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22 January 2026

To: The Independent Board Committee, the Takeovers Code Independent Shareholders, and the Proposed Acquisition LR Independent Shareholders of Hua Hong Semiconductor Limited

Dear Sirs,

(1) MAJOR AND CONNECTED TRANSACTION – ACQUISITION OF SHARE CAPITAL OF THE TARGET INVOLVING THE ISSUE OF CONSIDERATION SHARES UNDER SPECIFIC MANDATE; (2) APPLICATION FOR WHITEWASH WAIVER; (3) PROPOSED NON-PUBLIC ISSUANCE OF RMB SHARES TO RAISE SUPPORTING FUNDS; AND (4) SPECIAL DEAL

INTRODUCTION

We refer to our appointment by the Company to advise the Independent Board Committee, the Takeovers Code Independent Shareholders, and the Proposed Acquisition LR Independent Shareholders in respect of (i) the proposed acquisition of share capital of Shanghai Huali Microelectronics Corporation (the "**Target Company**") involving the issue of consideration shares under specific mandate contemplated thereunder (the "**Proposed Acquisition**"); (ii) the Whitewash Waiver; and (iii) the Special Deal in relation to the Proposed Non-issuance of RMB Shares, details of which are set out in the letter from the Board contained in the circular of the Company to the Shareholders dated 22 January 2026 (the "**Circular**"), of which this letter forms part. Capitalised terms used in this letter have the same meanings as those defined in the Circular unless the context requires otherwise.

References are made to the announcements of the Company dated 31 August 2025, 16 October 2025 and 31 December 2025 in relation to, among others, the Acquisition Agreement, the Supplemental Agreement and the Compensation Agreement entered into with the Vendors. As disclosed in the Announcement, on 29 August 2025, the Company and the Vendors entered into the Acquisition Agreement, pursuant to which the Company conditionally agreed to purchase, and the Vendors conditionally agreed to sell, a total of 97.4988% of the share capital of the Target Company. Subsequently, as disclosed in the Update Announcement, the Company and the Vendors entered into the Supplemental Agreement on 31 December 2025, which set out further details of the Proposed Acquisition and, pursuant thereto, the final Total Consideration was determined to be RMB8,267,902,153.26, to be satisfied by the allotment and issuance of 190,768,392 Consideration Shares (RMB Shares) to the Vendors at an issue price of RMB43.34 per share.

In addition to the Proposed Acquisition, on 29 August 2025, the Board approved the Proposed Non-public Issuance of RMB Shares to raise supporting funds. The total amount of supporting funds to be raised thereunder shall be RMB7,556,286,000 (being not exceeding 100% of the final Total Consideration for the Proposed Acquisition) and the number of RMB Shares to be issued shall not exceed 30% of the total issued share capital of the Company upon Completion.

LISTING RULES IMPLICATIONS

Proposed Acquisition

As one or more of the applicable percentage ratios in respect of the Proposed Acquisition in accordance with the Listing Rules exceed 25% but are less than 100%, the Proposed Acquisition constitutes a major transaction of the Company which is subject to the reporting, announcement and Shareholders' approval requirements under Chapter 14 of the Listing Rules.

As HH Grace (a wholly-owned subsidiary of the Company) holds the remaining approximately 2.5012% of the share capital of the Target Company, upon completion, the Company is expected to hold, directly and indirectly, the entire share capital of the Target Company.

As at the Latest Practicable Date,

(i) Huahong Group, one of the Vendors, is a substantial shareholder of the Company and a connected person of the Company under Chapter 14A of the Listing Rules; and

(ii) China IC Fund II, one of the Vendors, holds 29% of the equity interests in Hua Hong Manufacturing, a subsidiary of the Company. China IC Fund II also holds 48,334,249 RMB Shares as at the Latest Practicable Date, representing approximately 2.78% of the total issued share capital of the Company. Accordingly, China IC Fund II is a connected person of the Company at subsidiary level under Chapter 14A of the Listing Rules.

Therefore, as one or more of the applicable percentage ratios under Rule 14.07 of the Listing Rules in respect of the Proposed Acquisition exceeds 5%, the Proposed Acquisition constitutes a connected transaction of the Company which is subject to the reporting, announcement and Proposed Acquisition LR Independent Shareholders' approval requirements under Chapter 14A of the Listing Rules.

Save for the Directors who are considered to have material interests in the Proposed Acquisition under the Listing Rules and the Takeovers Code and have abstained from voting on the board resolutions, namely (i) Mr. Jun Ye who is also the Chairman of SAIL (a member of the Huahong Concert Group); (ii) Mr. Guodong Sun who was also a director of Shanghai IC Fund (being one of the Vendors and a member of the Huahong Concert Group) and holds certain position in Sino-IC Capital which in turn manages the China IC Fund II (being one of the Vendors and a member of the Huahong Concert Group); (iii) Mr. Bo Chen who is the vice president of Huahong Group and (iv) Ms. Chengyan Xiong who is the director of the capital and finance department of Huahong Group, none of the Directors is required to abstain from voting on the board resolutions approving the Proposed Acquisition and the transactions contemplated thereunder.

Proposed Non-public Issuance of RMB Shares

It is currently expected that the subscribers under the Proposed Non-public Issuance of RMB Shares will not be the connected persons of the Company and will not constitute a connected transaction under Chapter 14A of the Listing Rules.

TAKEOVERS CODE IMPLICATION

Application for Whitewash Waiver

As at the Latest Practicable Date, Huahong Group holds directly and indirectly 348,804,167 Shares (comprising 1,198,517 RMB Shares and 347,605,650 Hong Kong Shares), representing approximately 20.07% of the total issued share capital of the Company. In addition, as at the Latest Practicable Date, the Huahong Concert Group holds directly and indirectly 602,956,550 Shares (comprising 66,389,753 RMB Shares and 536,566,797 Hong Kong Shares), representing approximately 34.70% of the total issued share capital of the Company.

If the Proposed Acquisition materializes, it is expected that immediately after completion of the issuance of the Consideration Shares, the voting rights held by Huahong Concert Group in the Company will increase to approximately 41.16% (assuming (i) there will not be any further adjustment to the issue price of the Consideration Shares, (ii) there will not be any change in the total issued share capital of the Company since the Latest Practicable Date up to and including the date of issuance of the Consideration Shares and (iii) the Proposed Non-public Issuance of RMB Shares has not been completed). Accordingly, upon Completion, pursuant to Rule 26.1 of the Takeovers Code, Huahong Concert Group will be required to make a mandatory general offer for all the securities of the Company not already owned or agreed to be acquired by the Huahong Concert Group, unless the Whitewash Waiver from strict compliance with Rule 26.1 of the Takeovers Code is obtained from the Executive.

Further, Huahong Group, SAIL and China IC Fund II, being the top 20 shareholders of the Company among the Huahong Concert Group, have indicated that they will not participate in the Proposed Non-public Issuance of RMB Shares, and the Company has not received any indication from other parties in the Huahong Concert Group that any of them will participate in the Proposed Non-public Issuance of RMB Shares. On such basis, if the Proposed Non-public Issuance of RMB Shares materializes, it is expected that the voting rights held by the Huahong Concert Group in the Company will be diluted accordingly. For illustration purpose, the voting rights held by Huahong Concert Group in the Company shall be decreased to approximately 39.35% (subject to the assumptions set out in the section headed "11. Potential dilution effect on shareholding interests" below).

As such, the Completion is conditional upon, among other things, the Whitewash Waiver being granted by the Executive and approved by the Takeovers Code Independent Shareholders. An application has been made by Huahong Group (on behalf of itself and Huahong Concert Group) to the Executive for the granting of the Whitewash Waiver pursuant to Note 1 on dispensations from Rule 26 of the Takeovers Code. The Whitewash Waiver, if granted by the Executive, will be subject to (i) the approval of the Whitewash Waiver by at least 75% of the votes cast by Takeovers Code Independent Shareholders either in person or by proxy at the EGM; and (ii) the approval of the Proposed Acquisition by more than 50% of the votes cast by Takeovers Code Independent Shareholders either in person or by proxy at the EGM as required under the Takeovers Code. As at the Latest Practicable Date, the Executive has indicated that it is minded to grant the Whitewash Waiver. The Proposed Acquisition will not proceed if the Whitewash Waiver is not obtained or if the Whitewash Waiver is not approved by the Takeovers Code Independent Shareholders.

Special Deal in relation to the Proposed Non-public Issuance of RMB Shares

Pursuant to Article 41 of the Detailed Rules for the Implementation of Securities Issuance and Underwriting by Listed Companies on the Shanghai Stock Exchange 《上海證券交易所上市公司證券發行與承銷業務實施細則》, on the business day immediately preceding the start date of the issuance period, the listed company and the lead underwriter may provide subscription invitation letters to eligible specific parties. The recipients of the subscription invitation letters shall include investors who have submitted letters of intent after the announcement of the board resolution and the company's top 20 shareholders (but excluding (i) Huahong Group, SAIL and China IC Fund II which have indicated that they will not participate in the Proposed Non-public Issuance of RMB Shares and (ii) certain other Shareholders such as controlling shareholders and its related parties pursuant to the requirement of the Shanghai Listing Rules (both terms as defined thereunder)), and shall also include the following investors: (i) no fewer than 20 securities investment fund management companies; (ii) no fewer than 10 securities firms; (iii) no fewer than 5 insurance institutional investors.

The recipients of the subscription invitation letters must also comply with the relevant provisions of the Shanghai Stock Exchange. The listed company and the lead underwriter shall, in accordance with the relevant regulation set out above and the principles agreed upon in the subscription invitation letter, negotiate and determine the recipients of the subscription invitation letter.

The scope of targeted subscribers under the Proposed Non-public Issuance of RMB Shares will include not more than 35 specific target subscribers. Such specific target subscribers may include, but not limited to, institutional investors such as securities investment fund management company, securities firm, asset management company, insurance company, and other legal person or natural person investors in the PRC that comply with the regulations of the CSRC and the Shanghai Stock Exchange.

In addition, the identity of the target subscribers (and whether the target subscribers include existing RMB Shareholders) cannot be pre-determined as of the Latest Practicable Date. Therefore, given (i) the Proposed Non-public Issuance of RMB Shares may take place shortly after the completion of the Proposed Acquisition, (ii) the top 20 Shareholders of the Company may be approached pursuant to the above PRC regulatory requirements for invitation to subscribe for RMB Shares under the Proposed Non-public Issuance of RMB Shares, and (iii) their subscription (or any other subscriber who is a Shareholder) may be accepted by the Company, the Proposed Non-public Issuance of RMB Shares will potentially constitute a Special Deal under Rule 25 of the Takeovers Code which is not capable of being extended to all Shareholders and requires the consent of the Executive. Such consent, if granted, is expected to be subject to, among other things, (i) the Hong Kong Independent Financial Adviser publicly stating that in its opinion, the terms of the Special Deal are fair and reasonable and (ii) the approval of the Special Deal by the Takeovers Code Independent Shareholders by way of poll at the EGM.

Accordingly, the resolution in respect of the Special Deal will be submitted for Takeovers Code Independent Shareholders' consideration and approval at the EGM. (i) The Huahong Concert Group, (ii) Shareholders who have indicated to participate in the Non-public Issuance of RMB Shares before the EGM and their close associates (as defined under the Listing Rules), (iii) Shareholders who are involved in or interested in the Proposed Non-public Issuance of RMB Shares (otherwise than solely as Shareholders of the Company) and (iv) such other Shareholders who shall abstain from voting pursuant to the applicable laws, rules and regulations abstain from voting on the resolution to be proposed at the EGM to approve the Special Deal.

An application has been made by the Company to the Executive for its consent to the Special Deal pursuant to Rule 25 of the Takeovers Code. Such consent, if granted, is expected to be subject to, among other things, (i) the Hong Kong Independent Financial Adviser publicly stating that in its opinion, the terms of the Special Deal are fair and reasonable as far as the Takeovers Code Independent Shareholders are concerned, and (ii) the approval of the Special Deal by the Takeovers Code Independent Shareholders by way of poll at the EGM.

THE INDEPENDENT BOARD COMMITTEE

Pursuant to the Listing Rules and Rule 2.8 of the Takeovers Code, the Independent Board Committee, comprising all the independent non-executive Directors (namely Mr. Stephen Tso Tung Chang, Mr. Kwai Huen Wong, JP and Mr. Songlin Feng) has been established by the Company for the purpose of advising the Proposed Acquisition LR Independent Shareholders and the Takeovers Code Independent Shareholders on the Proposed Acquisition (including the grant of the Proposed Acquisition Specific Mandate and the approval of the Acquisition Agreement and the Supplemental Agreement), the Whitewash Waiver and the Special Deal. As

(i) Mr. Jun Ye is the Chairman of SAIL (a member of the Huahong Concert Group); (ii) Mr. Guodong Sun was a director of Shanghai IC Fund (being one of the Vendors and a member of the Huahong Concert Group) and holds certain position in Sino-IC Capital which in turn manages the China IC Fund II (being one of the Vendors and a member of the Huahong Concert Group); (iii) Mr. Bo Chen is the vice president of Huahong Group and (iv) Ms. Chengyan Xiong is the director of the capital and finance department of Huahong Group, each of them is not considered as independent for the purposes of giving advice or recommendations to the Takeovers Code Independent Shareholders under the Takeovers Code.

We, Innovax Capital Limited, have been appointed as the Hong Kong Independent Financial Adviser with the approval of the Independent Board Committee to advise the Independent Board Committee, the Takeovers Code Independent Shareholders and the Proposed Acquisition LR Independent Shareholders, in respect of the Proposed Acquisition, the Proposed Acquisition Specific Mandate, the Whitewash Waiver and the Special Deal.

OUR INDEPENDENCE

As at the Latest Practicable Date, we did not have any relationships or interests with the Company, its subsidiaries, its associates or their respective substantial shareholders or associates, the Huahong Concert Group, or any other parties that could reasonably be regarded as relevant in assessing our independence. In the previous two years from the date of the Circular, we have not acted as an independent financial adviser to the Independent Board Committee, the Takeovers Code Independent Shareholders, and the Proposed Acquisition LR Independent Shareholders of the Company for any transaction. Apart from normal professional fees paid or payable to us in connection with this appointment, no arrangements exist whereby we had received or will receive any fees or benefits from the Company or any other parties that could reasonably be regarded as relevant in assessing our independence. Accordingly, we consider that we are independent pursuant to Rule 13.84 of the Listing Rules.

BASIS OF OUR OPINION

In formulating our opinion to the Independent Board Committee, the Takeovers Code Independent Shareholders, and the Proposed Acquisition LR Independent Shareholders, we have reviewed, amongst other things, (i) the annual reports of the Company for the year ended 31 December 2023 (the "**2023 Annual Report**"); (ii) the annual report of the Company for the year ended 31 December 2024 (the "**2024 Annual Report**"); (iii) the interim report of the Company for the six months ended 30 June 2025 (the "**2025 Interim Report**"); (iv) the Acquisition Agreement and the Supplemental Agreement; (v) the Asset Valuation Report; and (vi) the prospectus for Huahong Semiconductor Limited's listing on the Shanghai Stock Exchange dated July 2023 (the "**SSE Prospectus**").

We have relied on the statements, information, opinions and representations contained in the Circular and the information and representations provided to us by the Company, the Directors and the management of the Company (the "**Management**"). We have assumed that all statements, information, opinions and representations contained or referred to in the

Circular, which have been provided by the Company, the Directors and the Management (for which they are solely and wholly responsible), were true and accurate at the time they were made and continue to be so as at the Latest Practicable Date. We have also assumed that all statements of belief, opinion and expectation made by the Directors in the Circular were reasonably made after due enquiry and careful consideration. The Directors have confirmed to us that no material facts have been withheld or omitted from the information provided, representations made or opinions expressed. We have no reason to suspect that any material facts or information has been withheld or to doubt the truth, accuracy and completeness of the information and facts contained in the Circular, or the reasonableness of the opinions expressed by the Directors and the Management. We believe 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, carried out any independent verification of the information provided by the Directors and the Management, nor have we conducted an independent investigation into the business and affairs of the Group. The Shareholders will be notified of any material changes to such information and representations or any change to our opinion as soon as possible in accordance with Rule 9.1 of the Takeovers Code. The Directors jointly and severally accept full responsibility for the accuracy of the information contained in the Circular and confirm having made all reasonable enquiries, that to the best of their knowledge, opinions expressed in this Circular have been arrived at after due and careful consideration and there are no other facts not contained in this Circular, the omission of which would make any statement in this Circular misleading.

This letter is issued for the information of the Independent Board Committee, the Takeovers Code Independent Shareholders, and the Proposed Acquisition LR Independent Shareholders solely in connection with their consideration of the Proposed Acquisition, the Proposed Acquisition Specific Mandate, the Whitewash Waiver and the Special Deal. Except for its inclusion in the Circular, this letter is not to be quoted or referred to, in whole or in part, nor shall this letter be used for any other purposes without our prior written consent.

PRINCIPAL FACTORS AND REASONS CONSIDERED

In arriving at our recommendation to the Independent Board Committee, the Takeovers Code Independent Shareholders, and the Proposed Acquisition LR Independent Shareholders, we have taken the following principal factors and reasons into consideration:

1. Background information of the Group

1.1 Principal activities of the Group

The Group is one of the global leaders in specialty process wafer foundry services and operates the most comprehensive specialty process platform in the industry. Established on 21 January 2005 and headquartered in Shanghai, the Company was listed on the Stock Exchange in 2014 and later on the Shanghai STAR Board in 2023. As a subsidiary of Huahong Group, which is ultimately controlled by Shanghai SASAC through a 51.74% direct stake and as to 15.29%, 15.29%, 9.73% and 7.96% by Shanghai SASAC and its subsidiaries, namely Shanghai International Group Corporation Limited (上海國際集團有限公司), Shanghai Guosheng Group

Co., Ltd (上海國盛(集團)有限公司) and INESA (Group) Co., Ltd. (上海儀電(集團)有限公司), being wholly-owned subsidiaries of Shanghai SASAC, and Shanghai Lingang Economic Development (Group) Co., Ltd. (上海臨港經濟發展(集團)有限公司)), being a non-wholly owned subsidiary of Shanghai SASAC, respectively. The Group operates advanced 8-inch and 12-inch wafer fabrication plants, focusing on high-reliability and specialty applications.

