邁時資本
MAXA CAPITAL

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28 November 2023

To the Independent Board Committee and the Independent Shareholders

Dear Sirs,

CONTINUING CONNECTED TRANSACTIONS, DISCLOSEABLE TRANSACTIONS AND MAJOR TRANSACTIONS
I. RENEWAL OF CONTINUING CONNECTED TRANSACTIONS UNDER THE EXISTING AGREEMENTS AND
II. PROPOSED REVISION OF ORIGINAL ANNUAL CAPS

INTRODUCTION

We refer to our appointment as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in respect of (i) the terms of the Non-exempt Transactions and the relevant proposed caps for such transactions (the "**Non-Exempt Annual Caps**"); and (ii) the term of the underlying specific contracts in relation to Finance Lease Services to be entered into pursuant to the Finance Lease and Factoring Framework Agreement which may exceed three years (the "**Finance Lease Term**"), details of which are set out in the letter from the Board (the "**Letter from the Board**") contained in the circular dated 28 November 2023 issued by the Company (the "**Circular**") of which this letter forms part. Terms used in this letter shall have the same meanings as those defined in the Circular unless the context requires otherwise.

References are made to the announcements of the Company dated 21 August 2020, 30 August 2022, 5 September 2022 and 28 October 2022, and the circulars dated 10 November 2020 and 16 January 2023 in relation to, among other things, the continuing connected transactions of the Group with AVIC Group contemplated under each of the Existing Agreements. As the term of the Existing Agreements will expire on 31 December 2023 and the Group intends to continue to enter into the transactions of similar nature after that date, the Company entered into the (i) the Mutual Product Supply Agreement; (ii) the Mutual Service Supply Agreement; (iii) the AVIC Airborne Mutual Product and Service Supply Framework Agreement; (iv) the Financial Services Framework Agreement; and (v) the Finance Lease and Factoring Framework Agreement (collectively, the "**Non-Exempt Renewal Agreements**") for a term of three years commencing from 1 January 2024. Most of the terms of the Non-Exempt Renewal Agreements are substantially the same as those of the Existing Agreements.

Reference is also made to the announcement of the Company dated 10 June 2022 and the circular of the Company dated 29 September 2022 in relation to the Share Swap and Absorption. After the Share Swap and Absorption, the number of subsidiaries of the Company has increased, the Board expects that there will be an increase in the Group's demand for the AVIC Finance Factoring Services, and the Original Annual Cap in respect of the AVIC Finance Factoring Services under the Existing Financial Services Framework Agreement will be insufficient to meet the Group's expected needs. On 22 August 2023, the Company and AVIC Finance entered into the Supplemental Financial Services Framework Agreement to increase the Original AVIC Finance Factoring Services Cap to the relevant Proposed Revised Cap.

As at the Latest Practicable Date, AVIC is a controlling shareholder of the Company holding directly and indirectly 60.25% of all issued Shares. Each of AVIC Finance and AVIC Lease is a subsidiary of AVIC. AVIC Airborne is a connected subsidiary of the Company by virtue of being directly owned as to over 10% by AVIC. Accordingly, each of AVIC, AVIC Finance, AVIC Lease and AVIC Airborne is a connected person of the Company pursuant to Chapter 14A of the Hong Kong Listing Rules. The transactions contemplated under the Non-Exempt Renewal Agreements, the Supplemental Financial Services Framework Agreement and the Proposed Revised Cap for the AVIC Finance Factoring Services therefore constitute continuing connected transactions.

As the highest applicable percentage ratio in respect the Non-Exempt Transactions exceeds 5%, such continuing connected transactions are subject to, among others, Independent Shareholders' approval requirements under Chapter 14A of the Hong Kong Listing Rules.

The Independent Board Committee comprising all independent non-executive Directors has been formed to advise and provide recommendations to the Independent Shareholders in respect of the Non-Exempt Transactions and the Non-Exempt Annual Caps. We, Maxa Capital, have been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in this regard. Given that the Finance Lease Term may exceeds three years, the Company has also appointed us as the Independent Financial Adviser to explain why the said specific contracts in relation to Finance Lease Services require a longer period and to confirm that it is a normal business practice for agreements of this type to be of such duration pursuant to Rule 14A.52 of the Hong Kong Listing Rules.

