

12 August 2011

*To the Independent Board Committee and the Independent Shareholders of
Polyard Petroleum International Group Limited*

**DEBT RESTRUCTURING AND CONNECTED TRANSACTION;
AND
APPLICATION FOR THE WHITEWASH WAIVER**

INTRODUCTION

We refer to our appointment to advise the Independent Board Committee and the Independent Shareholders in respect of the Subscription Agreement and the Whitewash Waiver, details of which are set out in the section headed "Letter from the Board" (the "**Board Letter**") in the Company's circular dated 12 August 2011 (the "**Circular**") to the Shareholders, of which this letter forms part. Terms used in this letter shall have the same meanings as those defined in the Circular unless the context requires otherwise.

On 30 June 2011, the Company entered into the Subscription Agreement with Silver Star and Mr. Lam pursuant to which (1) the Company will allot and issue to Silver Star 583,333,333 Subscription Shares at an issue price of HK\$0.240 per Subscription Share; (2) the Company will issue to Silver Star the Convertible Notes in an aggregate principal amount of HK\$100,000,000; (3) Mr. Lam will advance a loan up to HK\$36,352,231.22 (the "**Loan**") to the Company which will be used solely for the redemption of the Convertible Bonds A; and (4) the Company will redeem all the outstanding Convertible Bonds A which will be due on 10 October 2011.

Silver Star is wholly-owned by Mr. Lam. Since Silver Star is a controlling Shareholder, both Silver Star and Mr. Lam are connected persons of the Company and, accordingly, the Subscription constitutes a connected transaction for the Company under Chapter 20 of the GEM Listing Rules. As the relevant percentage ratios calculated pursuant to Rule 19.06 of the GEM Listing Rules in respect of the Subscription exceed 5%, the Subscription Agreement and the transactions contemplated thereunder are subject to the Independent Shareholders' approval by way of poll at the EGM pursuant to the GEM Listing Rules.

As at the date of the Subscription Agreement, Silver Star, Mr. Lam and persons acting in concert with any of them held 711,845,196 Shares, representing approximately 42.51% of the issued share capital of the Company. Immediately after the issuance of the Subscription Shares, Silver Star, Mr. Lam and persons acting in concert with any of them will be

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interested in 939,255,931 Consolidated Shares, representing approximately 66.12% of the issued share capital of Company as enlarged by the issue of the Subscription Shares. Under Rule 26 of the Takeovers Code, the acquisition of voting rights by more than 2% from the lowest collective holding of voting rights in the Company in any 12-month period by Silver Star will trigger an obligation on Silver Star, Mr. Lam and persons acting in concert with any of them to make a general offer for all the securities of the Company other than those already owned or agreed to be acquired by them, unless a whitewash waiver is granted by the Executive and approved by the Independent Shareholders of the Company.

Silver Star and Mr. Lam have made an application to the Executive for the Whitewash Waiver. The Whitewash Waiver, if granted by the Executive, will be subject to, among other things, the approval of the Independent Shareholders at the EGM by way of poll.

Immediately after the issuance of the Subscription Shares, the aggregate shareholding of Silver Star, Mr. Lam and persons acting in concert with any of them in the Company will exceed 50%, and if the Whitewash Waiver is granted by the Executive and approved by the Independent Shareholders at the EGM, Silver Star, Mr. Lam and persons acting in concert with any of them may further increase their shareholdings in the Company without incurring any further obligation under Rule 26 of the Takeovers Code to make a general offer. However, where there are changes in the make-up of the parties acting in concert with any of Mr. Lam or Silver Star that effectively result in a new group being formed or the balance of the parties acting in concert with any of Mr. Lam or Silver Star being changed significantly, it may trigger an obligation to make a mandatory offer under Rule 26 of the Takeover Code unless a waiver from the Executive is granted.

Mr. Lam, Silver Star, their respective associates and parties acting in concert with any of them (in aggregate holding 711,845,196 Shares) and anyone who is involved in or interested in the Subscription Agreement and the Whitewash Waiver will abstain from voting at the EGM in respect of the resolutions approving the Subscription Agreement and the transactions contemplated thereunder and the Whitewash Waiver. As at the Latest Practicable Date, none of the Directors held any Shares. The Directors have confirmed that so far as they are aware, save for the above, no other Shareholder and no Director is involved in or interested in the Subscription Agreement and the Whitewash Waiver.