Anchored in its strategic objective of advancing "Specialty IC + Power Devices," the Group focuses on expanding specialty process technologies and provides diversified wafer foundry and related services across multiple specialty platforms in the following:

- Embedded/Standalone Non-Volatile Memory (NVM): Manufacturing solutions for memory chips used in automotive, industrial control, and consumer electronics.

- Power Devices: Production of MOSFETs, IGBTs, and other power management components for energy-efficient applications.

- Analog and Power Management: Production of a broad portfolio of analog ICs and power management solutions across multiple voltage levels and process nodes for diverse applications.

- Logic and RF: specialized manufacturing processes for communication chips (like Wi-Fi and Bluetooth) and image sensors, serving smartphones, tablets, and other smart devices.

These platforms cater to high-reliability sectors such as new energy vehicles, green energy, the Internet of Things (IoT), and automotive chips, supported by a "one-stop" service model that encompasses design, mask manufacturing, packaging, and testing. The Group leverages technical collaborations, such as licensing 65nm/55nm CMOS technology from the Target Company via HHGrace, to bolster its R&D and production capabilities, driving revenue growth during recent reporting periods.

Capital-intensive nature of semiconductor foundry industry

The semiconductor foundry industry exemplifies a business sector defined by its highly capital-intensive nature, requiring vast and sustained capital expenditure ("**CAPEX**") primarily focused on manufacturing infrastructure. This intensive investment is essential for the Group to maintain its competitive position, leverage its "8-inch + 12-inch" specialty process advantages, and drive capacity expansion. The core business revolves around the specialized manufacture and sale of semiconductor products.

The necessity for such high CAPEX stems from two primary strategic drivers: capacity expansion and technology migration. Continuous, massive spending is required to build and ramp up new production facilities to meet anticipated demand. Key capacity projects include the significant ramp-up of Fab 9, the Group's second 12-inch fabrication facility, which requires substantial spending (estimated, for example, at USD3.2 billion for equipment move-in in 2026). Management is committed to continuous capacity growth, expecting to initiate the second-phase capacity deployment for the second 12-inch production line located in Wuxi (the "**Hua Hong Manufacturing Project**") ahead of schedule by the end of 2025, alongside Fab 5 of the Target Company in the Proposed Acquisition to quickly increase scale.

Beyond scaling, a significant portion of CAPEX is directed toward maintaining technological leadership and upgrading process platforms. This funding supports essential process migration, such as transitioning from 90nm to 55nm/40nm, and progressive migration to more advanced process nodes as market conditions and technological requirements continue to evolve in the future. Furthermore, funds are consistently committed to innovation through specific initiatives like the Specialty Technological Innovation, Research and Development Project.

1.2 Historical financial performance and financial position of the Group

Financial performance

Set out below is the summary of the consolidated financial information of the Company as extracted from the 2023 Annual Report, 2024 Annual Report, and 2025 Interim Report.

	For the year ended 31 December			**For the six months ended 30 June**	
	2022	**2023**	**2024**	**2024**	**2025**
	US$ million (audited)	*US$ million (audited)*	*US$ million (audited)*	*US$ million (unaudited)*	*US$ million (unaudited)*
Revenue	2,475	2,286	2,004	939	1,107
Gross profit	844	487	205	80	112
Profit/(Loss) for the year/ period	407	126	(140)	(67)	(85)

Note: Certain financial information set out herein has been extracted from the accountants' report and rounded to the nearest million. Accordingly, figures shown may not add up precisely due to rounding differences. Readers are advised to refer to the relevant annual reports and interim reports of the Company for detailed financial information.

*For the six months ended 30 June 2025 ("**1H2025**") and 30 June 2024 ("**1H2024**")*

The Group reported revenue of US$1,107 million, representing an 18.0% increase from US$939 million in 1H2024, primarily driven by higher wafer shipments. By process platform, the Analog & Power Management segment delivered the strongest performance with double-digit year-on-year and quarter-on-quarter growth, supported by domestic supply chain localization and sustained artificial intelligence ("AI") server demand. The Embedded NVM platform advanced with the 55nm eFlash MCU entering volume production, targeting IoT, security, and automotive applications, while the Standalone

NVM platform's 48nm NOR Flash products also entered large-scale production. In addition, the Deep-Trench Super-Junction MOSFET platform achieved double-digit growth, driven by demand in the new energy and consumer electronics markets.

Gross profit rose to US$112 million, a 40.0% increase from US$80 million in 1H2024, supported by higher wafer shipments and improved production capacity utilization, though partially offset by increased depreciation charges. Gross margin improved from 8.5% to 10.1%, with both 8-inch and 12-inch lines operating at full utilization.

Nevertheless, the Group reported a net loss of US$85 million, compared with a net loss of US$67 million in 1H2024, representing a 26.7% increase. The widened loss reflected higher engineering wafer costs mainly from the Hua Hong Manufacturing Project, foreign exchange losses, and a reduced reversal of dividend withholding tax, which collectively drove up administrative expenses, other expenses, and income tax charges, offsetting the improvement in gross profit.

*For the year ended 31 December 2024 ("**FY2024**") and 31 December 2023 ("**FY2023**")*

Revenue declined to US$2,004 million, a 12.3% decrease from US$2,286 million in FY2023, reflecting an environment of falling average selling prices despite higher shipment volumes. While the global semiconductor market achieved moderate growth, supported by rapid AI sector expansion and a partial recovery in consumer electronics, intensified competition from newly released domestic supply exerted downward pressure on wafer foundry pricing.

Within this environment, the Analog & Power Management and Logic & RF platforms managed to achieve double-digit revenue growth, driven by AI-related applications and recovering consumer electronics demand. Leveraging its technological expertise and proactive sales strategies, the Group sustained an average annual capacity utilization rate close to 100%, securing a leading position among global wafer foundry peers.

However, profitability deteriorated sharply. Gross profit fell by 57.9% to US$205 million from US$487 million in FY2023, with the gross margin declining from 21.3% to 10.2%. The margin contraction was primarily due to pricing pressure, higher depreciation charges, and increased costs associated with new fab start-ups. Coupled with higher administrative expenses, reflecting increased R&D spending, the Group reported a net loss of US$140 million, compared with a net profit of US$126 million in FY2023.

*For the year ended 31 December 2023 ("**FY2023**") and 31 December 2022 ("**FY2022**")*

The Group recorded revenue of US$2,286 million, representing a 7.6% decline from US$2,475 million in FY2022, primarily due to lower average selling prices. Higher provisions for inventories, along with increased depreciation and utility costs, led to a 42.3% decrease in gross profit, from US$844 million in FY2022 to US$487 million in FY2023.

FY2023 was marked by a confluence of external challenges, including a global economic slowdown, weakened semiconductor demand, and rising raw material and labor costs. Based on our market research on the PRC foundry industry and discussion with the Management, the deterioration in performance was mainly attributed to subdued post-pandemic market demand. During the pandemic years, strict lockdown measures drove extraordinary demand for consumer electronics such as laptops, tablets, and smartphones, resulting in widespread over-ordering and excessive inventory accumulation across the supply chain. However, as economies reopened in 2023, consumer spending patterns shifted rapidly from goods to services, including travel, entertainment, and dining, leading to a sharp contraction in demand for electronic devices. At the same time, persistent inflation, higher interest rates, and global macroeconomic uncertainty dampened consumer confidence and business investment, particularly in sectors such as personal computing and smartphones, which together account for a significant portion of semiconductor demand. According to Gartner, a NYSE-listed global research and advisory firm founded in 1979, the global semiconductor market contracted by an estimated 11.1% in 2023, reflecting weakness in end-consumer markets and intensified pricing pressure across the supply chain.

In addition to weak market demand, the semiconductor industry in China was further constrained by the geopolitical environment. The export controls introduced by the U.S. Department of Commerce's Bureau of Industry and Security in October 2022, which restricted the export of advanced semiconductor manufacturing equipment to China, had a far-reaching impact in 2023. These restrictions limited access to critical tools and components from key suppliers, thereby capping domestic foundries' technological advancement at around the 7nm node and impeding further progress to 5nm and below. Even for existing production lines, the inability to secure timely parts and maintenance services constrained yields and efficiency, further exacerbating the sector's challenges amid already weak demand. As a result of the above, most of the Group's business segments recorded revenue declines, except the power discrete segment, which achieved double-digit growth driven by robust demand in the new energy vehicle and industrial sectors. Overall, the Group's gross margin narrowed by 12.8 percentage points to 21.3% compared with FY2022.

Despite these pressures, the Group remained resilient, refining its strategic plan, strengthening internal management, and stepping up investment in R&D to position itself for recovery. It ultimately achieved a net profit of US$126 million, though this represented a 69.0% decrease from US$407 million in FY2022, also reflecting reduced government R&D grants, higher engineering wafer costs, and increased finance costs.

Financial position

The following table sets out a summary of the consolidated statements of the financial position of the Group as at 31 December 2022, 2023, and 2024, and as at 30 June 2025, as extracted from the 2023 Annual Report, 2024 Annual Report, and 2025 Interim Report.

	As at 31 December			**As at 30 June**
	2022	**2023**	**2024**	**2025**
	US$ million (audited)	*US$ million (audited)*	*US$ million (audited)*	*US$ million (unaudited)*
Non-current Assets	3,979	4,373	6,583	6,892
Current assets	3,075	6,569	5,832	5,345
Cash and cash equivalents	2,009	5,585	4,459	3,847
Total assets	7,054	10,943	12,415	12,237
Non-current liabilities	1,537	1,956	1,946	1,952
Current liabilities	1,382	972	1,562	1,411
Total liabilities	2,919	2,928	3,508	3,364
Net assets	4,135	8,015	8,907	8,874
Share in Issue	1,307	1,717	1,718	1,727
NAV per Share (USD)	3.16	4.67	5.18	5.14

Note: Certain financial information set out herein has been extracted from the accountants' report and rounded to the nearest million. Accordingly, figures shown may not add up precisely due to rounding differences. Readers are advised to refer to the relevant annual reports and interim reports of the Company for detailed financial information.

As at 30 June 2025 and 31 December 2024

The Group's total assets remained relatively stable with a slight decrease of 1.4% from US$12,415 million as at 31 December 2024 to US$12,237 million as at 30 June 2025, while the total liabilities of the Group decreased slightly, with a decrease of 4.1% from US$3,508 million as at 31 December 2024 to US$3,364 million as at 30 June 2025.

The change in total assets was primarily attributable to a net increase of US$267 million in property, plant and equipment, mainly driven by the Hua Hong Manufacturing Project. The project has completed the move-in, installation, and qualification of the first batch of process and metrology equipment required for production, resulting in an increase in non-current assets. This was partially offset by a decrease of US$612 million in cash and cash equivalents. Such decrease reflected the Group's rising net flows used in investing activities, amounting to approximately US$2,672 million for the year ended 31 December 2024 and approximately US$880 million for the first half of 2025, respectively, partially offset by its net cash flow generated from operating and financing activities.

The changes on the total liabilities were mainly due to a 9.7% decrease in current liabilities from US$1,562 million to US$1,411 million. This is primarily due to decreased payable for capital expenditures.

As at 31 December 2024 and 31 December 2023

The Group's total assets recorded a 13.5% increase from US$10,943 million as at 31 December 2023 to US$12,415 million as at 31 December 2024, while the total liabilities had a 19.8% increase from US$2,928 million as 31 December 2023 to US$3,508 million as at 31 December 2024.

The increase in total assets was primarily driven by growth in non-current assets, notably a US$2,340 million increase in property, plant and equipment, partially offset by a reduction in current assets. The rise in property, plant and equipment was mainly attributable to continued capital investment in production capacity expansion, particularly the Hua Hong Manufacturing Project. In addition, other current assets increased by US$373 million, mainly due to increased value-added tax credits. These increases were offset by a US$1,126 million decrease in cash and cash equivalents. The decline in cash and cash equivalents was mainly due to US$2,672 million of outflows for investing activities, partly offset by US$1,182 million of capital contributions from non-controlling interests and US$459 million of operating cash inflows during the period.

Total liabilities increased, mainly due to a 60.7% rise in current liabilities from US$972 million to US$1,562 million. The increase was primarily driven by higher payables for capital expenditures, reflected in a US$421 million increase in other current liabilities, together with an US$88 million increase in the current portion of interest-bearing bank borrowings and a US$63 million increase in trade payables, which was attributable to increased purchase of materials.

As at 31 December 2023 and 31 December 2022

The Group's total assets recorded a strong 55.1% increase from US$7,054 million as at 31 December 2022 to US$10,943 million as at 31 December 2023, while the total liabilities maintained at a stable level from US$2,919 million as at 31 December 2022 to US$2,928 million as 31 December 2023.

The increase in total assets was attributable to growth in both current and non-current assets. The rise in non-current assets was mainly driven by a US$152 million increase in property, plant and equipment following the commencement of the Hua Hong Manufacturing Project, a US$92 million increase in equity instruments designated at fair value through other comprehensive income, and a US$142 million increase in long-term prepayments. Current assets also increased, primarily due to higher cash and cash equivalents. This was mainly supported by the US$2,942 million proceeds from the issuance of shares on the STAR Board, US$788 million capital contributions from non-controlling interests, and US$642 million net cash inflows from operating activities, partially offset by US$907 million of capital expenditure outflows.

Total liabilities recorded a net decrease during the year. Current portions of interest-bearing bank borrowings declined by US$234 million following the repayment of bank loans, while other payables and accruals decreased by US$163 million due to lower advance payments from customers. These decreases were partially offset by the drawdown of bank borrowings, which increased the long-term portion of interest-bearing bank borrowings by US$425 million.

Statement of cashflow

Set out below is the summary of the condensed consolidated statement of cash flows of the Company as extracted from the 2023 Annual Report, 2024 Annual Report, and 2025 Interim Report.

	For the year ended 31 December			**For the six months ended 30 June**	
	2022	**2023**	**2024**	**2024**	**2025**
	US$ million (audited)	*US$ million (audited)*	*US$ million (audited)*	*US$ million (unaudited)*	*US$ million (unaudited)*
Net cash flows generated from operating activities	751	642	459	138	220

	For the year ended 31 December			For the six months ended 30 June	
	2022	**2023**	**2024**	**2024**	**2025**
	US$ million	*US$ million*	*US$ million*	*US$ million*	*US$ million*
	(audited)	*(audited)*	*(audited)*	*(unaudited)*	*(unaudited)*
Net cash flows used in investing activities	(930)	(833)	(2,672)	(471)	(880)
Net cash flows generated from financing activities	672	3,782	1,150	1,206	34
Net (decease)/ increase in cash and cash equivalents	493	3,590	(1,062)	873	(626)

Note: Certain financial information set out herein has been extracted from the accountants' report and rounded to the nearest million. Accordingly, figures shown may not add up precisely due to rounding differences. Readers are advised to refer to the relevant annual reports and interim reports of the Company for detailed financial information.

As illustrated above, from 2022 to the first half of 2025, the Group's business remained highly capital-intensive. Significant cash outflows were incurred for capacity expansion and the upgrade of specialized process technologies, which were recorded under investing activities (including capital expenditure on property, plant and equipment and intangible assets). In addition, substantial R&D investments, although expensed through profit or loss as part of operating activities, further reduced the net operating cash inflows generated by the Group's business operations. As a result, the net cash generated from operating activities was insufficient to cover the sizable investing cash outflows over the period.

To bridge the funding gap and support the Group's ongoing capital investments and R&D initiatives, the Group relied on financing activities. This included, for example, the net proceeds raised from the issuance of shares on the STAR Board of the Shanghai Stock Exchange in 2023. As advised by Management, the continued and significant increase in net cash used in investing activities primarily reflected the Group's strategic plan to undertake substantial capital expenditure for the upgrade and expansion of its existing production facilities, the development and ramp-up of new production capacities, and the enhancement of specialized process technologies through R&D innovation.

2. Reasons for and benefits of the Proposed Acquisition

Proposed Acquisition

As stated in the Letter from the Board, upon Completion, the Company expects to further enhance its 12-inch wafer foundry capacity. The strengths of process platforms of the Company and the Target Company are highly complementary, which facilitate development of more comprehensive wafer foundry and supporting services covering a wider range of application scenarios and technical specifications. In addition, by way of consolidating its control over the Target Company, the Company could benefit from integrated management, process platforms, R&D resources, bespoke design and supply chain between the two companies. The Company believes that this could generate synergies to achieve cost reduction, improved market share and economies of scale.

The Company intends to implement further integration with the Target Company in respect of business, assets, finance, personnel, and organizational structure, based on considerations of operations and resource allocation. The integration aspects are as follows:

(1) Business Integration

Prior to completion of this transaction, the Target Company and the Company were competitors. Upon completion, the Target Company will become a controlled subsidiary of the Company, and its production and operations will be managed under the Company's governance framework. The two companies will achieve comprehensive resource sharing and complementary advantages in procurement, production, R&D, and sales, thereby driving coordinated business development.

(2) Asset Integration

Following completion, the Target Company will remain an independent legal entity with its own property rights, and its assets will remain separate. The Target Company will formulate plans for the purchase and disposal of significant assets based on its capacity requirements and will comply with the Company's approval procedures. Leveraging its management expertise and capital operation capabilities, the Company will optimize resource allocation in light of the Target Company's market prospects and actual conditions to improve asset utilization and strengthen the combined competitiveness of both companies.

(3) Financial Integration

After completion, the Company plans to appoint a chief financial officer and other necessary finance personnel to the Target Company to oversee accounting and financial management. The Target Company will be incorporated into the Company's financial management system, aligning its financial systems, accounting practices, and internal control procedures with those of the Company. All financial arrangements and approval processes will be centrally managed to ensure effective implementation of the Company's standards.

(4) Personnel Integration

To maintain stability and preserve the competitive strengths of the Target Company's existing team, the Company will retain its current business team. At the same time, to enhance the Target Company's capabilities and support business expansion, the Company will introduce high-caliber talent as appropriate.