OUR INDEPENDENCE

As at the Latest Practicable Date, we were independent from the Company in accordance with Rule 13.84 of the Hong Kong Listing Rules and, accordingly, are considered eligible to give independent advice on the Non-Exempt Transactions, the Non-Exempt Annual Caps and the Finance Lease Term. Apart from normal professional fees payable to us in connection with this appointment, no arrangement exists whereby we will receive any fees or benefits from the Company. Save for this appointment, we were appointed three times as the independent financial adviser by the Company in the last two years in relation to the Share Swap and Absorption and certain continuing connected transactions of the Company, details of which were set out in the circular of the Company dated 29 September 2022, 16 January 2023 and 27 April 2023. The aforesaid previous appointments were limited to providing one-off independent advisory service, for which Maxa Capital received normal professional fees. Accordingly, we do not consider such previous appointments give rise to any conflict of interest for Maxa Capital in acting as the Independent Financial Adviser this time.

BASIS OF OUR OPINION

In formulating our opinion, we have relied on the statements, information, opinions and representations contained in the Circular and the information and representations provided to us by the Directors and the management of the Company (the "**Management**"). We have reviewed, inter alia, the statements, the information, opinions and representations contained or referred to in the Circular and the information and representations as provided to us by the Directors and the Management. We consider that we have reviewed sufficient and relevant information and documents and have taken reasonable steps as required under Rule 13.80 of the Hong Kong Listing Rules to reach an informed view and to provide a reasonable basis for our recommendation. We have assumed that (i) all statements, information and representations provided by the Directors and the Management; and (ii) the information referred to in the Circular, for which they are solely responsible, were true and accurate at the time when they were provided and continued to be so as at the Latest Practicable Date and the Shareholders will be notified of any material changes to such information and representations before the EGM. We have also assumed that all statements of belief, opinion, intention and expectation made by the Directors in the Circular were reasonably made after due enquiry and careful consideration.

The Company confirmed that they have, at our request, provided us with all currently available information and documents which are available under present circumstances to enable us to reach an informed view and we have relied on the accuracy of the information contained in the Circular so as to provide a reasonable basis for our opinion. We have no reason to suspect that any material facts or information have been withheld or to doubt the truth, accuracy and completeness of the information and facts contained in the Circular, or the reasonableness of the representation and opinions expressed by the Company, its advisers, the Directors and the Management. We have not, however, conducted any independent verification of the information included in the Circular and provided to us by the Directors and the Management nor have we conducted any form of in-depth investigation into the business and affairs or the future prospects of the Company, AVIC, AVIC Finance, AVIC Lease, AVIC Airborne and each of their respective subsidiaries or associates.

PRINCIPAL FACTORS AND REASONS CONSIDERED

In arriving at our opinion in respect of the Non-Exempt Transactions, the Non-Exempt Annual Caps and the Finance Lease Term, we have taken into consideration the following principal factors and reasons:

1. Background

1.1 Information of the Group

The Company is a joint stock limited liability company established in the PRC, whose H shares are listed on the Stock Exchange. The Company is mainly engaged in the research, development, manufacture and sales of aviation products and relevant engineering services.

Set out below is the summarised financial information of the Group for the two years ended 31 December 2022 as extracted from the 2022 annual report and the six months ended 30 June 2022 and 2023 as extracted from the 2023 interim report of the Company:

	For the year ended 31 December		**For the six months ended 30 June**	
	2021	**2022**	**2022**	**2023**
	(audited)	**(audited)**	**(restated)**	**(unaudited)**
	RMB (million)	*RMB (million)*	*RMB (million)*	*RMB (million)*
Revenue	60,296.28	63,639.43	33,515.01	40,872.60
Net profit attributable to owners	2,369.28	2,216.40	1,217.01	1,542.80

	As at 31 December		**As at 30 June**
	2021	**2022**	**2023**
	(audited)	**(restated)**	**(unaudited)**
	RMB (million)	*RMB (million)*	*RMB (million)*
Total assets	133,889.14	179,122.04	178,282.88
Total liabilities	79,122.63	103,602.75	93,479.03
Total equity	54,766.50	75,519.28	84,803.85

For the year ended 31 December 2022 ("**FY2022**"), the Group's revenue amounted to approximately RMB63,639.43 million, representing an increase of approximately 5.54% as compared to that for the year ended 31 December 2021 ("**FY2021**"), which is mainly attributable to the increase in revenue of the Group's aviation ancillary system and related business of approximately 10.28%. The Group recorded profit attributable to owners of approximately RMB2,216.40 million in FY2022, representing a decrease of approximately 6.45% as compared to that for FY2021, which is mainly attributable to (i) the decrease in results of Avicopter resulted in a year-on-year decline in its net profit attributable to the Company; and (ii) the enhanced research and development inputs by the Group resulted in an increase in the research and development expenses and other expenses.