The Independent Board Committee, comprising all the independent non-executive Directors, namely Mr. Wang Yanhui, Mr. Pai Hsi-Ping and Mr. Wong Kon Man Jason, has been established to make recommendations to the Independent Shareholders as to whether the Subscription Agreement and the Whitewash Waiver are fair and reasonable and in the

interests of the Company and the Independent Shareholders as a whole and to advise the Independent Shareholders on how to vote at the EGM.

Our role as the independent financial adviser is to give our independent opinion to the Independent Board Committee and the Independent Shareholders as to (i) whether the Subscription Agreement and the Whitewash Waiver are fair and reasonable so far as the Independent Shareholders are concerned and are in the interests of the Company and the Independent Shareholders as a whole; and (ii) advise the Independent Shareholders on how to vote on the resolutions at EGM in relation to the Subscription Agreement and the Whitewash Waiver. The appointment of Veda Capital has been approved by the Independent Board Committee.

BASIS OF OUR OPINION

In formulating our opinion to the Independent Board Committee and the Independent Shareholders, we have relied on the accuracy of the statements, information, opinions and representations contained or referred to in the Circular and the information and representations provided to us by the Company, the Directors and the management of the Company. 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 assumed that all information, representations and opinions contained or referred to in the Circular, which have been provided by the Company, the Directors and the management of the Company and for which they are solely and wholly responsible, were true and accurate at the time when they were made and continue to be true up to the Latest Practicable Date and should there be any material changes to our opinion after the despatch of the Circular, Shareholders would be notified as soon as possible.

The Directors have jointly and severally accepted full responsibility for the accuracy of the information contained in the Circular (other than information relating to Silver Star) and have confirmed in the Circular, having made all reasonable enquiries, that to the best of their knowledge, opinions expressed in the Circular have been arrived at after due and careful consideration and there are no other facts not contained in the Circular, the omission of which would make any statement in the Circular misleading. The sole director of Silver Star accepts full responsibility for the accuracy of the information relating to Silver Star contained in the Circular and confirms, having made all reasonable enquiries, that to the best of his knowledge, opinions expressed in the Circular by the director of Silver Star have been arrived at after due and careful consideration and there are no other

facts not contained in the Circular the omission of which would make any statement relating to Silver Star contained in the Circular misleading. We consider that we have been provided with sufficient information to reach an informed view and to provide a reasonable basis for our opinion. We have not, however, conducted any independent in-depth investigation into the business and affairs of the Company, or its subsidiaries or associated companies.

PRINCIPAL FACTORS AND REASONS CONSIDERED

In arriving at our recommendation in relation to the Subscription and the Whitewash Waiver, we have considered the following principal factors and reasons.

1. Background and financial information of the Company

The Company is principally engaged in (i) the exploration, exploitation and production of oil, natural gas and coal; and (ii) the trading of petroleum-related products.

As set out in the annual report 2009 for the year ended 31 December 2009 (the “AR 2009”), the Group recorded turnover from continuing operations of approximately HK\$3.92 million for the year ended 31 December 2009, representing a decrease of approximately 81.89% as compared with the turnover from continuing operations for the year ended 31 December 2008 of approximately HK\$21.64 million. As noted from AR 2009, the decrease in turnover was mainly due to the slowdown of economy from 2008 and oil price fluctuation during the year 2009 which continued to limit the trading volume of the petroleum-related products in 2009. The Group recorded loss attributable to Shareholders of approximately HK\$95.16 million for the year ended 31 December 2009, representing a decrease of approximately 69.96% as compared with the loss attributable to Shareholders of approximately HK\$316.76 million for the year ended 31 December 2008. As noted from AR 2009, the decrease in loss was mainly due to the decrease in impairment loss on interests in jointly controlled entities.

As set out in the annual report 2010 of the Company for the year ended 31 December 2010 (the “AR 2010”), the Group recorded turnover of approximately HK\$0.83 million, representing a decrease of approximately 78.83% from that for the year ended 31 December 2009 of approximately HK\$3.92 million. As noted from AR 2010, the drop in turnover was mainly due to the sluggish sales of petroleum-related products. The Group reported loss attributable to Shareholders of approximately

HK\$66.11 million for the year ended 31 December 2010, representing a decrease in loss of approximately 30.53% from that for the year ended 31 December 2009 of approximately HK\$95.16 million. As noted from AR 2010, the decrease in loss was mainly due to the reversal of impairment loss in interests in associates.