(5) Organizational Integration

Upon completion, the Target Company will become a controlled subsidiary of the Company. While maintaining relative organizational independence, its daily operations and governance will strictly comply with the PRC Company Law, PRC Securities Law, the Company's management and internal control systems, its Articles of Association, and the requirements of the Shanghai Stock Exchange and the CSRC. The Company will gradually unify management mechanisms while preserving the Target Company's existing structure, strengthening oversight in business, finance, and compliance, ensuring decision-making authority over significant matters, reducing internal control risks, and improving overall governance and operational standards.

The Company and the Target Company both operate in the wafer foundry sector and belong to the same industry. The two exhibit significant synergies across process technology platforms, customer resources, supply chain management, technology, and production capacity in the following manner:

(1) Process Technology Platforms

The Target Company's 65/55nm and 40nm platforms cover standalone non-volatile memory, embedded non-volatile memory, logic and radio frequency, and high-voltage processes. Upon completion of the transaction, the Company will further enrich its range of process platforms to meet diverse market demands.

(2) Customers and Suppliers

Different customers have varying requirements for wafer foundry services. Following completion, the Company's expanded process platforms and technologies will enable it to better satisfy diverse customer needs and enhance overall competitiveness. Given the high global concentration of semiconductor equipment and material suppliers, the enlarged scale of the Company post-transaction will strengthen its position within the industry value chain.

(3) Technology and Capacity

The transaction will allow the Company to broaden its technological capabilities in 65/55nm and 40nm processes, accelerating product iteration and development. The Target Company currently has a monthly capacity of approximately 38,000 wafers; upon completion, the Company's total capacity will increase further, enabling it to meet growing customer demand.

In summary, the Company and the Target Company will achieve synergies in process technology platforms, customer resources, supply chain management, technology, and production capacity. The transaction will improve the Company's asset quality, and safeguard the interests of minority shareholder.

Further, during the Company's listing on the STAR Board on the Shanghai Stock Exchange, Huahong Group had undertaken to, in accordance with the national strategic deployment arrangement, after performing the approval procedures of the competent government departments, Huahong Group will inject the Target Company into the Company within three years of the listing. As such, this Proposed Acquisition is a demonstration of Huahong Group's commitment to the Company's listing, which is in line with market expectations.

The terms of the Acquisition Agreement and the transactions contemplated thereunder were agreed after arm's length negotiations between the parties thereto. The Directors consider that the Acquisition Agreement, the Supplemental Agreement, the Compensation Agreement and the transactions contemplated thereunder are on normal commercial terms which are fair and reasonable, and are in the interests of the Company and the Takeovers Code Independent Shareholders and the Proposed Acquisition LR Independent Shareholders as a whole.

In arriving at our view, we have taken into account the aforementioned factors. In addition, we have reviewed the Company's SSE Prospectus and financial reports, conducted market research on the foundry industry, engaged in discussions with the Management. Based on the above, we have taken into account the following factors:

(i) **Strategic Consolidation of Complementary Technologies**: According to the SSE Prospectus, both the Target Company and the Group provide foundry services on certain overlapping process platforms at the 65/55nm process node, specifically across three process platforms: standalone NVM, embedded NVM, and logic & RF. As disclosed in the SSE Prospectus, Huahong Group has made clear business delineation commitments, including keeping the overlapping portion below 30%. The Proposed Acquisition would allow the Group to integrate its specialty process capabilities with the Target Company's advanced 65/55nm CMOS and logic/RF technologies, thereby enhancing the Group's product and technology offering. This integration is expected to expand the Group's portfolio in key growth markets such as new energy, customer electronics, IoT, automotive, and industrial applications;

(ii) **Operational and Cost Efficiencies**: The current operational ties, such as the Target leasing facilities from HH Grace, the Group settling utility costs on behalf of the Target, and the technology licensing arrangement could be streamlined under a single entity, reducing administrative overhead and optimising resource allocation. This would eliminate intercompany transactions (e.g., utility payments, leasing of production facilities, technology licensing), lowering costs and enhancing efficiency across the 12-inch wafer fabs;

(iii) **Resolution of Potential Competition**: Despite mitigated overlaps, the acquisition would eliminate any residual competitive risks in logic/RF and NVM segments, aligning with the Group's commitment to inject the Target Company into the Group. This move would fulfill the Group's pledge to prioritize business opportunities for the Group, ensuring long-term market stability;

(iv) **Favorable Industry Prospects:** The global semiconductor foundry industry is entering a new growth cycle, supported by strong demand from AI, high-performance computing, and automotive electronics. According to Semiconductor Equipment and Materials International (the "**SEMI**"), the global industry association for electronics supply chains, worldwide semiconductor sales are expected to grow at a compound annual growth rate of approximately 9% between 2025 and 2030, reaching USD1 trillion by 2030. Concurrently, mature process nodes, which underpin automotive, industrial applications, communications and consumer electronics are forecasted to grow steadily. According to the SEMI, wafer fab equipment sales for foundry and logic applications are forecasted to grow annually at around 6%, reaching US$69.0 billion in 2026. Yole Group, a leading market research and consulting firm specializing in semiconductor industry, forecasts China to dominate the global foundry landscape by 2030, accounting for 30% of installed capacity, outpacing Taiwan, South Korea, and Japan. Against this backdrop, the Group's consolidation of advanced and specialty process capabilities positions it to capitalize on both high-growth advanced applications and resilient demand for mature technologies, thereby aligning its long-term strategy with favorable industry trends and enhancing its competitive resilience.

(v) **Industry Challenges and Competitive Positioning**: While the long-term prospects of the semiconductor foundry industry are favorable, the market is also facing intensified competition and oversupply pressures, particularly in China where substantial new mature-node capacity has been released. These dynamics have exerted downward pressure on wafer pricing, compressing margins across the industry. The Proposed Acquisition would better equip the Group to navigate these challenges by expanding its technology and product portfolio, consolidating advanced and specialty process platforms, and strengthening economies of scale. The integration would enable the Group to compete on differentiation, through embedded and standalone NVM, logic/RF, and specialty power devices, rather than purely on price, thereby enhancing resilience against cyclical downturns. In this way, the Group will be better positioned to sustain profitability, defend market share, and continue its leadership role in China's foundry industry despite a more competitive supply landscape.

Taking into account the above, we concur with the Board that the Proposed Acquisition is expected to benefit the long-term development of the Group through enhancing its financial performance and further strengthening the Group's market position in the semiconductors industry, and are in the interests of the Company and the Takeovers Code Independent Shareholders and the Proposed Acquisition LR Independent Shareholders as a whole.

3. Principal terms of the Agreement

Set out below are the summaries of the principal terms of the Acquisition Agreement (as supplemented by the Supplemental Agreement). Shareholders and potential investors are advised to read in full further details of the Acquisition Agreement (as supplemented by the Supplemental Agreement) as set out in the letter from the Board in the Circular.

3.1 Target assets

The Company has conditionally agreed to purchase and the Vendors have conditionally agreed to sell, the Target Assets, being approximately 97.4988% of the equity interests in the Target Company, at the Total Consideration.

3.2 Basis of Consideration

Pursuant to the relevant laws, rules and regulations in the PRC, the parties have agreed to engage, the Valuer, a qualified asset appraisal agency in the PRC, to conduct a valuation on the Target Company and issue the Asset Valuation Report with the Valuation Benchmark as Date of 31 August 2025. In compliance with the requirement under Rule 11.4 of the Takeovers Code, the Valuer has confirmed that there is no material difference in the Valuation between the Valuation Benchmark Date and the date of the Valuation Report.

According to the Asset Valuation Report, the appraised value of the Target Company as at the Valuation Benchmark Date, which were primarily determined based on the market approach, is RMB8,480 million. The amount of final Total Consideration shall be RMB8,267,902,153.26. In considering the Total Consideration, even though the net asset value of the Target Group (approximately RMB2.002 million as set out in Appendix II to this Circular) is smaller than that of the appraised value based on the Asset Valuation Report, the Board understood that the difference lies in particular in the full description of fixed assets under accounting standards.

The wafer foundry industry in which the Target Company operates is characterized by its capital-intensive nature. Semiconductor equipment is depreciated over a financial period of seven years, which is significantly shorter than its actual economic useful life. At present, the Target Company's fixed assets have only recently completed their financial depreciation cycle, resulting in a relatively low book value and asset renewal ratio. However, this is merely a temporary accounting phenomenon and does not materially affect its actual production capacity. The Target Company remains fully capable of continuing as a going concern remains stable.

The Target Company's net asset scale is at a relatively low point in its corporate lifecycle, while its financial position as at 31 August 2025 has recovered in line with the industry rebound. As a result, its return on equity (ROE) for the year 2024 and eight months ended 31 August 2025 is significantly higher than the industry average. Please refer to Appendix II to this Circular for the audited financial information of the Target Company for the two years ended 31 December 2024 and eight months ended 31 August 2025.

Having discussed with the Valuer to understand the justification of selection of the valuation method, the assumptions and bases of valuation, the Board noted that the net asset value of the Target Company, which mainly represents the historical accounting value of its assets and liabilities, may not fully reflect its underlying fair value and business prospects and thus may not be an appropriate basis of valuation of a business of an operating nature. The Board considers that a significant portion of the future demand for the Target Company's products is expected to be driven by the growth of AI and next-generation technologies. The adoption of the market approach by the Valuer, which captures the market's assessment of value through the trading multiples of comparable listed companies, is therefore more appropriate than relying solely on book value for the purpose of the Target Company's valuation.

Based on the foregoing, the Board in the letter from the Board considers that the transaction amount (and thus the final Consideration) is fair and reasonable and in the best interests of the Shareholders.

Upon arms' length negotiations between the parties taking into account, among others, the appraised value of the Target Assets under the Asset Valuation Report, it has been agreed that the final Total Consideration shall comprise 190,768,392 Consideration Shares (together with such cash consideration in lieu of fractional shares), to be issued to the Vendors in the following proportion.

Vendor	Target Asset sold *(%)*	Corresponding value in the Target Asset *(RMB)*	Consideration Shares to be issued	Cash consideration in lieu of fractional Shares *(RMB)*
Huahong Group	63.5443	5,388,551,195.69	124,332,053	18.67
Shanghai IC Fund	15.7215	1,333,186,465.21	30,761,109	1.15
China IC Fund II	10.2503	869,227,665.01	20,056,014	18.25
Guotou IC Fund	7.9827	676,936,827.35	15,619,216	5.91
Total	97.4988	8,267,902,153.26	190,768,392	43.98

Further, the parties have considered the significant increase in price in the RMB Shares of the Company since the Announcement, the available cash reserve of the Company, the working capital requirements and tax obligations of the Vendors, it has been decided that the Total Consideration shall not comprise any cash element (except for such cash consideration in lieu of fractional shares). Notwithstanding the Group's substantial cash and bank balances, (i) the Group has substantive capital expenditure needs arising from its future business development plans in the upcoming years, including expansion and developments of the 8-inch and 12-inch foundry fabs of HHGrace, Hua Hong Wuxi and Hua Hong Manufacturing, and (ii) a substantial portion of the Group's cash possessed by the Group has been budgeted for dedicated long-term strategic purposes, as the semiconductor industry is a sector with intensive need for capital and talent acquisition, with rapid iteration of technologies from wafer manufacturing processes to downstream product demands. Having considered the need of cash set out above, the Board has decided to settle the Total Consideration by issuing new RMB Shares instead of using the Group's cash reserve.

Our view:

According to the Acquisition Agreement and the Supplemental Agreement, the Total Consideration will be settled solely by the issuance of RMB shares. We consider that it is beneficial to the Company and its existing Shareholders as it preserves the Group's cash resources for strategic development needs. The semiconductor foundry industry is highly capital-intensive and requires substantial and continuous investment in R&D, advanced process development, and capacity expansion to maintain technological competitiveness. As advised by the Management, the Group continued the rapid capacity ramp-up and volume production of the Hua Hong Manufacturing Project, which commenced risk production at the end of 2024. Due to the smooth progress of the first phase, the Company anticipates initiating the second-phase capacity deployment ahead of schedule by the end of 2025. Retaining cash on hand enables the Group to support future capital expenditure, strengthen its technology roadmap, and respond to market opportunities without increasing financial leverage or constraining liquidity. By adopting a non-cash settlement structure, the Group is able to complete the Proposed Acquisition without reducing its financial flexibility, while allowing the economic risks and benefits of the transaction to be shared with the Vendors through equity participation.

3.3 The Consideration Shares

In accordance with the relevant PRC laws and regulations, the issue price of the Consideration Shares shall be RMB43.34 per Consideration Share, representing not less than 80% of the Average Trading Price of the RMB Shares for the 120 trading days prior to the Pricing Benchmark Date. Notwithstanding the fact that the 120-day average price presented a lower average price, the 120 trading days was selected as the determination basis in light of the price fluctuation of the RMB Shares prior to the signing of the Acquisition Agreement, as a result, the longer reference period (i.e. 120 trading days, instead of the other reference period 20 trading days or 60 trading days), was chosen by the parties, as it neutralized the impact of the price rally prior to the signing of the Acquisition Agreement to achieve a fair and reasonable pricing basis.

During the period between the Pricing Benchmark Date and the date of issue of the Consideration Shares, in case of any ex-rights or ex-dividends events of the Company such as distribution of cash dividends, bonus issues, rights issues, allotment of shares, conversion of share premium into share capital or capitalization issues, the issue price of the Consideration Shares will be adjusted in accordance with the relevant PRC laws and regulations in the manner stated in the letter from the Board.

The Consideration Shares will be issued under the Proposed Acquisition Specific Mandate to be sought at the EGM.

3.4 Lock-up period

Huahong Group has undertaken that it shall not transfer any of the Consideration Shares within 36 months from the date of issue of the Consideration Shares. In the event that (i) the average closing price of the Shares for any 20 consecutive days within 6 months of Completion or (ii) the closing price of the Shares at the end of the 6-month period after the Completion is lower than the Consideration Shares issue price, the lock-up period on the Consideration Shares obtained by Huahong Group shall automatically extend for an additional 6-month period.

Shanghai IC Fund has undertaken that it shall not transfer any of the Consideration Shares within 12 months from the date of issue of the Consideration Shares. In the event that Shanghai IC Fund is regarded as a private equity fund under the applicable laws and has held its interests in the Target Assets for 48 months at the time when it obtains the Consideration Shares, and provided that (i) it is not the Company's controlling shareholder, ultimate beneficial owner or their respective associates, and (ii) it has not obtained control over the Company through the Proposed Acquisition, the lock-up period on the Consideration Shares obtained by Shanghai IC Fund shall be shortened to 6 months.

Each of China IC Fund II and Guotou IC Fund has undertaken that it shall not transfer any of the Consideration Shares within 12 months from the date of issue of the Consideration Shares. In the event that any of China IC Fund II and Guotou IC Fund has not held its interests in the Target Assets for 12 months at the time when it obtains the Consideration Shares, the lock-up period on the Consideration Shares obtained by such Vendor shall be extended to 36 months.

The final adjusted lock-up period of each of the Vendors will be determined at the Completion of the Proposed Acquisition and will be disclosed in the announcement in relation thereto. The lock-up undertaking shall also be applicable to any additional RMB Shares received by the Vendors as a result of bonus issues, capitalization issues, and/or conversion of share premium into share capital after completion of the Consideration Share Issuance.

Our view

Based on our discussion with the Management, the lock-up arrangement was determined in accordance with Article 47 of the "Administrative Measures for Major Asset Restructuring of Listed Companies" (《上市公司重大資產重組管理辦法》). Based on our review, it appears that the lock-up arrangement is consistent with the stipulations outlined in this regulation.

We view the lock-up arrangement as a vital safeguard for shareholder value and market stability. By restricting share transfers for 12 to 36 months, it mitigates the risk of a supply shock and protects the share price from volatility. Moreover, this commitment reflects the Vendors' enduring confidence in the Group's future prospects. We also noted that the use of "lock-up" mechanism is common amongst the Comparable Issuances (as defined in the analysis below) and the range of lock-up periods of the Comparable Transactions is between 12-months to 36 months. Since the Proposed Acquisition imposes a lock-up period requirements of 12-months and 36-months, which are in line with the market practice, we therefore are of the view that such lock-up period is reasonable.

3.5 Conditions precedent

The effectiveness of the Acquisition Agreement is conditional upon the fulfilment of all of the following conditions:

(i) the approval of the Proposed Acquisition by the Board and the Proposed Acquisition Independent Shareholders and the Takeovers Code Independent Shareholders at the EGM of the Company;

(ii) the approval of the Proposed Acquisition by the internal and external competent governing bodies of the Vendors;

(iii) the approval of Proposed Acquisition by the shareholders of the Target Company, and the waiver of the first right of refusal by the shareholders of the Target Company having been obtained;

(iv) the approval of the Proposed Acquisition by the state-owned assets supervision and administration authorities;

(v) the granting of a Whitewash Waiver by the Executive and the approval of the same by the Takeovers Code Independent Shareholders at the EGM of the Company;

(vi) the approval of the Proposed Acquisition by the Shanghai Stock Exchange and registration by the CSRC;

(vii) the Proposed Acquisition having obtained other necessary prior approvals, approvals or consents (if any) as required by laws, regulations and regulatory authorities.

There is no long stop date under the Acquisition Agreement in respect of the fulfilment and/or waiver of the conditions precedent, which is consistent with similar transactions undertaken by other A+H companies. Notwithstanding the lack of long stop date, the Company is of the view that the transaction terms, on the whole, are fair and reasonable given (1) the final Consideration shall be supported by a valuation, and the parties to the transactions have also considered other factors (such as price fluctuation, certainty of the transaction) when determining the pricing of the Consideration Shares; (2) after the completion of the Proposed Acquisition, the shareholders' equity attributable to the parent company, the net profit attributable to the owners of the parent company and the basic earnings per share of the Company will increase, evidencing that is be no harm to the interests of minority shareholders; (3) the setting of a long stop date may also increase the uncertainty of the Proposed Acquisition, causing market confusion and may in turn harm the interests of the minority shareholders; (4) in the event that the Proposed Acquisition is not completed within 12 months of the EGM (i.e. the validity period of the relevant resolution), the Company shall be required to convene another extraordinary general meeting, and the shareholders shall then be entitled to vote to decide whether to proceed with the Proposed Acquisition. The parties will however endeavours to take necessary steps to procure the fulfillment of the conditions precedent and proceed with Completion.