For the six months ended 30 June 2023 ("**1H2023**"), the Group's revenue amounted to approximately RMB40,872.60 million, representing an increase of approximately 21.95% as compared to that for the six months ended 30 June 2022 ("**1H2022**"), which is mainly attributable to the increase in revenue of the Group's aviation entire aircraft business of approximately 56.28% and the increase in revenue of the Group's aviation ancillary system and related business of approximately 20.66%. The Group recorded profit attributable to owners of approximately RMB1,542.80 million in 1H2023, representing an increase of approximately 26.77% as compared to that for 1H2022, which is mainly attributable to the increase in revenue of helicopters and avionics products and the increase in gross profit due to the price adjustment of certain helicopter products during the reporting period.

The Group's net assets have been increasing FY2021, FY2022 and 1H2023. The Group's net assets as at 31 December 2022 increased by approximately 37.89% as compared to that as at 31 December 2021, which was mainly due to the Share Swap and Absorption. The Group's net assets as at 30 June 2023 increased by approximately 12.29% as compared to that as at 31 December 2022, which was mainly due to the proceeds of approximately RMB5.5 billion from non-public issuance of domestic Shares by the Company and non-public issuance of A shares by a subsidiary of the Company and net profit of the Group of approximately RMB4 billion during 1H2023.

1.2 Information of AVIC

AVIC is controlled by the State Council of the PRC, and is mainly engaged in the development and manufacture of aviation products and non-aviation products. AVIC is the controlling Shareholder of the Company, holding directly and indirectly 60.25% equity interest in the Company as at the Latest Practicable Date.

1.3 Information of AVIC Airborne

AVIC Airborne is a joint stock limited company incorporated in the PRC, whose A shares are listed on the Shanghai Stock Exchange. AVIC Airborne is a 16.50% owned subsidiary of the Company, which is mainly engaged in the manufacture and sale of avionics products and electromechanical system products.

1.4 Information of AVIC Finance

AVIC Finance is a limited liability company established in the PRC and a subsidiary of AVIC as at the Latest Practicable Date. It is licensed by the CBIRC and is engaged in the provision of financial services which principally include absorption of deposits of member companies, handling loans of member companies, handling bills discounting of member companies, handling funds settlement and acceptance/payment of member companies, providing entrustment loans to member companies, underwriting of debentures, non-financing guarantee letters, financial advisory services, credit certification and advisory agency services, inter-bank lending, handling bills acceptance of member companies, handling buyer's credit and spending credit of member companies, fixed-income investments, and other businesses as may be approved by the NAFR.

So far as the Group is aware, AVIC Finance is subject to the following internal control measures, which ensure the safety of the Group's deposits with AVIC Finance:

(a) As a licensed financial institution in the PRC, AVIC Finance is under the supervision of the PBOC and the NAFR, including the regular examination of the audited financial statements and other relevant materials required to be filed by AVIC Finance, as well as face-to-face review and interview with the senior management of AVIC Finance;

(b) AVIC Finance has established strict internal control measures to ensure effective risk management and compliance with relevant laws and regulations, including the corporate governance structure, internal standards and policies and standard operating procedures, as well as intra-group check and balance mechanism; and

(c) AVIC Finance will adopt the following additional internal control measures in respect of the Deposit Services provided by AVIC Finance under the Financial Services Framework Agreement: (i) the Group shall have the right to use the deposit funds to offset against any accounts payable by the Group to AVIC Finance in the event that the Group is not able to recover its deposits with AVIC Finance; and (ii) AVIC Finance shall submit monthly and annual reports to the Group in respect of the Group's deposits with AVIC Finance during the period of having deposits with AVIC Finance.

1.5 Information of AVIC Lease

AVIC Lease is a limited liability company established in the PRC and a subsidiary of AVIC as at the Latest Practicable Date. It is mainly engaged in finance leasing, self-owned equipment leasing, residual value processing and maintenance of leased assets, contract energy management, and consulting services relevant to the above businesses, and non-bank financial services as approved by relevant departments such as factoring.

2. Reasons for and benefits

2.1 Reasons for and benefits of continuing connected transactions under Mutual Product Supply Agreement, Mutual Service Supply Agreement and AVIC Airborne Mutual Product and Service Supply Framework Agreement

Aviation industry is complex and technology intensive. The manufacturing of an entire aircraft (including the Group's helicopters and trainers) requires different products, parts and components from different enterprises.

The Group is an aviation manufacturing enterprise mainly engaged in the research, development, manufacture and sales of aviation entire aircraft (mainly helicopters and trainer aircraft) and aviation parts and components (mainly avionics products and electromechanical products), and the provision of aviation engineering services.