As set out in the interim results announcement of the Company for the six months ended 30 June 2011 (the “**IR Announcement 2011**”) dated 9 August 2011, the Group did not record any turnover for the six months ended 30 June 2011. As set out in the IR Announcement 2011, among the three ongoing projects, the oil and gas project in Brunei has completed drilling two exploratory wells while the coal mine project in the Philippines has entered into the development phase. As most of the projects are still in the exploratory phase, the Group continues to incur capitalizable and operating expenses, and sustain losses. Revenues will be generated when the projects progress to the exploitative phase with output of commercial quantity. The Group reported an unaudited loss attributable to Shareholders of approximately HK\$28.02 million for six months ended 30 June 2011, representing an increase in loss of approximately 23.44% from that for six months ended 30 June 2010 of approximately HK\$22.70 million. As noted from IR Announcement 2011, the increase in loss was mainly due to the increase in business development expenses and finance costs as a result of the increase in effective interest rate in amortising the Convertible Bonds A which matured in October 2010 and was extended for one year.

2. Reasons for the Subscription and the use of proceeds

Under the Subscription Agreement, (i) the Company will allot and issue to Silver Star 583,333,333 Subscription Shares at an issue price of HK\$0.240 per Subscription Share with an aggregate amount of approximately HK\$140,000,000; (ii) the Company will issue to Silver Star the Convertible Notes in an aggregate principal amount of HK\$100,000,000; (iii) Mr. Lam will advance a loan up to HK\$36,352,231.22 to the Company which it will use solely for the redemption of the Convertible Bonds A; and (iv) the Company will redeem all the outstanding Convertible Bonds A which will be due on 10 October 2011.

The Convertible Bonds A which has a coupon rate of 3% per annum were issued to Mr. Lam in October 2007. As at the Latest Practicable Date, the aggregate outstanding principal amount of the Convertible Bonds A was HK\$276,352,231.22. As noted from the Board Letter, the conversion price of the Convertible Bonds A is HK\$2.873 per Share (subject to adjustment).

As set out in the Board Letter, taking into account that (i) the debt restructuring through the Subscription can reduce the amount of interest payable by the Company pursuant to the terms and conditions of the Convertible Bonds A as well as the liabilities of the Company; and (ii) the issue of Subscription Shares and/or the Conversion Shares can enlarge the capital base of the Company, the Directors are of the view that the Subscription is fair and reasonable and is in the interests of the Company and the Shareholders as a whole.

As noted from the Board Letter, the Company has raised net proceeds amounting to approximately HK\$55 million and approximately HK\$23 million from the rights issue in August 2010 (the “**2010 Rights Issue**”) and in April 2011 (the “**2011 Rights Issue**”) respectively. As advised by the Company, approximately HK\$50 million of the net proceeds from the 2010 Rights Issue has been utilized for the gas and coal projects and general working capital of the Company as at the Latest Practicable Date and the remaining HK\$5 million is intended to be injected into the gas project. Further advised by the Company, the net proceeds from the 2011 Rights Issue have not been utilized as at the Latest Practicable Date and are intended to be utilized for the oil project in Brunei and coal project in the Philippines of the Company.

As noted from IR Announcement 2011, the Group recorded cash and bank balances of approximately HK\$29.78 million (the “**Cash Position**”) as at 30 June 2011 and has been loss making for the two years ended 31 December 2010 and for the six months ended 30 June 2011. We were also advised by the Company that save for Convertible Bonds A with outstanding principal amount of approximately HK\$276.35 million and Convertible Bonds B with outstanding principal amount of approximately HK\$120.00 million, the Company has no other borrowings as at the Latest Practicable Date. The Convertible Bonds A carry coupon rate of 3% per annum accrued on a day to day basis with maturity in October 2011 and the Convertible Bonds B which was issued under two tranches are non interest bearing with maturity in December 2013 for the first tranche and in February 2014 for the second tranche.