In respect of the condition set out in paragraph (vii) above, as at the date of this letter, the Company is not aware of any other approval and/or filings which are required to be obtained by it in respect of the Proposed Acquisition.

None of the above conditions precedent may be waived by any party to the Acquisition Agreement. Other than conditions set out in paragraph (i) (in respect of the approval by the Board), (ii) and (iii) above, none of the conditions precedent has been fulfilled as at Latest Practicable Date. The Proposed Acquisition will not proceed if the Whitewash Waiver is not obtained or if the Whitewash Waiver is not approved by the Takeovers Code Independent Shareholders.

Our view

Although there is no long stop date stipulated under the Acquisition Agreement as supplemented by the Supplemental Agreement, we note that the Completion and the issuance of the Consideration Shares are subject to the satisfaction of certain conditions precedent, including obtaining the requisite approvals from the relevant regulatory authorities in Hong Kong and the PRC as well as the shareholders of the Company. These approvals are being diligently pursued by the parties, and the absence of a long stop date primarily reflects the inherent uncertainty in the approval timeline rather than any lack of commitment to Completion. In this regard, we consider that the absence of a long stop date does not materially affect the fairness and reasonableness of the transaction terms, given that Completion remains conditional upon clearly defined regulatory and shareholder approvals.

3.6 Completion

Upon registration of the Proposed Acquisition with the CSRC, the parties agree to cooperate and complete the necessary steps in respect of completion in accordance with applicable laws and regulations within the validity period of the registration. Completion of the Proposed Acquisition shall take place upon completion registration of the Target Assets with the relevant administration of market regulation of the PRC, which is expected to be within one year from the date of the CSRC's agreement to register.

4. Compensation Agreement

Pursuant to the Guidance on the Application of Regulatory Rules – Listing Category No. 1. (監管規則適用指引–上市類第1號) issued by the CSRC ("CSRC Listing Guidance Category No. 1"), where a listed company acquires asset(s) from its controlling shareholder (as defined under the Shanghai Listing Rules) which involve cash consideration or issuance of consideration shares, the controlling shareholder shall compensate the listed company for any impairment of target asset. Accordingly, on 31 December 2025, the Company and Huahong Group entered into the Compensation Agreement, pursuant to which, for a period of three financial years (including the year in which the Proposed Acquisition is completed and the two subsequent financial years, a period which follows the CSRC Listing Guidance Category No. 1), the Company shall conduct an impairment test on the total value of the assets of the Target Assets upon the end of the financial year end, based on a valuation conducted by a qualified valuer under the PRC Securities Laws with the valuation method to be determined.

In the event of an impairment in the Target Assets in any of the three financial years, Huahong Group shall compensate the Company for the impairment value, multiplied by the proportion of Huahong Group's share in the Total Consideration (representing approximately 65.2%) by way of (i) subject to compliance with laws, rules and regulations, the Company's repurchase of a corresponding number of Consideration Shares held by Huahong Group in consideration of RMB1; and (ii) cash. The Company shall within 30 working days of the impairment report, make an announcement on the compensation arrangement setting out the impairment loss recorded and the compensation received from Huahong Group (if any) in compliance with its obligation thereunder, after which, Huahong Group shall settle such compensation within 30 working days of the announcement. The amount of impairment made and compensation received/receivable shall be disclosed in the Company's annual report.

As the Compensation Agreement has been entered into upon arm's length negotiation with Huahong Group in accordance with the requirements of the CSRC Listing Guidance Category No. 1 and allows the Company to hedge against the commercial and financial risks of impairment loss arising from the Proposed Acquisition and the conduct of the Target's business going forward, the Board considers that the terms of the Compensation Agreement are fair and reasonable and in the best interests of the Takeovers Code Independent Shareholder and the Proposed Acquisition LR Independent Shareholders. The Company shall disclose (i) whether the Target Company has recorded any impairment loss in each of the financial years covered by the Compensation Agreement, (ii) whether the compensation mechanism is triggered and (iii) the amount of compensation received thereunder, as and when appropriate.

Our view

The above compensation arrangement provides downside protection to existing Shareholders in the event that the Proposed Acquisition does not achieve the expected performance or synergy outcomes which result in impairment. By requiring Huahong Group to compensate for any impairment in the value of the Target Assets, this mechanism ensures that Huahong Group effectively guarantees the value of the Target Assets for three financial years, effectively safeguarding the Company from bearing the full financial impact of underperformance. Additionally, it may help preserve shareholder value by mitigating dilution if the repurchase of Consideration Shares is chosen, ensuring that the economic risk of potential impairment is shared by the Vendors. This alignment of interests between Huahong Group and existing Shareholders underscores that the Compensation Agreement not only mitigates the commercial risk of asset devaluation but also serves as a powerful anti-dilutive measure that protects the interests of Takeovers Code Independent Shareholders and the Proposed Acquisition LR Independent Shareholders.

5. Information on the Target Group

5.1 Background and businesses of the Target Group

The Target Company is a limited liability company established in the PRC on 18 January 2010. As at the Latest Practicable Date, its issued share capital was owned as to approximately 63.5443% by Huahong Group, 15.7215% by Shanghai IC Fund, 10.2503% by China IC Fund II, 7.9827% by Guotou IC Fund, and 2.5012% by HH Grace, a wholly-owned subsidiary of the Company. Accordingly, the Target Company is controlled by Huahong Group, which is ultimately owned by the Shanghai SASAC, holding a 51.74% direct interest and the remaining 48.26% through wholly-owned subsidiaries and a non-wholly owned subsidiary. As disclosed in the letter from the Board, Huahong Group is a high-tech industry group which primarily focuses on IC manufacturing, R&D of advanced IC manufacturing process, IC systems integration and application services, sale of electronic component and overseas venture capital investment.

The Target Company, with its logic processes as foundation, also specializes in specialty processes, providing wafer foundry and supporting services to design companies, IDM companies, and other system companies, covering diverse process platforms including logic and radio frequency (RF), embedded/standalone NVM, and high voltage IGBT.

Building on over 15 years of technical experience in the semiconductor manufacturing, the Target Company persists in independent innovation, while continuing to research, develop, and master core key technologies for specialty processes. Currently, it operates the first fully automated 12-inch integrated circuit foundry production line in Mainland China, with process capabilities reaching the 65/55nm and 40nm technology nodes, and a design capacity of 38,000 wafers per month. The Target Company leases its primary production facility, a 12-inch wafer fab in Shanghai, from the Group under a market-based lease agreement. It has licensed its 65nm/55nm CMOS process technology to the Group, enabling the development and industrialization of high-reliability products such as automotive-grade NOR Flash with capacities above 32Mb. The licensing arrangement covers technical documentation, process design kits, and ongoing support, allowing the Group to adapt these nodes to its specialty process platforms.

The Target Company's extensive process portfolio provides customers with complete technology solutions, which are applicable across four major end-product markets: mobile communications, consumer electronics, IoT, and automotive electronics. The chip products manufactured cover baseband processors, image sensors, small and medium-sized LCD display driver chips, touch screen controllers, integrated touch and display driver chips, wireless connectivity, RF, microprocessors, smart cards, set-top box integrated chips, and power management chips.

5.2 Financial performance, financial position and cash flows of the Target Company

The following table sets out a summary of the combined statements of profit or loss of the Target Company for the three years ended 31 December 2022, 2023 and 2024, and for the eight months ended 31 August 2025, as extracted from the Historical Financial Information of the Target Company set out in Appendix II to the Circular:

	For the year ended 31 December			**For the eight months ended 31 August**	
	2022	**2023**	**2024**	**2024**	**2025**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
	(audited)	*(audited)*	*(audited)*	*(unaudited)*	*(audited)*
Revenue	5,492,787	2,371,122	4,476,976	2,878,119	3,401,413
Gross profit/(loss)	1,930,417	(152,917)	302,181	(66,510)	787,059
Profit/(Loss) for the year/period	2,184,333	(372,291)	521,524	(20,563)	514,643

The Target Company recorded revenue of RMB2.4 billion in FY2023, representing a significant decline of 56.4% from RMB5.5 billion in FY2022. The downturn was primarily attributable to (i) weak post-pandemic market demand and inventory correction across the semiconductor supply chain, which forced brands to cut orders with the Target Company, consistent with broader industry trends, and (ii) the impact of export controls imposed by the United States. The effects of these measures were felt throughout 2023, constraining access to critical tools and components from key suppliers and weighing on the Target Company's overseas business.

In particular, revenue from North America fell sharply from RMB1.7 billion in FY2022 to RMB0.4 billion in FY2023, representing a steep contraction of 76.5%. Affected by the two major factors mentioned above, the Target Company recorded significant write-down of inventories to net realisable value of RMB184.0 million in the FY2023, compared to only RMB5.4 million in the preceding year. This resulted in a gross loss for the year and placed significant downward pressure on overall profitability.

The deterioration in earnings was further aggravated by a sharp reduction in government grants, which fell from RMB380.1 million in FY2022 to merely RMB10.4 million in FY2023 as the R&D project subsidies from government were largely recognised upon completion and acceptance in FY2022, as well as a significant increase in administrative expenses arising from higher R&D expenditure. Consequently, the Target Company recorded a net loss of RMB372.3 million for FY2023.

In FY2024, the Target Company achieved a strong rebound, with revenue rising to RMB4.5 billion, representing an increase of 87.5% year-on-year. The recovery was mainly driven by improving market conditions, particularly the rapid expansion of AI applications which spurred demand for semiconductor components, as well as improvement in the downstream consumer electronics industry. Although revenue from North America continued to decline in FY2024 due to the ongoing impact of U.S. export restrictions, this was more than offset by a substantial increase in revenue from Asia. This swift diversification strategy mitigated regional exposure and enabled the Target Company to broaden its customer base and enhance business resilience.

Supported by the strong sales recovery and a partial reversal of previously written-down inventories to net realisable value, the Target Company returned to profitability in FY2024, recording gross profit of RMB302.2 million. The Group also recorded a turnaround to a net profit of RMB521.5 million in FY2024, compared with a net loss in FY2023. The improvement was mainly attributable to the significant recovery in gross profits, the recognition of technical development service income from transferring existing developed processes to the Group and the increase in interest income.

The robust growth momentum continued into FY2025, with revenue for the first eight months of the year increasing by 17.2% from RMB2.9 billion in the corresponding period of FY2024 to RMB3.4 billion. The growth was mainly driven by the increase in shipment volumes resulting from further improvement in downstream consumer electronics demand, coupled with a rise in average selling prices, while gross profit and gross profit margin also improved owing to the increase in average selling price and the improvement in capacity utilization rate. As a result, the Target Company recorded strong profitability of RMB514.6 million for the first eight months of FY2025.

Financial position

The following table sets out the combined statement of financial position of the Target as at 31 December 2022, 2023, 2024 and as at 30 June 2025, as extracted from Historical Financial Information of the Target Company set out in Appendix II to the Circular:

	As at 31 December,			**As at 31 August,**
	2022	**2023**	**2024**	**2025**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*
	(audited)	*(audited)*	*(audited)*	*(unaudited)*
Total assets	10,043,335	8,899,821	6,258,892	7,258,503
Total liabilities	8,933,922	8,157,415	4,991,960	5,256,589
Net current assets	476,217	426,688	1,669,214	2,981,018
Net assets	1,109,413	742,406	1,266,932	2,001,914

As illustrated in the table above, the Target Company's financial position has shown continuous improvement from 2024. As at 31 August 2025, the Target Company maintained a solid financial position, with net current assets of approximately RMB3.0 billion and net assets of approximately RMB2.0 billion. The principal assets of the Target

Company as at 31 August 2025 comprised (i) property, plant and equipment of approximately RMB1.7 billion; (ii) right-of-use assets of approximately RMB0.4 billion; (iii) inventories of approximately RMB1.4 billion; (iv) trade and notes receivables of approximately RMB0.5 billion; and (v) cash and cash equivalents of approximately RMB3.0 billion. The major liabilities as at the same date mainly consisted of: (i) interest-bearing bank borrowings of approximately RMB3.7 billion; (ii) trade payables of approximately RMB0.6 billion; and (iii) lease liabilities of approximately RMB0.5 billion.

Statement of cashflows

The following table sets out a summary of the statements of cash flows of the Target Company for the three years ended 31 December 2022, 2023 and 2024, and for the eight months ended 31 August 2025, as extracted from the Historical Financial Information of the Target Company set out in Appendix II to the Circular:

	For the year ended 31 December			**For the eight months ended 31 August**	
	2022	**2023**	**2024**	**2024**	**2025**
	(audited)	*(audited)*	*(audited)*	*(unaudited)*	*(audited)*
Cash flow (used in)/generated from operating activities	1,743,522	(523,440)	1,960,930	2,063,258	979,728
Cash flow (used in)/generated from investing activities	(2,013,509)	(263,488)	764,297	960,768	1,368,935
Cash flow (used in)/ generated from financing activities	(500,724)	(272,864)	(3,701,645)	(540,432)	691,069
Net (decrease)/increase in cash and cash equivalents	**(770,711)**	**(1,059,792)**	**(976,418)**	**562,058**	**3,039,732**

As demonstrated in the table, the Target Company has maintained largely positive cash flows from operating activities throughout the period, with the exception of the year ended 31 December 2023, which reflected the temporary deterioration in the financial performance previously discussed. The Target Company recorded net cash used in investing activities for the two years ended 31 December 2023. However, this outflow was not predominantly driven by core capital expenditure on property, plant, and equipment, but was largely attributable to strategic placements of fixed deposits held at banks with maturity exceeding three months, alongside the purchase of PP&E, prepaid lease payments, and intangible assets.

In terms of financing activities, the Target Company recorded net cash outflows across all annual periods, indicating regular debt servicing. A significant reversal occurred during the eight months ended 31 August 2025, where there was a net cash inflow generated from financing activities. This shift was a result of increased capital contribution from shareholders and new bank and other borrowings that collectively exceeded the repayment of existing obligations during that specific period.

The net effect of these movements resulted in a net decrease in cash and cash equivalents over the three years ended 31 December 2024, confirming the overall liquidity pressure during the heavy investment and borrowing phase. Conversely, the successful execution of financing and treasury activities in the most recent period led to a substantial net increase in cash and cash equivalents during the eight months ended 31 August 2025, significantly strengthening the Target Company's current liquidity position.

6. Assessment of the Total Consideration

The Total Consideration comprises 190,768,392 Consideration Shares to be issued to the Vendors at an issue price of RMB43.34 per Consideration Share, giving rise to a corresponding value in the Target Company of RMB8,267,902,153.26, which represents approximately 97.4988% of the appraised value of the Target Company under the Asset Valuation Report and corresponds to the same shareholding percentage in the Proposed Acquisition of the Target Company. To assess the fairness and reasonableness of the Total Consideration, we have considered the following factors:

6.1 Valuation of the Target Company

The Company engaged the Valuer to prepare a Valuation Report in respect of the fair value of 100% equity interest of the Target Company as of 31 August 2025 (the "**Valuation**"). As set out in the Valuation Report contained in Appendix V of the Circular, the appraised value of 100% equity interest of the Target Company is RMB8.48 billion as at 31 August 2025. In reviewing the Valuation Report, we have complied with the requirements under Rule 13.80(2)(b) Note 1(d) of the Listing Rules and Rule 11.1(b) of the Takeovers Code. Our letter in relation to the Valuation Report under Rule 11.1(b) of the Takeovers Code is set out in Appendix VI to the Circular. We have enquired with the Valuer as to their independence and were given to understand that the Valuer is an independent third party of the Group, the Vendors and their respective connected persons. The Valuer also confirmed to us that they were not aware of any relationship or interest between themselves and the Group, the Vendors or any other parties that would reasonably be considered to affect their independence to act as the independent valuer of the Company. We have also reviewed the supporting documents on the qualifications of the Valuer and discussed the same with the Valuer. We noted that the persons signing the Valuation Report, whom are partners of the Valuer, have more than 15 years of experience in providing valuation services to listed companies of different industries, including the semiconductor industry, in the PRC and Hong Kong. Based on the work conducted by us, we are satisfied that the Valuer is suitably qualified and experienced with sufficient knowledge, skills and understanding necessary to prepare the Valuation Report competently. Furthermore, we also reviewed the Valuer's terms of engagement stated in the engagement letter entered into between the Company and the Valuer and noted that the scope of work was appropriate for the Valuer to form the opinion required to be given and there were no limitations on the scope of work which might adversely impact the degree of assurance given by the Valuer in the Valuation Report.

6.2 Valuation Methodologies

As set out in the Valuation Report and based on our discussions with the Valuer, both the asset-based approach and the market approach were considered in the valuation of the 100% equity interest in the Target Company as of 31 August 2025, and the market approach was adopted as the basis for the concluded appraised value.

We understand from the Valuer that three generally accepted approaches are available for valuing equity interests, namely, the asset-based approach, the income approach, and the market approach. After considering the applicability of each method, the Valuer concluded that the market approach is the most appropriate for this valuation, as (i) a sufficient number of comparable listed companies in the same industry can be identified in the capital market, and (ii) adequate and reliable operating and financial data of these comparable companies are publicly available to support meaningful comparison and adjustment.

The asset-based approach was also assessed to be applicable, as the Target Company's assets are either in the state of continued use or assumed to be in the state of continued use, and sufficient historical operating data are available. However, due to its inherent characteristics, this approach primarily measures the value of individual tangible and identifiable intangible assets, and does not fully capture the synergistic and integrated value generated by the combination and interaction of these assets. In particular, important intangible resources such as process technologies, management capabilities, technical expertise, and self-created goodwill are difficult to quantify under the asset-based approach, thereby limiting its ability to reflect the Target Company's overall enterprise value relative to the market approach.

The income approach, on the other hand, was considered inappropriate for this valuation. The wafer foundry industry is significantly affected by international relations and macroeconomic conditions, and is characterised by strong cyclicality and uncertainty. These factors make reliable forecasting of future profitability and cash flows difficult, rendering the income approach less suitable in this valuation.

