of the Company as enlarged by the issue of the Subscription Shares. As such, in the absence of the Whitewash Waiver, Huachen would incur an obligation pursuant to Rule 26 of the Takeovers Code to make a mandatory general offer in respect of all the securities of the Company (other than those held by or agreed to be acquired by Huachen and parties acting in concert with it) in accordance with Rule 26 of the Takeovers Code.



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

An application has been made by Huachen to the Executive for the Whitewash Waiver pursuant to the Takeovers Code. The Whitewash Waiver, if granted by the Executive, would be subject to, among other things, the approval of the Independent Shareholders at the SGM by way of poll, which Huachen and parties acting in concert with it will abstain from voting on the relevant resolution.

(b) *The Whitewash Waiver as a condition of the Subscription Agreement*

It is a condition precedent to the completion of the Subscription Agreement that the Whitewash Waiver is granted by the Executive and approved by Independent Shareholders. If the Whitewash Waiver is not granted by the Executive or not approved by Independent Shareholders, the Subscription Agreement will lapse and the Subscription will not proceed.

(c) *The Subscriber and parties acting in concert with it shall remain as the largest group of Shareholders*

As at the Latest Practicable Date, Huachen and parties acting in concert with it are beneficially interested in 1,446,121,500 Shares, representing approximately 39.41% of the existing issued share capital of the Company. Upon the Completion (assuming that no further Shares are issued by the Company between the Latest Practicable Date and Completion), the beneficial shareholding interest of Huachen (and parties acting in concert with it) in the Company will increase from approximately 39.41% to 55.38%. On such basis, Independent Shareholders should note that Huachen is already the largest Shareholder prior to the Subscription and shall remain as the largest Shareholder upon completion of the Subscription.

The granting and approval of the Whitewash Waiver will enable the Group and all the Shareholders, including the Independent Shareholders, to take the opportunity to enjoy the financial benefits upon Completion which include, among other things, (i) the significant improvement in cash and working capital position of the Group; (ii) the increase in net assets and the enhancement of the equity base of the Group; (iii) the reduction in the gearing level of the Group upon completion of the Subscription; and (iv) the significant reduction in the gearing level of the Group upon repayment of the debt by proceeds from the Subscription. Accordingly, we consider that the granting of the Whitewash Waiver is fair and reasonable so far as the Company and the Independent Shareholders are concerned.

**RECOMMENDATION**

After taking into account the above principal factors and reasons, we consider that the Subscription was entered into on normal commercial terms and the terms of the Subscription Agreement are fair and reasonable so far as the Independent Shareholders are concerned, and in the interests of the Company and Shareholders as a whole. On the basis that the grant of the Whitewash Waiver is a condition of the Subscription Agreement, we also consider that the grant of the Whitewash Waiver is fair and reasonable and in the interest of the Company and the Shareholders as a whole. Accordingly, we recommend the Independent Board Committee to advise the Independent Shareholders to, and we recommend the Independent Shareholders to, vote in favour of the resolution to approve the Subscription Agreement and the Whitewash Waiver.

Yours faithfully,  
For and on behalf of  
**Partners Capital International Limited**



Alan Fung  
Managing Director