As advised by the Company, the holder of Convertible Bonds A has the right at any time during the conversion period (i.e. from 10 October 2007 to 10 October 2011) to convert the whole or part of the principal amount of the Convertible Bonds A into Shares pursuant to the terms of the Convertible Bonds A. Any Convertible Bonds A which remains outstanding on the maturity date i.e. 10 October 2011 (the “**Maturity Date**”) shall be redeemed by the Company at a redemption amount equal

to the principal amount of such Convertible Bonds A together with interest accrued thereon and such sum shall be payable to the Convertible Bonds A holder on the business day immediately following the Maturity Date. Pursuant to the terms and conditions of the Convertible Bonds A, on the Maturity Date, other than redemption of the outstanding Convertible Bonds A, there is no other payment option to settle the outstanding amount of the Convertible Bonds A. As advised by the Directors, the Company will not be able to redeem the Convertible Bonds A by the internal resources of the Company or by obtaining other resources (other than the proceeds from the Subscription). In the event that the Subscription Agreement is not approved by the Independent Shareholders at the EGM, the Company will further negotiate with Silver Star and Mr. Lam with a view to agree on a possible alternative plan for the payment of the outstanding amount of the Convertible Bonds A. As at the Latest Practicable Date, save for the Subscription, there was no other potential restructuring plan in respect of the payment on the outstanding amount of the Convertible Bonds A.

In view of (i) the loss-making track records of the Company; (ii) the net proceeds from the 2010 Rights Issue and 2011 Rights Issue are intended to be reserved for the development of the projects of the Company; (iii) the outstanding principal amount of Convertible Bonds A which will be matured in October 2011 represented approximately 9.28 times of the Cash Position of the Company as at 30 June 2011; (iv) given that the principal amount of Convertible Notes is smaller than the outstanding principal amount of Convertible Bonds A and hence less interest expense will be arised from the Convertible Notes, no interest expense would be incurred from the subscription of Subscription Shares and the Loan does not carry any interest, the Subscription Agreement enables the Group to reduce the interest expense of the Company as well as the liabilities of the Company; and (v) the Company will not be able to redeem the Convertible Bonds A by the internal resources of the Company or by obtaining other resources (other than the proceeds from the Subscription), we are of the view that the Subscription Agreement is fair and reasonable and is in the interests of the Company and the Independent Shareholders as a whole.

3. The Subscription Agreement

(a) *The Subscription Shares*

Pursuant to the Subscription Agreement, Silver Star has conditionally agreed to subscribe for and the Company has conditionally agreed to allot and issue a total of 583,333,333 Subscription Shares.

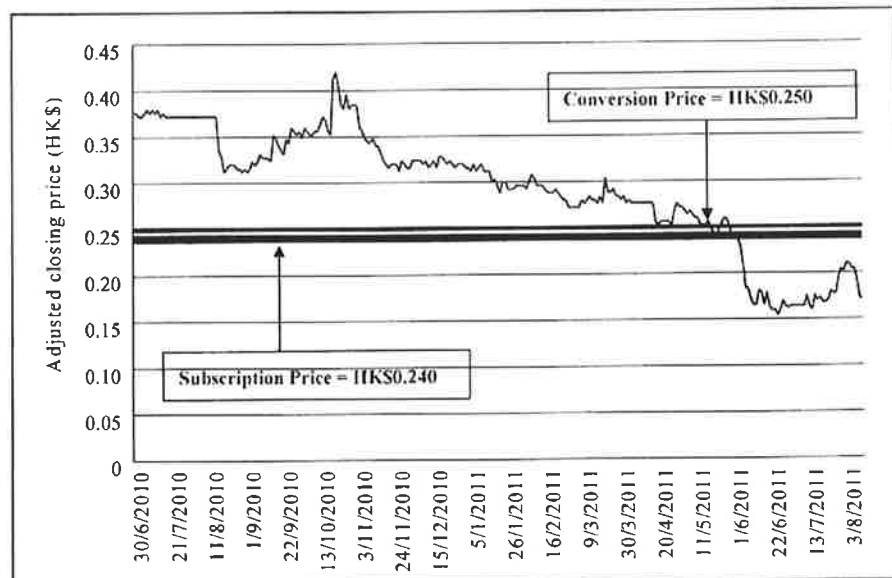
Subscription Price

As set out in the Board Letter, the Subscription Price was determined after arm's length negotiation between the Company and Silver Star with reference to the recent trading prices of the Shares on the Stock Exchange and theoretical closing price of Consolidated Share (the "**Theoretical Closing Price**"), based on the closing prices per Share and adjusted for the effect of the Share Consolidation. The Subscription Price of HK\$0.240 per Subscription Share represents:

- (i) a premium of approximately 46.34% over the Theoretical Closing Price on the Last Trading Day of HK\$0.164, based on the closing price of HK\$0.082 per Share as quoted on the Stock Exchange on the Last Trading Day and adjusted for the effect of the Share Consolidation;
- (ii) a premium of approximately 46.34% over the 5-day average Theoretical Closing Price of HK\$0.164, based on the closing prices as quoted on the Stock Exchange for the five trading days up to and including the Last Trading Day and adjusted for the effect of the Share Consolidation;
- (iii) a premium of approximately 46.34% over the average 10-day Theoretical Closing Price of HK\$0.164, based on the closing prices as quoted on the Stock Exchange for the last 10 trading days up to and including the Last Trading Day and adjusted for the effect of the Share Consolidation;
- (iv) a premium of approximately 8.11% over the average 50-day Theoretical Closing Price of HK\$0.222, based on the closing prices as quoted on the Stock Exchange for the last 50 trading days up to and including the Last Trading Day and adjusted for the effect of the Share Consolidation;

- (v) a discount of approximately 67.74% over the Group's audited consolidated net asset per Consolidated Share (excluding non-controlling interests) as at 31 December 2010 of approximately HK\$0.744, based on a total of 837,281,844 Consolidated Shares as at the date of the Subscription Agreement (assuming the Share Consolidation has become effective) and the Group's audited consolidated net asset value attributable to owners of the Company of approximately HK\$622,250,000 as at 31 December 2010; and
- (vi) a premium of approximately 39.53% over the Theoretical Closing Price on the Latest Practicable Date of HK\$0.172, based on the closing price of HK\$0.086 per Share as quoted on the Stock Exchange on the Latest Practicable Date and adjusted for the effect of the Share Consolidation.

In order to assess the fairness and reasonableness of the Subscription Price, we have reviewed the trading price of the Shares for the period from 30 June 2010, being the 12-month period prior to the Last Trading Day, up to and including the Latest Practicable Date (the "Review Period"). The chart below illustrates the daily closing prices of the Shares (adjusted with the Share Consolidation) versus the Subscription Price and the Conversion Price during the Review Period:



Source: the website of the Stock Exchange

During the Review Period and assuming that the Share Consolidation has become effective throughout the Review Period, the highest Theoretical Closing Price and the lowest Theoretical Closing Price were HK\$0.420 on 20 October 2010 and HK\$0.154 on 23 June 2011 respectively. The Subscription Price represents a discount of approximately 42.86% and a premium of approximately 55.84% respectively to such highest and lowest Theoretical Closing Prices during the Review Period. As noted from the above, the Theoretical Closing Price has experienced a decreasing trend since October 2010 and fluctuated around the price level of HK\$0.25 in April and May 2011 before it dropped to the price level below HK\$0.20 on 7 June 2011.

We have also reviewed fundraising activities by way of subscription and placing of shares from one month preceding the date of the Subscription Agreement (i.e. 30 June 2011) announced by companies which are listed on the Main Board and GEM and principally engaged in businesses similar to the exploration, exploitation and production of oil, natural gas and coal with loss-making financial performance in the latest financial year (the “**Potential Comparables**”). We observed that there are four Potential Comparables and the subscription prices of the Potential Comparables (i) equivalent to or represented discount to the closing price per share of the Potential Comparables on the last trading day prior to the respective announcements; and (ii) represented discount to the average closing price per share of the Potential Comparables for the five trading days prior to the last trading day prior to the respective announcements. In light of (i) the small sample size; (ii) the subscription prices of the Potential Comparables were equivalent to or represented discount to the closing prices of the shares at the time of the fundraising; and (iii) the Subscription Price represented a premium to the Theoretical Closing Price on the Last Trading Day and a premium to the 5-day average Theoretical Closing Price (based on the closing prices as quoted on the Stock Exchange for the five trading days up to and including the Last Trading Day), we consider that the Potential Comparables are not appropriate for assessing the fairness and reasonableness of the Subscription Price.

Having taken into account that (i) the loss-making track records of the Company; (ii) the bargaining power of the Company given the outstanding principal amount of Convertible Bonds A which will be matured in October 2011 represented approximately 9.28 times of the Cash Position of the Company as at 30 June 2011; (iii) the decreasing trend of the Theoretical Closing Price since October 2010; and (iv) the Subscription Price is at a premium to the recent Theoretical Closing Prices and at a premium to the average 50-day Theoretical Closing Price (based on the closing prices as

quoted on the Stock Exchange for the last 50 trading days up to and including the Last Trading Day and adjusted for the effect of the Share Consolidation), we consider the Subscription Price is fair and reasonable so far as the Independent Shareholders are concerned.