As advised by the Valuer, the fair value of 100% equity interest in the Target Company was determined with reference to comparable listed companies (the "**Comparable Companies**") as comparable transaction analysis was not feasible due to a lack of recent similar transactions in the market. According to the Valuation Report, the Comparable Companies are listed on the Shanghai Stock Exchange, and were selected based on the following criteria:

1. Listing history – the Comparable Companies must have been listed for at least two years as of the valuation benchmark date to avoid potential distortions caused by insufficient market information, IPO effects, or market expectation – driven price volatility;

2. Industry and business model – the Comparable Companies must operate in the semiconductor manufacturing or wafer foundry industry, with a primary business model involving large-scale investment, high capital expenditure, and continuous technological process enhancement, namely under an IDM (Integrated Device Manufacturer) or foundry model, and their product application areas should be similar to those of the Target Company;

3. Trading status – the Comparable Companies must have been normally traded near the valuation benchmark date, without suspension or other abnormal trading conditions, and must not have experienced significant share price fluctuations arising from merger, acquisition, or restructuring activities around that period;

4. Exclusion of ST stocks – "ST" stocks, (stocks under delisting risk warning) are more likely to deviate significantly from their actual value due to speculative and manipulative factors in the market and are excluded; and

5. Scale comparability – to ensure a comparable operating scale, companies with gross book value of equipment-related fixed assets below RMB10 billion were excluded, given that the Target Company's corresponding asset value exceeds RMB15 billion.

Based on the above criteria, the Valuer was able to identify three Comparable Companies, which the Valuer confirmed was an exhaustive list. We also understand from the Valuer that the Comparable Companies are considered comparable to the Target Company notwithstanding differences in their listing status, as an appropriate discount for lack of liquidity has been taken into account in the Valuation. Based on our review of the Valuation Report and the discussion with the Valuer, we were given to understand that the liquidity discount rate was derived from a comparative analysis of newly listed companies in the relevant industries. This approach quantifies the lack of liquidity by comparing the price at which shares are sold in a private context (represented by the IPO price) to their price after achieving liquidity in the public market (represented by the post-listing trading price). The median liquidity discount rate of 39.26% was calculated based on the differences between the IPO and the closing prices on the 90th, 120th, and 250th trading days after their respective listings. This liquidity discount reflects the reduced marketability of the Target Company's shares.

We consider the above criteria to be reasonable for the following reasons:

(i) a sufficient listing history ensures that the trading and financial data of the Comparable Companies are reliable and less affected by IPO-related or short-term market volatility;

(ii) similar business models ensure that the Comparable Companies operate under broadly similar industry conditions and risk-return profiles;

(iii) the exclusion of companies with suspended or irregular trading avoids potential distortions in valuation multiples; and

(iv) comparable scale ensures that differences in market capitalisation and operating size do not materially bias the valuation outcome.

Although the number of Comparable Companies is limited to three, we note that such number satisfies the minimum requirement for the application of the market approach and that each selected company exhibits a high degree of relevance and similarity to the Target Company. We are of the view that the quality and comparability of the selected companies are the key factors underpinning the robustness of the valuation, and that including additional but less comparable companies could reduce the overall reliability of the valuation result. Taking into account the above and that a sufficient number of Comparable Companies satisfying the above criteria can be identified, we consider that the selected Comparable Companies provide objective and relevant benchmarks for assessing the fair value of 100% equity interest in the Target Company. Accordingly, we concur that the adoption of the market approach by the Valuer is appropriate and reasonable for this Valuation.

Under the market approach, the Valuer did not adopt asset-based ratios such as the price-to-book ratio because the Target Company's fixed assets were almost fully depreciated as of the Valuation Benchmark Date. This resulted in very low net and total asset values, making them not comparable to the Comparable Companies, which have significantly higher net asset ratios. Similarly, revenue-based ratios, including the price-to-sales ratio, were deemed inappropriate because they assume a direct correlation between a company's value and its revenue scale. In the wafer foundry industry, value is driven primarily by technology and profitability rather than revenue size.

Although earnings-based multiples generally better reflect the industry's value drivers, traditional profitability ratios such as the price-to-earnings ratio and enterprise value to EBIT were considered unsuitable. This is because wafer foundries involve substantial capital investment and long payback periods, often resulting in low or negative profits after depreciation and amortization. Instead, EV/EBITDA was adopted as the valuation multiple for this appraisal, as adding back depreciation and amortization provides a more accurate measure of the company's sustainable profitability. Using the adjusted value ratios of comparable companies, in combination with the relevant financial data or indicators of the appraised entity, the enterprise value of the appraised entity was calculated. After further adjustments for non-operating assets, liabilities, and surplus assets, the total equity value attributable to the shareholders of the appraised entity was finally determined.

We obtained and reviewed the calculations described above. The appraised enterprise value of the Target Company was determined by multiplying the Target Company's adjusted EBITDA as of 31 August 2025 by the average adjusted EV/EBITDA multiples of the Comparable Companies. We reviewed the data and information used by the Valuer in deriving the adjusted multiples, including making reference to market data available from Bloomberg and public disclosures, and discussed with the Valuer to understand the adjustments made and the rationale behind such adjustments. We also reviewed and discussed with the Valuer the key bases and assumptions adopted for the valuation. These assumptions are set out in the Valuation Report contained in Appendix V to the Circular. Based on our discussions, we noted that the assumptions are commonly adopted in business valuations. We did not identify any material factors that would lead us to question the reasonableness of the assumptions used in the Valuation Report.

Having taken into account the above, we concur with the Valuer that the market approach is commonly used and is the appropriate method for deriving the appraised value of 100% equity interest of the Target Company. On this basis and taking into account that the Total Consideration of the Proposed Acquisition of RMB8,267.9 million represents approximately 97.4988% to the appraised value of 100% equity interest of the Target Company of approximately RMB8,480.0 million, we consider the Total Consideration for the Proposed Acquisition is fair and reasonable.

We noted that the Total Consideration represents a significant premium over the net asset value of the Target Company as at 31 December 2024 and 30 June 2025. Having discussed with the Management and the Valuer and reviewed the Valuation Report, we understand that the Total Consideration was determined with reference to the appraised fair value of the Target Company assessed under the market approach, which reflects its earnings potential and market comparables rather than solely its book value.

We consider that the net asset value of the Target Company, which mainly represents the historical accounting value of its assets and liabilities, may not fully reflect its underlying fair value or earning capability, particularly for a business of an operating nature. This is especially relevant given the strong growth trends in AI and next-generation technologies, which are expected to drive significant future demand for the Target Company's products. The adoption of the market approach by the Valuer, which captures the market's assessment of value through the trading multiples of comparable listed companies, is therefore more appropriate than relying solely on book value for assessing the Target Company's fair value.

Taking into account the above factors, including the valuation approach adopted, the justification for the valuation premium relative to book value, and the strategic benefits expected to accrue to the Group, we consider that the consideration for the Proposed Acquisition, though representing a premium over the Target Company's NAV, is fair and reasonable so far as the Takeovers Code Independent Shareholders and the Proposed Acquisition LR Independent Shareholders are concerned.

According to the Acquisition Agreement and the Supplemental Agreement, the Total Consideration will be settled solely by the issuance of RMB shares. We consider that it is beneficial to the Company and its existing Shareholders as it preserves the Group's cash resources for strategic development needs. The semiconductor foundry industry is highly capital-intensive and requires substantial and continuous investment in R&D, advanced process development, and capacity expansion to maintain technological competitiveness. As advised by the Management, the Group continued the rapid capacity ramp-up and volume production of the Hua Hong Manufacturing Project, which commenced risk production at the end of 2024. Due to the smooth progress of the first phase, the Company anticipates initiating the second-phase capacity deployment ahead of schedule by the end of 2025. Retaining cash on hand enables the Group to support future capital expenditure, strengthen its technology roadmap, and respond to market opportunities without increasing financial leverage or constraining liquidity.

By adopting a non-cash settlement structure, the Group is able to complete the Proposed Acquisition without reducing its financial flexibility, while allowing the economic risks and benefits of the transaction to be shared with the Vendors through equity participation.

7. Assessment of the Issue Price of the Consideration Shares

In accordance with the relevant PRC laws and regulations, the issue price of the Consideration Shares shall be RMB43.34 per Consideration Share, representing not less than 80% of the average trading prices of the RMB Shares for the 120 trading days prior to the Pricing Benchmark Date. Notwithstanding the fact that the 120-day average price presented a lower average price, the 120 trading days was selected as the pricing determination basis in light of the price fluctuation of the RMB Shares prior to the signing of the Acquisition

Agreement, as a result, a longer reference period (i.e. 120 trading days, instead of the other reference period 20 trading days or 60 trading days), was chosen by the parties, as it neutralized the impact of the price rally prior to the signing of the Acquisition Agreement to achieve a fair and reasonable pricing basis.

The issue price of RMB43.34 per Consideration Shares represents:

(a) a discount of approximately 44.79% to the closing price per RMB Share of RMB78.50 as quoted on the Shanghai Stock Exchange on the date of the Acquisition Agreement;

(b) a discount of approximately 59.82% to the closing price per RMB Share of RMB107.87 as quoted on the Shanghai Stock Exchange on the date of the Supplemental Agreement;

(c) a discount of approximately 44.79% to the closing price per RMB Share of RMB78.50 as quoted on the Shanghai Stock Exchange on the last trading day prior to the Pricing Benchmark Date;

(d) a discount of approximately 31.78% to the average trading price per RMB Share of RMB63.53 based on the as quoted on the Shanghai Stock Exchange of the last 20 trading days immediately prior to the Pricing Benchmark Date;

(e) a discount of approximately 24.94% to the average trading price per RMB Share of RMB57.74 based on the as quoted on the Shanghai Stock Exchange of the last 60 trading days immediately prior to the Pricing Benchmark Date;

(f) a discount of approximately 19.99% to the average closing price per RMB Share of RMB54.17 based on the as quoted on the Shanghai Stock Exchange of the last 120 trading days immediately prior to the Pricing Benchmark Date;

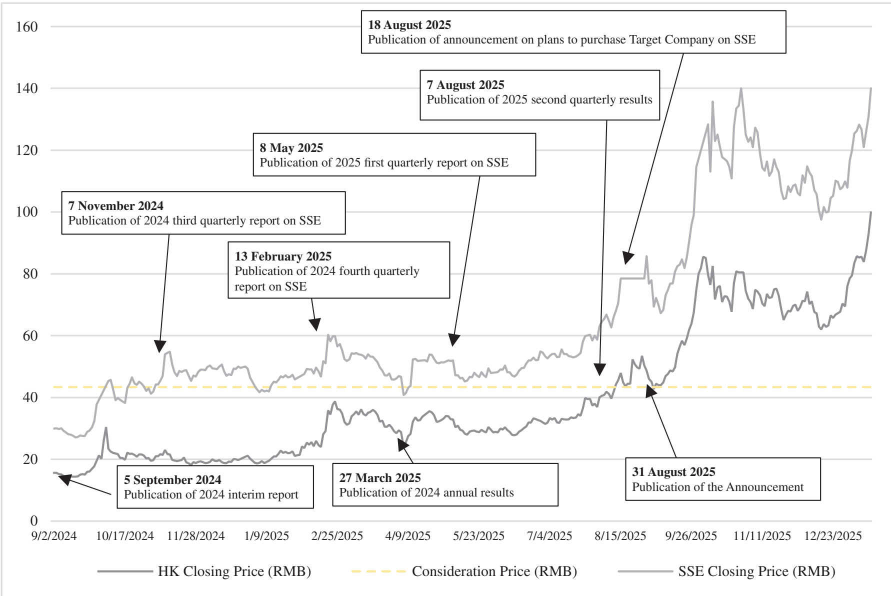
(g) a premium of approximately 65.85% over the audited net asset value attributable to the Shareholders of approximately US$3.64 per Share as at 31 December 2024, based on the exchange rate of US$1 to RMB7.1884 on 31 December 2024 as announced by People's Bank of China;

(h) a premium of approximately 65.97% over to the unaudited net asset value attributable to the Shareholders of approximately US$3.65 per Share as at 30 June 2025, based on the exchange rate of US$1 to RMB7.1586 on 30 June 2025 as announced by People's Bank of China; and

(i) a discount of approximately 67.92% to the closing price per RMB Share of RMB135.08 as quoted on the Shanghai Stock Exchange on the Latest Practicable Date.

7.1 Historical price performance of the Shares

The graph below illustrates the historical closing prices of the RMB Shares as quoted on the Shanghai Stock Exchange from 1 September 2024 and up to and including the Latest Practicable Date (the "**Review Period**"), which covers one year before the Pricing Benchmark Date to illustrate the general trend and level of movement of the closing prices of the RMB Shares. We consider the duration of the Review Period would be a reasonable and sufficient period to provide a general and fair overview of the recent trend of the closing price of the RMB Shares free from the influence of, if any, short term market volatility when assessing the issue price of the RMB Share:



Source: Website of the Stock Exchange, Bloomberg

During the Review Period, the lowest and highest closing prices of RMB Shares were RMB27.08 per RMB Shares recorded on 17 September 2024 and RMB140.00 recorded on 29 October 2025 and 16 January 2026, respectively. The issue price of RMB43.34 per RMB Share is within the RMB Shares' closing price range during the Review Period.

The RMB Share price of the Group was hovering around the RMB40-60 range for the majority of the period prior to the Announcement from early October 2024 to July 2025, reflecting a prolonged consolidation phase. The RMB Share price experienced a brief initial drop in early September 2024 to its lowest point below RMB30 for a short duration around the time at which the 2024 Interim Report was published on the Hong Kong Stock Exchange, likely due to the lingering effects from the 2023 industry downturn as reflected in the 2024 Interim Report published on 5 September 2024. The RMB Share price of the Group only began to surge shortly before the publication of the second quarterly results of 2025, breaking above the RMB40-60 range in early August 2025 and accelerating sharply through August and September and peaking in mid-October 2025. The rally was believed to be driven by a combination of factors including (i) improvement in financial performance as reflected in the second quarterly report of 2025; (ii) positive market sentiment regarding the strategic consolidation following the announcement of the Proposed Acquisition; and (iii) the broader positive uptrend in the semiconductor sector. Following a brief correction in October 2025, the RMB Share price resumed its upward trajectory and continued to rise and reached the peak again on the Latest Practicable Date.

Pursuant to the stipulations in the Administrative Measures for Material Asset Restructuring (the "**Administrative Measures**"), the price at which a listed company issues new shares shall not be lower than 80% of the market reference price. The market reference price is made reference to one of the average trading prices of the company's stocks on the 20 trading days, 60 trading days, or 120 trading days immediately before the announcement of the board of directors' resolution for the issuance of shares to the acquisition of assets, which can be the lowest among the above three average trading prices (the "**Basic Pricing Criteria**"). 80% of the average trading price of the RMB Shares of the Company of 20 trading days, 60 trading days, and 120 trading days prior to the Pricing Benchmark Date, which are RMB50.824, RMB46.192 and RMB43.336 per Consideration Share, respectively. We noted that the Issue Price of RMB43.34 per RMB Share is higher than 80% of the average trading price of the RMB Shares of the Company of 120 trading days prior to the Pricing Benchmark Date. The issue price of the Consideration Shares is therefore in compliance with the Administrative Measures.

The issue price was higher than the H-share closing price for the entirety of the Review Period and was in line with the closing prices around the time the announcement of the Proposed Acquisition was published on the SSE, notwithstanding a notable increase in the share price shortly prior to the Announcement. Given that the RMB Shares have consistently traded at a premium to the H shares during the Review Period, the issuance of RMB shares as consideration shares is expected to result in comparatively less dilution to the percentage interest of the existing public Shareholders than an issuance of H shares.

We also noted that since the Announcement, the market price of the Company's H shares and RMB Shares have both increased significantly, and as a result, the Issue Price and the Total Consideration now represent a deeper discount to the latest market price. While the Issue Price is below the recent market price, we attribute the appreciation in share price to the market's positive expectation of the strategic synergies and benefits the Target Company would bring to the Group, specifically regarding potential earnings growth and enhanced market positioning.

In our view, the Total Consideration, which was determined with reference to the fair value of the Target Company assessed under the market approach, remains fair and reasonable. The recent share price movement does not affect the underlying valuation of the Target Company, which was based on an objective assessment of its business, earnings potential, and market comparables, rather than short-term market fluctuations. Accordingly, we consider that the Total Consideration is fair and reasonable so far as the Takeovers Code Independent Shareholders and the Proposed Acquisition LR Independent Shareholders are concerned, taking into account both the Valuer's assessment and the market's positive reception of the Proposed Acquisition.

7.2 *Comparison with recent issuances of RMB Shares as consideration*

To further assess the fairness and reasonableness of the Issue Price in view of the aforementioned discounts, we also identified transactions in relation to the acquisition of over 50% equity interests in target companies involving the issuance of RMB Shares as consideration (the "**Comparable Issuances**"), that were announced by companies listed on the main board of Shanghai Stock Exchange or both Shanghai Stock Exchange and the Hong Kong Stock Exchange during the Review Period. We selected Comparable Issuances involving the acquisition of over 50% equity interests because such transactions signify the acquisition of control, making them more relevant to the Proposed Acquisition. We consider the Review Period is commonly adopted for analysis and reflects the recent market practice up to the date of the Latest Practicable Date. Based on the data sourced from Eastmoney.com (東方財富網), a leading and publicly-listed Chinese online financial information service provider, we identified 21 completed issuances which met the said criteria, which is an exhaustive list. Despite that the businesses, operations and prospects of the Group are not the same as the subject companies of the Comparable Issuances, the Comparable Issuances can demonstrate the market practices of issuance of RMB Shares as consideration shares by companies listed on the main board of the Shanghai Stock Exchange during the Review Period.

Company Name	Stock code	Principal business	Market capitalisation as at the Latest Practicable Date (RMB'billion)	Announcement date	Initial issue price not less than 80% of the 20-day/ 60-day/120-day average trading price of the RMB Shares immediately preceding the price benchmark date	Initial lock-up period	Connected Transaction (Y/N)	Non-pubic issuance (Y/N)
Ningbo Construction Co., Ltd. (寧波建工股份有限公司)	601789.SH	The provision of municipal and construction engineering, including landscaping, roads and bridges, building decoration and curtain walls, prefabricated buildings and steel structures, as well as related general contracting works. It also manufactures and installs building components, provides property management and construction equipment leasing services, and sells building materials.	7.88	January 2026	Y(Note)	36 months	Y	N

Company Name	Stock code	Principal business	Market capitalisation as at the Latest Practicable Date (RMB'billion)	Announcement date	Initial issue price not less than 80% of the 20-day/ 60-day/120-day average trading price of the RMB Shares immediately preceding the price benchmark date	Initial lock-up period	Connected Transaction (Y/N)	Non-pubic issuance (Y/N)
Inner Mongolia MengDian HuaNeng Thermal Power Corporation Limited(內蒙古蒙電華能熱電股份有限公司)	600863.SH	The production, supply and management of thermal, wind and solar energy, as well as the development, construction and operation of coal and coal chemical projects. It also invests in power-related raw materials, railway supporting infrastructure, and provides management and consulting services.	34.01	January 2026	Y, 60-day	60 months	Y	Y
National Silicon Industry Group Co., Ltd. (上海硅產業集團股份有限公司)	688126.SH	The manufacture and sale of semiconductor silicon wafers. It offers 300mm silicon wafers; SOI wafer; and customized silicon wafer.	75.09	December 2025	Y, 20-day	36 months	Y	Y
Huaihe Energy (Group) Co., Ltd (淮河能源(集團)股份有限公司)	600575.SH	The provision of thermal power generation, electricity sales, railway transportation, and coal blending	24.80	December 2025	Y, 120-day	18/36 months	Y	N
Shenzhen Original Advanced Compounds Co., Ltd. (深圳至正高分子材料股份有限公司)	603991.SH	The research and development, production, and sale of polymer materials in the China and internationally.	11.80	December 2025	Y, 120-day	12/36 months	Y	Y
Jiangsu HHCK Advanced Materials Co., Ltd. (江蘇華海誠科新材料股份有限公司)	688535.SH	The manufacture and sale of semiconductor packaging materials, such as epoxy molding compounds and electronic adhesives in China.	12.34	December 2025	Y, 60-day	12/36 months	N	Y

Company Name	Stock code	Principal business	Market capitalisation as at the Latest Practicable Date (RMB'billion)	Announcement date	Initial issue price not less than 80% of the 20-day/ 60-day/120-day average trading price of the RMB Shares immediately preceding the price benchmark date	Initial lock-up period	Connected Transaction (Y/N)	Non-pubic issuance (Y/N)
Spic Yuanda Environmental-Protection Co., Ltd. (國家電投集團遠達環保股份有限公司)	600292.SH	Provision of energy-saving and environmental protection services in China and internationally	60.27	November 2025	Y*(Note)*	36 months	Y	Y
ZhuZhou QianJin Pharmaceutical Co., Ltd (株洲千金藥業股份有限公司)	600479.SH	The research, development, production, and sales of traditional Chinese medicines, chemicals and API, and TCM derivatives in China.	5.12	October 2025	Y*(Note)*	12/36 months	Y	N
Yangtze Optical Electronic Co., Ltd. (武漢長盈通光電技術股份有限公司)	688143.SH	Provision of engineering design and consulting services in China and internationally.	7.24	October 2025	Y*(Note)*	12 months	N	N
IKD Co., Ltd. (愛柯迪股份有限公司)	600933.SH	Research, development, production, and sales of automotive aluminum alloy precision die castings parts in the United States, Europe, and Asia.	20.90	October 2025	Y*(Note)*	12 months	N	Y
United Nova Technology Co., Ltd. (芯聯集成電路製造股份有限公司)	688469.SH	Manufacture and market power discrete and modules in China and internationally.	59.10	September 2025	Y, 20-day	36 months	Y	N
Huadian Power International Corporation Limited (華電國際電力股份有限公司)	600027.SH	The construction and operation of power plants, including large-scale and fuel-fired power plants; and coal and gas-fired power generation units and renewable energy projects	57.94	August 2025	Y, 20-day	36 months	Y	Y

Company Name	Stock code	Principal business	Market capitalisation as at the Latest Practicable Date (RMB'billion)	Announcement date	Initial issue price not less than 80% of the 20-day/ 60-day/120-day average trading price of the RMB Shares immediately preceding the price benchmark date	Initial lock-up period	Connected Transaction (Y/N)	Non-pubic issuance (Y/N)
JDM JingDaMachine (Ningbo) Co.Ltd (寧波精達成形裝備股份有限公司)	603088.SH	Production and sale of precision stamping parts in China and internationally	5.73	June 2025	Y, 20-day	36 months	Y	Y
Guangdong Songfa Ceramics Co., Ltd. (廣東松發陶瓷股份有限公司)	603268	Production and sale of ceramic products in China and internationally	82.67	May 2025	Y, 60-day	36 months	Y	Y
Seres Group Co., Ltd (賽力斯集團股份有限公司)	601127.SH	The research and development, production, sales, and servicing of new energy vehicles and components in China and internationally	211.00	March 2025	Y, 120-day	12/36 months	N	N
Guolian Minsheng Securities Co., Ltd. (國聯民生證券股份有限公司)	601456.SH	Provision of various financial products and services in the People's Republic of China.	56.19	March 2025	Y*(Note)*	12/36 months	N	Y
Shanghai Sanyou Medical Co., Ltd (上海三友醫療器械股份有限公司)	688085.SH	Research, development, manufacture, and sales of orthopedics implants in China	6.69	February 2025	Y, 60-day	12/36 months	Y	Y
Haohua Chemical Science & Technology Corp., Ltd. (昊華化工科技集團股份有限公司)	600378.SH	Research and development, production, and sales of manufactures and sells fluorine materials, electronic gases, high-end manufacturing chemical materials, and carbon emission reduction products in China and internationally.	49.25	January 2025	Y*(Note)*	36 months	Y	Y

Company Name	Stock code	Principal business	Market capitalisation as at the Latest Practicable Date (RMB'billion)	Announcement date	Initial issue price not less than 80% of the 20-day/ 60-day/120-day average trading price of the RMB Shares immediately preceding the price benchmark date	Initial lock-up period	Connected Transaction (Y/N)	Non-pubic issuance (Y/N)
Chinese Universe Publishing and Media Group Co., Ltd. (中文天地出版傳媒集團股份有限公司)	600373.SH	The editing and publishing of books, newspapers, periodicals, audio-visual, and electronic publications in China and internationally	13.00	October 2024	Y, 120-day	36 months	Y	N
Rigol Technologies Co., Ltd. (普源精電科技股份有限公司)	688337.SH	The research, development, manufacturing, and sale of electronic testing and measuring instruments and accessories in China and internationally	7.70	October 2024	Y, 60-day	36 months	N	N
CCCC Design & Consulting Group Co., Ltd. (中交設計諮詢集團股份有限公司)	600720.SH	provision of engineering design and consulting services in China and internationally.	16.93	October 2024	Y*(Note)*	36 months	Y	Y

Note: The issue price is not less than 80% of the average trading price of the shares over the 20, 60 and 120 trading days prior to the pricing benchmark date and is sufficiently higher than the Basic Pricing Criteria.

Based on our review, we noted that the basis for determining the initial issue price for all the Comparable Issuance complied with the Basic Pricing Criteria as under the Administrative Measures. We also noted that nine out of the 21 Comparable Issuance adopted a longer reference period of up to 60-day or 120-day average trading prices of RMB Shares when determining their issue prices.

The Consideration Price is determined as 80% of the Average Trading Price of the RMB Shares for the 120 trading days prior to the Pricing Benchmark Date, which is the longest reference period permitted under the relevant PRC regulations. While only four out of 21 Comparable Issuance referenced the 120-day average trading prices of RMB Shares, it is not uncommon and we also noted that the share price of the Group only surged shortly before the publication of the Announcement of the Proposed Acquisition, the shorter reference periods of 20-day and 60-day would be inflated by such sudden price surge just before the Announcement while the 120-day average would be a more prudent and representative price mechanism that smooths out short-term price fluctuations and provide a more stable and reliable anchor reflective of the stock's fundamental value over a longer period. Further, the use of the longer reference period is legally permissible. In evaluating the five Comparable Issuances that reference the 120-day average trading prices, we observed three connected issuances and two independent issuances, indicating that the distinction between connected and independent issuances does not significantly impact the issuance of RMB shares.

To further enhance our assessment of the Total Consideration, we identified a set of comparable companies operating in similar segments of the semiconductor industry (the "**Market Comparables**"). The Market Comparables were selected with reference to the following criteria: (i) listed on a recognized stock exchange in Hong Kong, the PRC, or the United States; (ii) principally engaged in semiconductor manufacturing or wafer foundry operations, adopting a business model characterised by large-scale investment, high capital expenditure, and continuous technological process enhancement, namely under an IDM (Integrated Device Manufacturer) or pure-play foundry model; (iii) generating over 50% of total revenue from wafer manufacturing; and (iv) having revenue exceeding USD 1 billion for the year ended 31 December 2024 to ensure comparability in terms of scale. Based on these criteria, we identified eight companies as the Market Comparables, which we consider a comprehensive and relevant set for benchmarking purposes.

For each Market Comparables, the valuation ratios were calculated based on: (i) financial information extracted from the latest published annual reports; and (ii) the respective market capitalisation as at the Pricing Benchmark Date, as this date aligns with the time at which the Issue Price, and consequently the implied market capitalization, was determined. We consider the Market Comparables to represent an exhaustive list of suitable peer companies based on the above criteria.

In comparing the Proposed Acquisition against the Market Comparables, we adopted the EV/EBITDA ratio, recognising that wafer foundry businesses involve substantial capital investment and long asset payback periods, which often lead to low or negative profitability after depreciation and amortisation. The P/E ratio is not considered meaningful given that the

Group recorded a net loss for the year ended 31 December 2024. The P/S ratio was also deemed unsuitable due to significant wafer-pricing pressure attributable to intensified market competition and weaker demand conditions, as discussed in the financial performance section above.

The results of the EV/EBITDA ratios of the Market Comparables compared to those implied by the Proposed Acquisition are summarised in the table below:

Company name	Stock code	Stock Exchange	Principal business	Market Capitalisation as at the Pricing Benchmark Date (USD'million)(Note 1)	Revenue (USD' million)	EV/EBITDA (Note 2)
Semiconductor Manufacturing International Corporation ("SMIC")	00981/ 688981	Hong Kong/Shanghai	SMIC Group provides semiconductor foundry and technology services to global customers on 8-inch and 12-inch wafers.	613,499.0 (Hong Kong)/ 561,259.0 (Shanghai)	8,029.9	23.42
China Resources Microelectronics Limited ("CRM")	688396	Shanghai, China	CRM engages in the manufacture and sale of semiconductors in China and internationally.	69,562.5	1,419.0	32.08
Nexchip Semiconductor Corporation ("Nexchip")	688249	Shanghai, China	Nexchip engages in the research and development, production, and sales of integrated circuit related products and supporting products in China and internationally.	6,830.8	1,297.1	17.04

Company name	Stock code	Stock Exchange	Principal business	Market Capitalisation as at the Pricing Benchmark Date (USD'million)[(Note 1)]	Revenue (USD' million)	EV/EBITDA [(Note 2)]
Power Semiconductor Manufacturing Corporation ("PSMC")	6770	Taiwan	PSMC provides chip design and manufacturing services. It provides foundry, design, overhaul, manufacturing, and memory wafer testing services.	2,176.8	1,462.1	67.57
Vanguard International Semiconductor Corporation ("VSIC")	5347	Taiwan	VISC engages in manufacturing, selling, packaging, testing, and computer-aided design of integrated circuits and other semiconductor devices in Taiwan and internationally.	5,585.6	1,440.2	9.04
Global Foundries Inc. ("GFS")	GFS	Nasdaq, United States	GFS is a semiconductor foundry, providing range of mainstream wafer fabrication services and technologies worldwide.	18,528.6	6,750.0	7.56
United Microelectronics Corporation ("UMC")	UMC	New York Stock exchange, United States	UMC operates as a semiconductor wafer foundry internationally. It manufactures and sells integrated circuits.	508,531.3	7,594.0	4.86

Company name	Stock code	Stock Exchange	Principal business	Market Capitalisation as at the Pricing Benchmark Date (USD'million)(Note 1)	Revenue (USD' million)	EV/EBITDA (Note 2)
Tower Semiconductor Ltd. ("TSEM")	TSEM	Nasdaq, United States	TSEM is a semiconductor foundry which provides technology development, and process platforms for integrated circuits internationally.	6,578.8	1,436.1	14.15
Maximum						67.57
Minimum						4.86
Median						15.60
Average						21.97
The Company (as implied by the Issue Price)(Note 3)						21.16

Notes:

1. The market capitalization of the Market Comparables as at the Pricing Benchmark Date are extracted from Bloomberg.

2. The EV is calculated as the market capitalization as at the Pricing Benchmark Date plus net debt (short-term and long-term debt minus cash and cash equivalents) and non-controlling interests of a company based on the latest published annual financial statements. The EBITDA of the Market Comparables are extracted from Bloomberg based on the latest published annual financial information.

3. The Enterprise Value (EV) of the Company is implied by multiplying the Issue Price of RMB43.34 per Share by the total number of shares outstanding as of the Pricing Benchmark Date to calculate the market capitalization. To this market capitalization, the Company's net debt (calculated as short-term and long-term debt, less cash and cash equivalents), and non-controlling interests as of 31 December 2024 are added. The Company's EBITDA is calculated based on the profit before tax for the year ended 31 December 2024, adjusted by adding back depreciation, amortization, and finance costs.

As set out in the table above, EV/EBITDA of the Company (as implied by the Issue Price) fall within the range of those of the Market Comparables. The Proposed Acquisition, in terms of the EV multiple, is higher than the median and approximated the average, indicating that the Issue Price was not unduly low compared to the Market Comparables, confirming the stock of the Group is not undervalued at the time the Issue Price was determined that lead to excessive dilution for the existing shareholders as a result of the Proposed Acquisition.

Our conclusion

Based on our comprehensive assessment of the Target Company's Valuation, the determination of the RMB-Share Issue Price, and the resulting impact on the Group's existing shareholders, we conclude that the Total Consideration and the Issue Price for the Proposed Acquisition are fair and reasonable.

1. Fairness of the Target Valuation

The Total Consideration is deemed fair as it is firmly supported by an independent, professional Valuation Report. The Valuer is suitably qualified and experienced, and the final valuation derived through market-accepted methodologies, specifically the market approach, is robust. This consideration represents a significant premium over the net asset value of the Target Company as at both 31 December 2024 and 30 June 2025, confirming that the Group is acquiring the Target at a justifiable enterprise value. The strategic value is further warranted by the anticipated strategic benefits, synergies, and potential earnings growth the acquisition is expected to deliver to the Group.

2. Justification of the Issue Price

The selection of the 120-day average price as reference for the RMB Share issuance, while less common than the shorter periods, is justified as a prudent and necessary measure. This price fully complies with all relevant PRC regulations. The decision to use the longer horizon provides a stable, non-volatile benchmark, which is essential given that the Group's share price was in a prolonged consolidation phase (RMB40-60 range) but began to surge only shortly before the Announcement. Using the 120-day average mitigates the pricing distortion that would have been caused by relying on a short-term price spike that likely reflected market speculation regarding the Proposed Acquisition. The Issue Price also represents a premium of 65.85% and 65.97% over the net asset value per share as at 31 December 2024 and 30 June 2025, respectively.

3. Mitigation of Dilution Risk

To address the potential for increased dilution resulting from the lower 120-day price, we performed a critical check on the Group's valuation metrics. Our financial analysis confirms that the Group's implied EV/EBITDA, calculated using the Issue Price, are within the acceptable range of the Market Comparables, and indeed exceed the median and approximated the average. This demonstrates that the Issue Price is not unduly low and does not result in excessive dilution. Furthermore, the continued trading of the Group's shares above the Issue Price since the Announcement provides market validation that the price is not perceived as low, thereby confirming that the potential dilution is justified by the compelling strategic and financial benefits anticipated from the Proposed Acquisition.

8. The Whitewash Waiver

8.1 Background

As at the Latest Practicable Date, Huahong Group holds directly and indirectly 348,804,167 Shares (comprising 1,198,517 RMB Shares and 347,605,650 Hong Kong Shares), representing approximately 20.07% of the total issued share capital of the Company. In addition, as at the date of the Latest Practicable Date, the Huahong Concert Group holds directly and indirectly 602,956,550 Shares (comprising 66,389,753 RMB Shares and 536,566,797 Hong Kong Shares), representing approximately 34.70% of the total issued share capital of the Company.

If the Proposed Acquisition materializes, it is expected that immediately after completion of the issuance of the Consideration Shares, the voting rights held by Huahong Concert Group in the Company will increase to approximately 41.16% (assuming (i) there will not be any further adjustment to the issue price of the Consideration Shares, (ii) there will not be any change in the total issued share capital of the Company since the Latest Practicable Date up to and including the date of issuance of the Consideration Shares and (iii) the Proposed Non-public Issuance of RMB Shares has not been completed). Accordingly, upon Completion, pursuant to Rule 26.1 of the Takeovers Code, Huahong Concert Group will be required to make a mandatory general offer for all the securities of the Company not already owned or agreed to be acquired by the Huahong Concert Group, unless the Whitewash Waiver from strict compliance with Rule 26.1 of the Takeovers Code is obtained from the Executive.

8.2 The Whitewash Waiver as a condition to the Proposed Acquisition

Shareholders and potential investors should note that the completion of the Proposed Acquisition is conditional upon, among other things, the Whitewash Waiver being granted by the Executive and approved by the Takeovers Code Independent Shareholders. An application has been made by Huahong Group (on behalf of itself and Huahong Concert Group) to the Executive for the granting of the Whitewash Waiver pursuant to Note 1 on dispensations from Rule 26 of the Takeovers Code. The Whitewash Waiver, if granted by the Executive, will be subject to (i) the approval of the Whitewash Waiver by at least 75% of the votes cast by Takeovers Code Independent Shareholders either in person or by proxy at the EGM; and (ii) the approval of the Proposed Acquisition by more than 50% of the votes cast by Takeovers Code Independent Shareholders either in person or by proxy at the EGM as required under the Takeovers Code. The Proposed Acquisition will not proceed if the Whitewash Waiver is not obtained or if the Whitewash Waiver is not approved by the Takeovers Code Independent Shareholders.