(b) *The Convertible Notes*

Pursuant to the Subscription Agreement, the Company will issue to Silver Star the Convertible Notes in an aggregate principal amount of HK\$100,000,000 with interest rate of 3% per annum and with maturity date falling on the third anniversary of the date of issue of the Convertible Notes.

Conversion Price

As advised by the Company, the Conversion Price is determined after arm's length negotiation between the Company and Silver Star with reference to the recent trading prices and Theoretical Closing Price and the Subscription Price.

The initial Conversion Price of HK\$0.250 per Conversion Share represents:

- (i) a premium of approximately 52.44% over the Theoretical Closing Price on the Last Trading Day of HK\$0.164, based on the closing price of HK\$0.082 per Share as quoted on the Stock Exchange on the Last Trading Day and adjusted for the effect of the Share Consolidation;
- (ii) a premium of approximately 52.44% over the 5-day average Theoretical Closing Price of approximately HK\$0.164, based on the closing prices as quoted on the Stock Exchange for the last five trading days up to and including the Last Trading Day and adjusted for the effect of the Share Consolidation;
- (iii) a premium of approximately 4.17% over the Subscription Price; and
- (iv) a premium of approximately 45.35% over Theoretical Closing Price on the Latest Practicable Date of HK\$0.172, based on the closing price of HK\$0.086 per Share as quoted on the Stock Exchange on the Latest Practicable Date and adjusted for the effect of the Share Consolidation.

Under the debt restructuring, the Convertible Bonds A issued to Mr. Lam in October 2007 with conversion price of HK\$2.873 per Share (subject to adjustment) will be replaced by the Subscription. We noted that the conversion price of Convertible Bonds A is different from the Conversion Price, however, in view that market price of the Shares and the market sentiment are different in the year 2007 and year 2011, we consider it is reasonable that the Conversion Price does not make reference to the conversion price of Convertible Bonds A. We also noted from the Company's circular dated 6 August 2007 in respect of, among others, the issue of Convertible Bonds A (the "2007 Circular") that no conversion right of the Convertible Bonds A maybe exercised, to the extent that following such exercise, a holder of the Convertible Bonds A and its associates, taken together, will directly or indirectly, control 25% or more of the Shares (the "Conversion Restriction") whilst the Convertible Notes does not have the Conversion Restriction. Having considered the shareholding interests of Mr. Lam and its associates were 16.41% as at the latest practicable date of the 2007 Circular and their shareholding interests are over 25% as at the Latest Practicable Date, we consider it is commercially justifiable that the Conversion Restriction is not included in the terms of the Convertible Notes.

Given (i) both of the Convertible Notes and the Convertible Bonds A carry the same interest rates; (ii) the interest rate of Convertible Notes is below the Hong Kong dollar best lending rate of 5.0% as quoted from the Hong Kong and Shanghai Banking Corporation Limited as at the Latest Practicable Date; and (iii) as advised by the Company, save for the principal amount, the conversion price and the abovementioned Conversion Restriction, there is no material difference between the major terms of the Convertible Bonds A and the Convertible Notes, we are of the view that the Convertible Notes represents an extension of partial liabilities obligation under the Convertible Bonds A. In light of the above and the Conversion Price represents premium to the recent Theoretical Closing Price and the Subscription Price, we are of the view that the Convertible Notes are fair and reasonable and in the interests of the Company and the Independent Shareholders as a whole.

(c) Loan

Pursuant to the Subscription Agreement, Mr. Lam will advance the Loan up to HK\$36,352,231.22 to the Company with a term of payable on the date falling on the second anniversary of the date of drawdown of the Loan and zero interest.

Having considered that (i) the Loan is interest free; (ii) there is no pledge of assets under the Loan; and (iii) the purpose of the Loan is to redeem the Convertible Bonds A which will be expired in October 2011, we are of the view that the Loan is fair and reasonable and in the interests of the Company and the Independent Shareholders as a whole.

4. Alternatives

We have been advised by the Company that the management has considered other alternative means for the Group to raise funds other than the Subscription, including but not limited to, debt financing and rights issue/open offer or placing of new Shares. Given (i) the Company was unable to find underwriters for the 2011 Rights Issue due to, among others, the financial conditions of the Company and the then trading conditions of the Shares; (ii) the acceptance level of approximately 37.62% in the 2011 Rights Issue; and (iii) the loss making track records of the Company, the Company considers rights issue/open offer or placing of new Shares may not be desirable alternatives as compared with the Subscription. In addition, in view that the existing projects of the Company are still in the development stage and no revenue has been generated from such existing projects, the Company considers it may not be able to obtain bank financing with favourable terms in a timely manner.

We noted from the announcement of the Company dated 10 June 2011 in relation to, among others, the results of the 2011 Rights Issue, the acceptance under the 2011 Rights Issue represented approximately 37.62% of the total maximum rights shares and the acceptance of the rights shares by Silver Star, Mr. Lam and parties acting in concert with them represented approximately 29.25% of the total maximum rights shares. In light of (i) the acceptance level of the 2011 Rights Issue; (ii) the loss-making track record of the Company; and (iii) given the Cash Position of the Company as at 30 June 2011, the Subscription would enable the Company to resolve the redemption of Convertible Bonds A which will be matured in October 2011 and to reduce the liabilities and interest expense of the Company, we consider the Subscription is in the interests of the Company and the Independent Shareholders as a whole.

5. Financial effects

(i) Net asset value

As set out in IR Announcement 2011, the unaudited net asset value of the Group was approximately HK\$662.49 million as at 30 June 2011 and based on the issued share of 1,674,563,688 Shares as at the Latest Practicable Date and such unaudited net asset value of the Group as at 30 June 2011, the net asset per Share was approximately HK\$0.40. As advised by the Company, upon completion of the Subscription Agreement, there is no material effect on the total assets of the Group and the total liabilities will be (i) decreased by the outstanding amount of the Convertible Bonds A; and (ii) increased by the liabilities of the Loan and the liability component of the Convertible Notes. As the liabilities of the Loan and the liability component under the Convertible Notes in aggregate are less than the liabilities of the Convertible Bonds A, the total liabilities of the Group will be reduced upon completion of the Subscription Agreement. As such, the Subscription Agreement will have a positive impact on the net asset value of the Group.

(ii) Working capital

Upon completion of the Subscription Agreement, the Company would be able to (i) retain the capital which would be used for the purpose of redemption of the Convertible Bonds A; and (ii) bear less interest expense arising from the Convertible Notes as comparing with the Convertible Bonds A given the different principal amount. Based on the difference of the principal amount of the Convertible Bonds A and the Convertible Notes of approximately HK\$176.35 million and the interest rate per annum of 3.0% of the Convertible Bonds A and the Convertible Notes, the interest expense per year is expected to be reduced by approximately HK\$5.29 million.

In light of the enhancement on the financial position of the Group as mentioned above, we are of the opinion that the Subscription Agreement is in the interests of the Company and the Independent Shareholders as a whole.

6. Potential dilution

Based on the shareholding structure of the Company as set out in the Board Letter, the shareholding of the existing Independent Shareholders will be diluted from approximately 57.49% as at the Latest Practicable Date to (i) approximately 33.88% upon completion of the Subscription Agreement, assuming none of the Convertible Notes is converted into Conversion Shares; and (ii) approximately 26.44% upon completion of the Subscription Agreement, assuming the Convertible Notes is fully converted into Conversion Shares.

Having considered:

- (i) the loss-making track records of the Company;
- (ii) the net proceeds from the 2010 Rights Issue and 2011 Rights Issue are intended to be reserved for the development of the projects of the Company;
- (iii) the outstanding principal amount of Convertible Bonds A which will be matured in October 2011 represented approximately 9.28 times of the Cash Position of the Company as at 30 June 2011;
- (iv) given that the principal amount of Convertible Notes is smaller than the outstanding principal amount of Convertible Bonds A and hence less interest expense will be arised from the Convertible Notes, no interest expense would be incurred from the subscription of Subscription Shares and the Loan does not carry any interest, the Subscription Agreement enables the Group to reduce the interest expense of the Company as well as the liabilities of the Company;
- (v) the Company will not be able to redeem the Convertible Bonds A by the internal resources of the Company or by obtaining other resources (other than the proceeds from the Subscription);
- (vi) the Subscription Price is at premium to the recent Theoretical Closing Prices and at a premium to the average 50-day Theoretical Closing Price (based on the closing prices as quoted on the Stock Exchange for the last 50 trading days up to and including the Last Trading Day and adjusted for the effect of the Share Consolidation);