Having considered (i) the benefits of the Proposed Acquisition as set out in the section headed "Reasons for and benefits of the Proposed Acquisition"; (ii) the fairness and reasonableness of the terms of the Acquisition Agreement (as supplemented by the Supplemental Agreement); and (iii) the obtaining of the Whitewash Waiver being an essential element of the Proposed Acquisition, we are of the view that the approval of the Whitewash Waiver is considered fair and reasonable and in the interests of the Company and the Takeovers Code Independent Shareholders as a whole as far as the Takeovers Code Independent Shareholders are concerned.

9. Financial effects of the Proposed Acquisition on the Group

Following the Completion, the Target Company will become a wholly-owned subsidiary of the Company. As such, the operating results and the financial position of the Target Company will be consolidated into the financial statements of the Group. The unaudited pro forma financial information of the Enlarged Group is set out in Appendix III to the Circular. The financial effects of the Proposed Acquisition on the Group's earnings, cashflow and net asset value and gearing are set out below. However, it should be noted that the analysis below is for illustrative purpose only and does not purport to represent how the financial performance and the financial position of the Group will be upon Completion.

9.1 Earnings

As discussed in the section headed "Background information of the Group – *Historical financial performance and financial position of the Group",* the Group recorded net losses for the six months ended 30 June 2025 and the year ended 31 December 2024. Meanwhile, as discussed in the section headed "Information on the Target Company – Financial Performance and Position of the Target Company", the Target Company recorded net profits for the eight months ended 31 August 2025 and the year ended 31 December 2024.

As discussed in the section headed "Reasons for and benefits of the Proposed Acquisition" of this letter above, among others, the Proposed Acquisition allows the Group to further strengthen its market position in the semiconductor industry and enhance the Group's overall competitiveness. Also, through synergetic integration, the Group is expected to lower the operating costs and benefit the financial performance of the Group. Considering the above, the Proposed Acquisition is expected to have a positive effect on the future growth of the Group's earnings and profitability.

9.2 Net asset value

According to the unaudited pro forma financial information of the Enlarged Group set out in Appendix III to the Circular, the unaudited pro forma net assets of the Enlarged Group attributable to owners of the parent would have increased to approximately USD9.0 billion. The asset enhancement is considered to be in the interests of the Company and the Takeovers Code Independent Shareholders and the Proposed Acquisition LR Independent Shareholders as a whole.

9.3 Liquidity, gearing and working capital

The Proposed Acquisition is structured as a share-based consideration, with the Total Consideration settled exclusively through the issuance of Consideration Shares. As a result, the Proposed Acquisition will have no direct impact on the Group's liquidity position, gearing ratio, or working capital requirements.

As at 30 June 2025, the Group's current ratio, calculated as current assets over current liabilities, was approximately 3.8 times. Based on the unaudited pro forma financial information of the Enlarged Group set out in Appendix III to the Circular, the current ratio of the Enlarged Group would remain at a healthy level of approximately 3.6 times upon Completion.

The net gearing ratio, calculated on the basis of interest-bearing borrowings less cash, bank balances and pledged deposits as a percentage of equity, was approximately –18.1%, reflecting a strong net cash position. According to the unaudited pro forma financial information of the Enlarged Group, the net gearing ratio would remain negative at approximately –16.7% after completion of the Acquisition, indicating that the Enlarged Group will continue to be in a net cash position notwithstanding a slight decrease. Therefore, the Enlarged Group is expected to retain a solid liquidity buffer and low financial leverage, and the level of negative net gearing continues to demonstrate prudent capital structure and ample financial flexibility.

As set out in the section headed "3. Working Capital" of Appendix I to the Circular, the Directors are of the opinion that, after taking into account the effect of the Acquisition Agreement and the Supplemental Agreement and the transactions contemplated thereunder, its internal resources, the financial resources available to the Group, including its existing cash and cash equivalents on hand, its cash flow from operating activities, the working capital available to the Group is sufficient for the Group's requirements for at least 12 months from the date of this letter.

10. The Special Deal in relation to the non-public Issuance of RMB Shares

10.1 Rationale of the Non-public Issuance of RMB Shares

According to the Letter from the Board, the proceeds to be raised from the Proposed Non-public Issuance of RMB Shares are proposed to be used for, amongst others, replenishing the working capital of the Group and the repayment of debt, financing technology update and renovation of the Target, and funding the research and development and the industrialization of the Target's specialized process, which would improve the overall financial position and facilitate the future development of the Group.

The Proposed Non-public Issuance of RMB Shares is subject to the approval of the Shanghai Stock Exchange and registration by CSRC and Completion, but the Proposed Acquisition is not conditional on completion of the Proposed Non-public Issuance of RMB Shares.

Following further discussions with the Management and our review of the Company's 2025 Interim Report, 2024 Annual Report and 2023 Annual Report, we have summarised below the key reasons for and benefits of the Proposed Non-public Issuance of RMB Shares:

(i) Easing of cash flow pressure and support in working capital requirements

We noted from the 2025 Interim Report, 2024 Annual Report and 2023 Annual Report, and as shown in the financials above, net cash generated from operating activities for all the three years ended 31 December 2024 and the first half of 2025 has been consistently and grossly inadequate to cover the sizable investing cash outflows, which are dominated by the purchases of items of property, plant and equipment and intangible assets for capacity expansion, facility upgrades and upgrade of specialized process technologies. The deficit necessitates continuous reliance on external funding. When external financing activities decrease (as seen in the year ended 31 December 2024 and the first half of 2025), the underlying liquidity pressure becomes immediately apparent, resulting in overall net decrease in cash and cash equivalent during these periods.

In addition, the Proposed Acquisition will increase the Enlarged Group's gearing ratio, thereby heightening the importance of strengthening its capital structure. The enlarged business may also require a higher level of working capital to support its expanded scale of operations, including greater inventory requirements, higher receivables and a longer operational cash cycle. As such, bolstering the Group's cash reserves is critical to ensuring that it can fund the operational needs of the enlarged business and maintain a sufficient liquidity buffer.

Considering the foregoing, we concur with the Management that, there is an on-going financing need to maintain sufficient liquidity cushion to support its enlarged business, repay its interesting bearing debts and supplement its working capital.

(ii) Other fundraising methods available to the Company

As advised by the Company, apart from the Proposed Non-public Issuance of RMB Shares, the Company also considered other fundraising alternatives, including debt financing from banks or money lenders and other forms of equity financing, with a view to obtaining sufficient funds to meet its interest-bearing obligations, supplement working capital and finance the Target's projects. Management explained that the Proposed Non-public Issuance was selected primarily because it offers greater flexibility and efficiency, allowing the Company to obtain approval for the fundraising and the intended use of proceeds through a streamlined regulatory process. Management also noted that the Group has largely exhausted its available external financing channels, which are typically restricted to project-specific uses and cannot be applied towards replenishing general working capital.

In respect of bank or money-lender financing, the Company noted that such borrowings would incur additional interest expenses and further increase the Group's leverage, which would be contrary to its objective of improving the capital structure through this fundraising exercise. Based on the unaudited pro forma financial information of the Enlarged Group, the gearing ratio is expected to rise from 25.6% as at 30 June 2025 to 30.6% upon Completion. Any additional external debt financing would therefore further deteriorate the Group's gearing and liquidity positions. In addition, debt financing would likely be subject to lengthy due diligence and internal risk assessments by banks or money lenders. In light of these considerations, the Company does not regard debt financing as a preferable option.

Regarding the issuance of RMB Shares under public channels, the Company has considered the regulatory requirements under the Regulatory Requirements for Guiding and Regulating the Financing Activities of Listed Companies (Revised Edition) (《關於引導規範上市公司融資行為的監管要求(修訂版)》) issued by the CSRC on 14 February 2020. Under this regime, where a listed company raises funds through channels other than non-public issuance, placement, issuance of preferred shares, or issuance to designated persons approved by the board, the amount applied towards working capital replenishment and debt repayment must not exceed 30% of the total proceeds. Given that the Company intends to allocate 48.97% the fundraising proceeds towards replenishing the working capital of the Group, debt repayment, payment of fees of intermediaries in connection with the Proposed Acquisition through public issuance of RMB shares would not be suitable for the Group.

Having considered the above, we concur with the Management that the Proposed Non-public Issuance of RMB Shares represents the most financially viable and optimal fundraising method for the Group to raise supporting funds for the Group post-Acquisition.

10.2 Principal terms of the Proposed Non-public Issuance of RMB Shares

The details of the Proposed Non-public Issuance of RMB Shares are set out below:

10.2.1 Target subscribers

The Proposed Non-public Issuance of RMB Shares will be carried out by way of non-public issue of RMB Shares to not more than 35 specific target subscribers, excluding (i) Huahong Group, SAIL and China IC Fund II which have indicated that they will not participate in the Proposed Non-public Issuance of RMB Shares and (ii) certain other Shareholders such as controlling shareholders and its related parties pursuant to the requirement of the Shanghai Listing Rules (both terms as defined thereunder). Such specific target subscribers may include, but not limited to, institutional investors such as securities investment fund management company, securities firm, financial services company, asset management company, insurance company, and other legal person or natural person investors in the PRC that comply with the regulations of the CSRC and the Shanghai Stock Exchange.

As at the Latest Practicable Date, the Company has not entered into any agreement with any potential subscribers in respect of the Proposed Non-public Issuance of RMB Shares, nor has the Company received any persons' indication to participate in the Proposed Non-public Issuance of RMB Shares. In addition, the identity of the target subscribers cannot be pre-determined as at the Latest Practicable Date and will only be determined after (i) obtaining the approval in respect of the Proposed Non-public Issuance of RMB Shares from the Shareholders at the EGM, the Shanghai Stock Exchange and the CSRC, and (ii) the commencement of the Offering Period of the Proposed Non-public Issuance of RMB Shares in accordance with the relevant PRC laws and regulations. The Company shall make further announcement on the identity of the subscribers if they become substantial shareholders of the Company upon the completion of the Proposed Non-public Issuance of RMB Shares.

10.2.2 Number of RMB Shares to be issued

Having considered the Company's future funding needs, the total amount of supporting funds to be raised under the Proposed Non-public Issuance of RMB Shares shall be RMB7,556,286,000, being (i) not exceeding 100% of the final Total Consideration for the Proposed Acquisition, and (ii) the number of RMB Shares to be issued shall not exceed 30% of the total issued share capital of the Company upon Completion, both thresholds following that of applicable PRC rules and regulations (i.e. Administrative Measures for Major Asset Restructuring of Listed Companies (《上市公司重大資產 重組管理辦法》) and The Measures for the Administration of Registration of Securities Offering by Listed Companies (《上市公司證 券發行註冊管理辦法》)) governing the issuance.

The number of RMB Shares to be issued shall be calculated by dividing the total amount of supporting funds to be raised, by the issue price to be determined according to the paragraph headed "Price Determination Date, pricing principles and issue price" (rounded down to the nearest share), as adjusted in the event of any ex-right or ex-dividend event in accordance with applicable PRC laws and regulations.

10.2.3 Price determination date, pricing principles and issue price

The issue price shall not be lower than 80% of the Average Trading Price of the RMB Shares for the 20 trading days prior to the Price Determination Date and no less than RMB52 (i.e. the price of the Company's its initial public offering of RMB Shares) pursuant to CSRC Measures to Balance Primary and Secondary Markets and Optimize IPO/Refinancing Regulation (《統籌一二級市場平衡優化IPO、再融資監管安排》).

The Offering Period, the Price Determination Date and the specific time of Issuance of the Proposed Non-public Issuance of RMB Shares shall be determined by the Company and the PRC independent financial adviser (the lead underwriter) having due regards to the market conditions and the proposal for use of proceeds, and shall be subject to approval by the Shanghai Stock Exchange and the CSRC.

The Offering Period shall commence after the Completion of the Proposed Acquisition. The Price Determination Date shall be the first day of the Offering Period of the Issuance of the Proposed Non-public Issuance of RMB Shares, and shall be a date falling within 12 months of the CSRC registration. The final issue price will be determined by the Board and the authorized persons of the Board and the lead underwriter according to the bookbuilding results in accordance with the authorization of the general meeting of shareholders, the provisions of relevant laws and regulations (i.e. The Measures for the Administration of Registration of Securities Offering by Listed Companies (《上市公司證券發行註冊管理辦法》)) and the requirements of regulatory authorities (including the CSRC and the Shanghai Stock Exchange).

All the target subscribers will subscribe for the RMB Shares under the Proposed Non-public Issuance of RMB Shares at the same issue price in cash.

According to the annual results announcement of the Company for the year ended 31 December 2024 published on the Shanghai Stock Exchange, the audited net asset per Share attributable to the Shareholders of the Company prepared in accordance with China Accounting Standards for Business Enterprises as at 31 December 2024 was approximately RMB25.37.

The final issue price, i.e. Non-Public Issuance Benchmark Price, will be determined by negotiations between the Board and its authorized person(s) with the authorization by the Shareholders at the EGM and the PRC independent financial adviser (the lead underwriter) based on the price inquiry results in accordance with the relevant PRC laws and regulations (e.g. Detailed Rules for the Implementation of the Offering and Underwriting Business for Securities of Listed Companies on the Shanghai Stock Exchange (《上海證券交易所上市公司證券發行與承銷業務實施細則 (2025年修訂）》) and The Measures for the Administration of Registration of Securities Offering by Listed Companies (《上市公司證券發行註冊管理辦法》)), which, amongst others, laid out requirements on the Company and the lead underwriter, having considered the valid applications and their quotation, to determine the issue price and the target investors reasonably based on principle of price priority (and other principles as decided by the Board, if any). The principles determined by the Board shall be fair, impartial and in line with the interest of the Company and its shareholders in its entirety. The lead underwriter's report on the issuance process and the compliance of subscription targets shall include a detailed disclosure of the entire issuance process, list the subscription quotations of eligible specific investors and the allocation results, and express an opinion on whether the issuance outcome is fair and impartial and whether it complies with the relevant regulations governing the issuance of shares to specific investors. Where specific investors who submitted quotations above the issue price did not receive allocations or had their allocation quantities reduced, the lead underwriter shall provide those investors with a full explanation of the reasons and disclose the circumstances in the report.

The Non-public Issuance Benchmark Price will be adjusted if there occurs any ex-right or ex-dividend event (such as distribution of cash dividend, bonus issue, rights issues, allotment of shares, conversion of share premium into share capital or capitalization issues) between the Price Determination Date and the date of issuance of the Proposed Non-public Issuance of RMB Shares in accordance with the applicable PRC laws and regulations.

10.2.4 Conditions precedents of the Proposed Non-public Issuance of RMB Shares

The Proposed Non-public Issuance of RMB Shares is conditional upon:

(i) Completion;

(ii) the approval of the Proposed Non-public Issuance of RMB Shares by the Board and the Non-public Issuance Independent Shareholders at the EGM;

(iii) the consent to the Special Deal from the Executive and the approval of the Special Deal by the Takeovers Code Independent Shareholders;

(iv) the approval of the Proposed Acquisition and the Proposed Non-public Issuance of RMB Shares by the competent state-owned assets supervision and administrative authorities or its authorized entities;

(v) the approval of the Proposed Acquisition and the Proposed Non-public Issuance of RMB Shares by the Shanghai Stock Exchange and the registration of the Proposed Acquisition and the Proposed Non-public Issuance of RMB Shares by the CSRC; and

(vi) the obtaining of any other necessary approval and/or filings in respect of the Proposed Non-public Issuance of RMB Shares from any applicable regulatory authorities.

None of the conditions above may be waived by any party to the Proposed Non-public Issuance of RMB Shares and therefore, if any of the conditions above is not satisfied (save as to the extent where condition (iii) above is no longer applicable), the Company will not proceed with the Proposed Non-public Issuance of RMB Shares.

Other than the condition precedent set out in paragraph (ii) (in respect of approval by the Board only) above, none of the conditions precedent has been fulfilled as at the Latest Practicable Date.

In respect of the condition set out in paragraph (v) above, as at the Latest Practicable Date, the Company is not aware of any other approval and/or filings which are required to be obtained by it in respect of the Proposed Non-public Issuance of RMB Shares.

10.2.5 Lock-up period

All target subscribers shall not transfer the RMB Shares subscribed under the Proposed Non-public Issuance of RMB Shares within six months from the date of completion of the Proposed Non-public Issuance of RMB Shares, provided that if any applicable regulatory authorities of the PRC require a lock-up period of different length to be imposed, the lock-up period shall be the one as required by such regulatory authorities.

The lock-up undertaking shall also be applicable to any additional RMB Shares received by the target subscribers in respect of the relevant RMB Shares subscribed under the Proposed Non-public Issuance of RMB Shares as a result of bonus issues, conversion of share premium into share capital, capitalization issues and/or rights issue of the Company after completion of the Proposed Non-public Issuance of RMB Shares.

10.3 Use of proceeds

The net proceeds from the Proposed Non-public Issuance of RMB Shares (after deducting all applicable costs and expenses incurred in connection with the Proposed Non-public Issuance of RMB Shares) are intended to be used in the subsequent five years after the completion of the Proposed Non-public Issuance of RMB Shares to (i) finance the Target's technology upgrades and renovations, and (ii) research and development and industrialization of the Target's specialized process and (iii) replenish the working capital of the Group, the repayment of debt, payment of fees of intermediaries in connection with the Proposed Acquisition in the following manner:

Use of proceeds	**Intended allocation of proceeds**	**Intended percentage of proceeds from the Proposed Non-public Issuance of RMB Shares allocated for such purposes** *(%)*
Upgrade and renovation of the Target Company's technology	3,294,760,000	43.60
Research and development (R&D) and industrialization of the Target Company's specialized process	561,526,000	7.43
Replenish (i) the working capital of the Group, (ii) the repayment of debt, (iii) payment of fees of intermediaries (including PRC independent financial advisers, underwriting fees, legal fees for PRC and overseas counsel, accounting fees for accountants, and other intermediary expenses) in connection with the Proposed Acquisition	3,700,000,000	48.97
Total	**7,556,286,000**	**100%**

More specifically on the above, the Target Company is primarily engaged in 12-inch wafer foundry operations. Approximately 51.03% of net proceeds will be allocated to two aspects:

(1) **Upgrading and renovating the Target Company's technology:** Having assessed market landscape, it is considered that the Target Company has pressing need to comprehensively upgrade the technological specifications of its 12-inch production line by way of replacing and updating the equipment. This will foster the Target Company's adaptation to the market's demand of various specialty processes, thereby optimizing the existing factory production lines, expanding production capacity and further enhancing the Company's core competitiveness amid market fluctuations. The net proceeds will also be used for maintenance costs of the production line. This limb takes up a larger trunk of the net proceeds since the new equipment with advanced technological specifications and an overhaul and renovation of the entire production line are inherently capital-intensive, based on the Company's and the Target Company's preliminary assessment. Before commencement of the renovation work, the Company and the Target Company shall conduct a comprehensive study of the technological specifications which best suit its future needs and conduct a robust selection of suppliers through its standard procurement procedure.

(2) **Research and development (R&D) and industrialization of the Target Company's specialized process:** The diversity of specialized process platforms is an important factor in assessing the overall strength of a semiconductor wafer foundry. The Target Company urgently needs to enhance the depth and breadth of its process platform products through developing new products. The proceeds will serve as an important source of funds for the R&D expenses of the Target Company in the upcoming years. This project entails an investment in R&D which seeks to explore new markets, and is different from the first limb which focuses on enhancing hardware, equipment and production capacity. The allocation between the two limbs has been determined having balanced the need for capital and cost-efficiency of each project.

Further, in view of the capital expenditure requirements in the upcoming three years arising from (i) the Company's future business development plans such as the expansion and developments of the 8-inch and 12-inch foundry fabs of HHGrace, Hua Hong Wuxi and Hua Hong Manufacturing, including but not limited to upgrading of equipment and building of new factory and (ii) the Company's budget for dedicated long-term strategic purpose, the Company is expected to incur a substantial amount of expenses. As a result, the existing cash and bank balance of the Group has already been budgeted for the development of the Group as aforementioned, and the Company shall require proceeds from the Proposed Non-public Issuance of RMB Shares to replenish its working capital to reserve cash for its business operations and development plans in the future (and the development of the Target Company which has not been previously budgeted by the Group) and maintain liquidity for the sustainable operations of the Group. Moreover, the net proceeds shall be used to (x) settle liabilities as they fall due as appropriate and (y) pay the fees of intermediaries (including PRC independent financial advisers, underwriting fees, legal fees for PRC and overseas counsel, accounting fees for accountants, and other intermediary expenses) in connection with the Proposed Acquisition. As the Proposed Acquisition and the Proposed Non-public Issuance of RMB Shares are still in progress, the professional fees of the intermediaries could not be fully determined as at the Latest Practicable Date and could only be confirmed once the Proposed Non-public Issuance of RMB Shares has been completed.

If the Proposed Non-public Issuance of RMB Shares does not proceed or the actual proceeds to be raised from the Proposed Non-public Issuance of RMB Shares are less than the proposed use of proceeds, the Company will make up for the shortfall by utilizing its internal resources or other means of financing. The Company may make appropriate adjustments as to the order of priority, allocation amount and methods in respect of the proposed use of proceeds based on the net proceeds actually raised and make a supplemental announcement as appropriate.

Our view on the terms of the Proposed Non-public Issuance of RMB Shares

As at the date of this letter, the detailed terms of the Proposed Non-public Issuance of RMB Shares have not been fully determined. Nevertheless, as stated in the letter from the Board, the Proposed Non-public Issuance will be conducted strictly in accordance with the applicable laws, rules and regulations governing non-public offerings by listed companies in the PRC.

We note that the Proposed Non-public Issuance of RMB Shares will be carried out under a comprehensive regulatory framework which stipulates, among other things, the pricing principles, subscription and allocation requirements, permitted use of proceeds, and mandatory lock-up arrangements. These regulatory requirements collectively provide safeguards to ensure that (i) the Issue Price is determined based on an objective, market-based mechanism, (ii) the allocation process is conducted in a fair and regulated manner, (iii) the use of proceeds is consistent with prescribed limits and aligned with value-enhancing purposes, and (iv) the interests of existing shareholders are protected. In addition, the Special Deal will be subject to approval by the Takeovers Code Independent Shareholders and the Proposed Non-public Issuance of RMB Shares will be subject to approval by Non-public Issuance Independent Shareholders of the Company and the final review and approval by the CSRC, which further enhances the transparency and fairness of the process.

Taking into account the above, and noting that the definitive pricing, allocation and use of proceeds for the Proposed Non-public Issuance of RMB Shares will ultimately be determined and implemented through a process mandated by a transparent and protective regulatory framework, we are of the view that the terms of the Proposed Non-public Issuance of RMB Shares, insofar as they are ascertainable at this stage, are fair and reasonable so far as the Company and its shareholders are concerned.

10.4 Our view on the Special Deal

Since the Proposed Non-public Issuance of RMB Shares is expected to complete within 6 months of the completion of the Proposed Acquisition, and may be an arrangement made between the Company and certain shareholders, which is not capable of being extended to all Shareholders, the Proposed Non-public Issuance of RMB Shares constitutes a special deal of the Company under Rule 25 of the Takeovers Code and requires the consent of the Executive. Such consent, if granted, will be subject to (i) our opinion as independent financial adviser on the fairness and reasonableness of the terms of the Special Deal are as far as the Takeovers Code Independent Shareholders are concerned; and (ii) the approval of the Special Deal by the Takeovers Code Independent Shareholders by way of poll at the EGM.

Having considered the following factors, we are of the view that the terms of the Special Deal (i.e., the Proposed Non-public Issuance of RMB Shares and the transactions contemplated thereunder) are fair and reasonable and in the interests of the Company and its Takeovers Code Independent Shareholders as a whole:

(i) **Ongoing cash flow pressures and liquidity needs:** As demonstrated above, the Group has experienced persistent cash flow deficits, with cash generated from operating activities insufficient to cover investing activities. The Group therefore requires ongoing funding to maintain sufficient liquidity cushion to support its enlarged business, repay its interesting bearing debts and supplement its working capital.

(ii) **Strengthening capital structure following the Proposed Acquisition:** As advised by Management, the consolidation of the Target Company has increased the Group's debt level. The equity fundraising is intended to improve the Enlarged Group's capital structure, reduce reliance on debt financing and enhance overall financial stability.

(iii) **Clear and value-accretive use of proceeds:** As stated in the letter from the Board, approximately 51.03% of the proceeds will be allocated to post-Acquisition integration and expansion — particularly the upgrade of the Target Company's 12-inch production lines and the development of 12-inch specialty processes. These enhancements, including equipment modifications and replacements, are expected to improve capacity utilization, support multiple specialty platforms, and strengthen the Enlarged Group's core competitiveness and resilience against market fluctuations.

(iv) **Efficiency and streamlined regulatory process:** The Proposed Acquisition and the Proposed Non-public Issuance of RMB Shares are both subject to CSRC review. Conducting the Proposed Non-public Issuance of RMB Shares alongside the Acquisition allows the Company to undergo a consolidated approval process, improving efficiency and reducing time and transaction costs for the Group.

(v) **Lack of preferable funding alternatives:** Based on our discussion with the Management, other fundraising channels were considered but found unsuitable. Bank or money-lender financing is generally restricted to project-specific purposes and cannot be applied to replenish general working capital. Such borrowings would also increase interest expenses and leverage, contrary to the Group's objective of optimizing its capital structure. Public issuance or placement of RMB-shares is subject to stricter restrictions on the permitted use of proceeds, including a cap whereby no more than 30% may be applied to working capital or debt repayment, rendering it unsuitable given the Group's intended allocation of funds.

(vi) **Fairness and reasonableness of the Proposed Non-public Issuance:** Based on our analysis of the pricing mechanism, allocation method and regulatory safeguards governing the Proposed Non-public Issuance of RMB Shares, and noting that the definitive pricing, allocation and use of proceeds will be determined through a transparent and protective regulatory framework, we consider the terms of the Proposed Non-public Issuance to be fair and reasonable from a financial perspective.

Taking all the above factors into account, we concur with Management that the terms of the Special Deal are fair and reasonable and in the interests of the Company and the Takeovers Code Independent Shareholders as a whole.

11. Potential dilution effect on shareholding interests

For illustrative purpose, set out below is a table showing the shareholding structure of the Company:

(i) as at the Latest Practicable Date

	Shareholding as at Latest Practicable Date					
Shareholders	**Hong Kong Shares held**	**Percentage of Hong Kong Shares held**	**RMB Shares held**	**Percentage of RMB Shares held**	**Total Shares held**	**Percentage of issued Share capital**(Note 2)
Huahong Group	347,605,650	26.14%	1,198,517	0.29%	348,804,167	20.07%
SAIL	188,961,147	14.21%	–	–	188,961,147	10.87%
Shanghai IC Fund	–	–	–	–	–	–
Guotou IC Fund	–	–	–	–	–	–
China IC Fund II	–	–	48,334,249	11.85%	48,334,249	2.78%
Others(Note 1)	–	–	16,856,987	4.13%	16,856,987	0.97%
Huahong Concert Group sub-total	*536,566,797*	*40.35%*	*66,389,753*	*16.28%*	*602,956,550*	*34.70%*
China IC Fund(Note 3)	62,351,603	4.69%	–	–	62,351,603	3.59%
Other public Shareholders	730,950,793	54.96%	341,360,247	83.72%	1,063,626,042	61.71%
Total	**1,329,869,193**	**100%**	**407,750,000**	**100%**	**1,737,614,193**	**100.00%**

(ii) immediately after Completion (assuming that (a) there will not be any further adjustments to the issue price of the Consideration Shares of RMB43.34 per Consideration Share; and (b) there will be no change in the total issued share capital of the Company since the Latest Practicable Date save for the issue of the RMB Shares pursuant to the Acquisition Agreement (as supplemented by the Supplemental Agreement); and

	Shareholding immediately after completion of the Proposed Acquisition					
Shareholders	**Hong Kong Shares held**	**Percentage of Hong Kong Shares held**	**RMB Shares held**	**Percentage of RMB Shares held**	**Total Shares held**	**Percentage of issued Share capital**(Note 2)
Huahong Group	347,605,650	26.14%	125,530,570	20.97%	473,136,220	24.54%
SAIL	188,961,147	14.21%	–	–	188,961,147	9.80%
Shanghai IC Fund	–	–	30,761,109	5.14%	30,761,109	1.60%
Guotou IC Fund	–	–	15,619,216	2.61%	15,619,216	0.81%
China IC Fund II	–	–	68,390,263	11.43%	68,390,263	3.55%
Others(Note 1)	–	–	16,856,987	2.82%	16,856,987	0.87%
Sub-total	*536,566,797*	*40.35%*	*257,158,145*	*42.97%*	*793,724,942*	*41.16%*
China IC Fund	62,351,603	4.69%	–	–	62,351,603	3.23%
Other public Shareholders	730,950,793	54.96%	341,360,247	57.03%	1,072,311,040	55.61%
Total:	**1,329,869,193**	**100%**	**598,518,392**	**100%**	**1,928,387,585**	**100.00%**

(iii) immediately after Completion and the Proposed Non-public Issuance of RMB Shares (assuming that (a) the total amount of supporting funds to be raised under the Proposed Non-public Issuance of RMB Shares is RMB 7,556,286,000; (b) there will not be any further adjustments to the issue price of the Consideration Shares of RMB43.34 per Consideration Share; (c) the issue price of the Proposed Non-public Issuance of RMB Shares shall be RMB95.85 per RMB Share (assuming the price determination date is the Latest Practicable Date); (d) the subscribers of the Proposed Non-public Issuance of RMB Shares are and remain as public Shareholders of the Company; and (e) there will be no change in the total issued share capital of the Company since the Latest Practicable Date save for the issue of the RMB Shares pursuant to the Acquisition Agreement (as supplemented by the Supplemental Agreement) and under the Proposed Non-public Issuance of RMB Shares):

Shareholding immediately after completion of the Proposed Acquisition and the Proposed Non-public Issuance of RMB Shares

Shareholders	**Hong Kong Shares held**	**Percentage of Hong Kong Shares held**	**RMB Shares held**	**Percentage of RMB Shares held**	**Total Shares held**	**Percentage of issued Share capital** *(Note 2)*
Huahong Group	347,605,650	26.14%	125,530,570	18.53%	473,136,220	23.57%
SAIL	188,961,147	14.21%	–	–	188,961,147	9.41%
Shanghai IC Fund	–	–	30,761,109	4.54%	30,761,109	1.53%
Guotou IC Fund	–	–	15,619,216	2.31%	15,619,216	0.78%
China IC Fund II	–	–	68,390,263	10.10%	68,390,263	3.41%
Others *(Note 1)*	–	–	16,856,987	2.49%	16,856,987	0.84%
Huahong Concert Group sub-total	*536,566,797*	*40.35%*	*257,158,145*	*37.97%*	*793,724,942*	*39.54%*
China IC Fund *(Note 3)*	62,351,603	4.69%	–	–	62,351,603	3.11%
Other public Shareholders	730,950,793	54.96%	420,194,738	62.03%	1,151,145,531	57.35%
Total	**1,329,869,193**	**100%**	**677,352,883**	**100%**	**2,007,222,076**	**100.00%**

Notes:

1. Including Shanghai Hua Hong International, Inc., Haitong Innovation Securities Investment Co., Ltd. (海通創新證券投資有限公司), Guotai Junan Zhengyu Investment Co., Ltd. (國泰君安證裕投資有限公司), Shanghai Technology Venture Investment (Group) Co., Ltd. (上海科技創業投資(集團)有限公司) and Wisdom Power Technology Limited.

2. Percentage holdings are subject to rounding adjustments and may not add up to the aggregate figures shown or 100%.

3. China IC Fund is not one of the Vendors, and is not considered to be part of the Huahong Concert Group given it is not a party acting in concert with Huahong Group nor China IC Fund II to consolidate control over the Company, based on its historical investment in the Company and different compositions of fund investors and decision-making process vis-à-vis China IC Fund II.

As illustrated above, the shareholding in the Company held by the existing other public Shareholders would be diluted from approximately 61.71% as at the Latest Practicable Date to approximately 55.61% upon the allotment and issuance of the Consideration Shares and completion of the Proposed Acquisition. Upon the completion of the Proposed Acquisition and the Proposed Non-public Issuance of RMB Shares, the shareholding in the Company held by other public Shareholders would increase to 57.35% assuming the subscribers of the Proposed Non-public Issuance of RMB Shares are and remain as public Shareholders of the Company. For further details on the shareholding structure of the Company, please make reference to the letter from the Board in the Circular.

We noted that there will be dilution to the shareholdings in the Company held by the existing public Shareholders as a result of the issuance of the Consideration Shares. However, having considered (i) the benefits of the Proposed Acquisition as set out in the section headed "Reasons for and benefits of the Proposed Acquisition" and (ii) the terms of the Acquisition Agreement (as supplemented by the Supplemental Agreement) being fair and reasonable; (iii) the Compensation Agreement; (iv) the ongoing cashflow pressures and funding needs; and (v) the fact that existing Shareholders have also benefited from recent appreciation in the Company's share price prior to the Announcement, reflecting market anticipation of the Company's strategic initiatives and enhanced prospects, we are of the view that the dilution effect of around 9.88% or 6.1 percentage point on the shareholding of the Takeovers Code Independent Shareholders and the Proposed Acquisition LR Independent Shareholders upon the Completion is acceptable and justifiable.

We note that since the Announcement, the market prices of the Group's shares including both RMB Shares and H shares have increased and have generally traded above the Issue Price of the Consideration Shares. This indicates that the market has responded positively to the Proposed Acquisition, reflecting investors' confidence in its strategic rationale and the expected benefits arising from the Proposed Acquisition. In our view, the appreciation in the share price mitigates the dilution impact to the existing shareholders, as the increase in the Group's overall market capitalization suggests that the value of the shareholders' investments has not been adversely affected notwithstanding the enlarged share base. Furthermore, the continued trading of the Group's shares above the Issue Price of the Consideration Shares implies that the Issue Price is not considered unduly low by the market and that existing shareholders may continue to benefit from potential upside if the Acquisition delivers the anticipated synergies and earnings contribution. Accordingly, we consider that the potential dilution impact on the existing shareholders is acceptable and justifiable.

RECOMMENDATION

Having taken into account the principal factors and reasons as mentioned above, we are of the view that while the Proposed Acquisition is not conducted in the ordinary and usual course of business of the Group, (i) the Proposed Acquisition is on normal commercial terms; and (ii) the Proposed Acquisition, the Proposed Acquisition Specific Mandate, the Whitewash Waiver and the Special Deal in relation to the Proposed Non-public Issuance of RMB Shares are fair and reasonable so far as the Proposed Acquisition LR Independent Shareholders and the Takeovers Code Independent Shareholders are concerned and in the interests of the Company, the Proposed Acquisition LR Independent Shareholders and the Takeovers Code Independent Shareholders as a whole. Accordingly, we advise the Independent Board Committee to recommend the Proposed Acquisition LR Independent Shareholders and the Takeovers Code Independent Shareholders, and we also recommend the Proposed Acquisition LR Independent Shareholders and the Takeovers Code Independent Shareholders to vote in favor of the relevant resolution for approving the Proposed Acquisition, the Proposed Acquisition Specific Mandate, the Whitewash Waiver and the Special Deal at the EGM.

Yours faithfully,
For and on behalf of
Innovax Capital Limited

Alvin Kam
Managing Director

Erica Ling
Director

Notes:

Mr. Alvin Kam is a Responsible Officer under the SFO to engage in Type 1 (Dealing in Securities) and Type 6 (advising on corporate finance) regulated activity and has over 21 years of experience in investment banking and corporate finance.

Ms. Erica Ling is a Responsible Officer under the SFO to engage in 1 (Dealing in Securities) and Type 6 (advising on corporate finance) regulated activity and has around 13 years of experience in investment banking and corporate finance.