- (vii) both of the Convertible Notes and the Convertible Bonds A carry the same interest rates;
- (viii) the interest rate of Convertible Notes is below the Hong Kong dollar best lending rate of 5.0% as quoted from the Hong Kong and Shanghai Banking Corporation Limited as at the Latest Practicable Date;
- (ix) the Conversion Price represents a premium to the recent Theoretical Closing Price and the Subscription Price;
- (x) the Loan is interest free; and
- (xi) the positive impact on the financial position of the Group as a result of the Subscription Agreement,

we consider the potential dilution effect on the shareholding of the existing Independent Shareholders is acceptable.

7. Whitewash Waiver

As at the date of the Subscription Agreement, Silver Star, Mr. Lam and persons acting in concert with any of them held 711,845,196 Shares, representing approximately 42.51% of the issued share capital of the Company. Immediately after the issuance of the Subscription Shares, Silver Star, Mr. Lam and persons acting in concert with any of them will be interested in 939,255,931 Consolidated Shares, representing approximately 66.12% of the issued share capital of Company as enlarged by the issue of the Subscription Shares. Under Rule 26 of the Takeovers Code, the acquisition of voting rights by Silver Star, Mr. Lam and persons acting in concert with any of them for more than 2% from the lowest collective holding of voting rights in the Company in any 12-month period by Silver Star will trigger an obligation on Silver Star, Mr. Lam and persons acting in concert with any of them to make a general offer for all the securities of the Company other than those already owned or agreed to be acquired by them, unless a whitewash waiver is granted by the Executive and approved by the Independent Shareholders of the Company.

Silver Star and Mr. Lam have made an application to the Executive for the Whitewash Waiver. The Whitewash Waiver, if granted by the Executive, will be subject to, among other things, the approval of the Independent Shareholders at the EGM by way of poll.

Immediately after the issuance of the Subscription Shares, the aggregate shareholding of Silver Star, Mr. Lam and persons acting in concert with any of them in the Company will exceed 50%, and if the Whitewash Waiver is granted by the Executive and approved by the Independent Shareholders at the EGM, Silver Star, Mr. Lam and persons acting in concert with any of them may further increase their shareholdings in the Company without incurring any further obligation under Rule 26 of the Takeovers Code to make a general offer. However, where there are changes in the make-up of the parties acting in concert with any of Mr. Lam or Silver Star that effectively result in a new group being formed or the balance of the parties acting in concert with any of Mr. Lam or Silver Star being changed significantly, it may trigger an obligation to make a mandatory offer under Rule 26 of the Takeover Code unless a waiver from the Executive is granted.

Based on our analysis of the Subscription Agreement, we consider that the Subscription Agreement is in the interests of the Company and the Independent Shareholders as a whole. If the Whitewash Waiver is not approved by the Independent Shareholders at the EGM, the Subscription will not proceed and the Company will lose all the benefits that are expected to be brought by the completion of the Subscription Agreement. Accordingly, we are of the view that for the purposes of implementing the Subscription Agreement, we consider the Whitewash Waiver is fair and reasonable and in the interests of the Company and the Independent Shareholders as a whole.

RECOMMENDATION

Taking into account the factors and reasons as mentioned above, we consider that the Subscription Agreement is fair and reasonable so far as the Independent Shareholders are concerned and the Subscription Agreement is in the interests of the Company and the Independent Shareholders as a whole. We would therefore advise the Independent Shareholders and the Independent Board Committee to recommend the Independent Shareholders to vote in favour of the resolution to approve the Subscription Agreement to be proposed at the EGM.

The Subscription is conditional upon the approval of the Whitewash Waiver. If the Whitewash Waiver is not approved, the Subscription will not proceed. Having taken into account our recommendation on the Subscription Agreement above, we consider the Whitewash Waiver is fair and reasonable so far as the Independent Shareholders are concerned and the Whitewash Waiver is in the interests of the Company and the

Independent Shareholders as a whole. Accordingly, we would advise the Independent Shareholders and the Independent Board Committee to recommend to the Independent Shareholders to vote in favour of the resolution to approve the Whitewash Waiver to be proposed at the EGM.

Yours faithfully,
For and on behalf of
Veda Capital Limited



Hans Wong
Chairman

Julisa Fong
Managing Director