AVIC Group is the sole relatively complete system aviation manufacturer established under the support of the PRC's national government. It has the research and development capacities to manufacture aviation products independently, and it is mainly engaged in the manufacturing of aircraft, airborne equipment systems and other related pairing products and systems (other than helicopters, trainer aircrafts and aviation parts products manufactured by the Group).

(1) Mutual Product Supply Agreement

The Group is the sole production platform of helicopters and main production platform of trainer aircrafts for AVIC Group and it primarily provides the aviation entire aircrafts (mainly trainers and general aircrafts) and aviation parts and components (mainly avionics products and electromechanical products) to AVIC Group under the Mutual Product Supply Agreement to meet the orders received by AVIC Group from independent third parties and the production demands of AVIC Group.

The Group mainly procures from AVIC Group the necessary parts and components for manufacturing helicopters and trainers by the Group, such as control and navigation systems researched and developed by AVIC Group.

Due to the high technology barriers in aviation industry and the high quality requirements of customers, it is also difficult for the Group and AVIC Group to source substitute aviation products or aviation parts and components of comparable quality, specifications and value in the PRC from other producers.

(2) Mutual Service Supply Agreement

The Group primarily provides the aviation engineering services to AVIC Group through AVIC CAPDI, and provide labour services to AVIC Group; while AVIC Group primarily provides labour services and other support or composite services to the Group such as import and export agency services, test flight services and logistic services; in relation to the supply of labour services, AVIC Group will supply to the Group, and vice versa, depending on the requirements of different projects and the needs for the manufacturing businesses. The services under the Mutual Service Supply Agreement are essential to facilitate the smooth running of the Group's business operations.

(3) AVIC Airborne Mutual Product and Service Supply Framework Agreement

The transactions contemplated under the AVIC Airborne Mutual Product and Service Supply Framework Agreement are intragroup transactions of the Group, and are mostly product pairing transactions between AVIC Airborne Group and the Group's entire aircraft business. Avionics products and electromechanical products are necessary aviation parts and components for the manufacturing of the aviation entire aircraft. AVIC Airborne Group is the major supplier for the related avionics products and electromechanical products in the Group's helicopters and trainers.

The Company considers that the products and services provided by the relevant party are different from those provided by the counterparty, and are necessary for the business operation of the counterparty. Based on the following grounds, the Directors consider that it is beneficial to continue the relevant continuing connected transactions by way of entering into new framework agreements as set out in Section I of the Letter from the Board:

(a) the historical connection and long-standing business cooperation relationship between the Group and AVIC Group and AVIC Airborne Group;

(b) AVIC, AVIC Airborne and their respective associates generally have a better understanding of the Group's business and can better ensure the standards of technology, quality, delivery and technical support of the products to meet the Group's requirements;

(c) the continuing connected transactions between AVIC, AVIC Airborne and their respective associates and the Group in relation to mutual supply of products and services have facilitated and will continue to facilitate the overall operations and growth of the Group's business; and

(d) the Directors (including the independent non-executive Directors) consider that such continuing connected transactions are and will continue to be conducted on normal commercial terms or better to the Group and in the ordinary and usual course of business of the Group, and in the interests of the Company and the Shareholders as a whole, and the terms and the proposed caps of such continuing connected transactions will continue to be fair and reasonable to the Company.

We have discussed with Management and understood that the Group sells a large amount of defense related products to AVIC Group and the Group is currently the only helicopter production platform and a main production platform of training aircraft and aviation airborne system products in AVIC Group after several restructuring activities. In respect of certain aviation entire aircraft, AVIC Group is a procurement agent representing the government to purchases entire aircraft from the Group; in respect of the aviation parts, AVIC Group needs to purchase aviation parts from the Group to satisfy its production demand of aircraft without better alternatives due to the high technical barriers of the aviation manufacturing industry and the leading position of the Group in the industry. Therefore, the revenue of the Group generated from the AVIC Group should not be regarded as the Group's reliance on the AVIC Group while the Group and the AVIC Group rely on each other for business development. In addition, Harbin Aircraft Industry Group Co., Ltd.* and Changhe Aircraft Industries (Group) Co., Ltd.* have become subsidiaries of the Group after assets restructuring and the connected transactions in relation to sales of the aviation entire aircraft have been reduced accordingly. Taking into account the transaction model between the Group and AVIC Group as described above, we concur with the Directors that the Group can develop independently in a steady and healthy way, and there is no major reliance risk in this regard.

2.2 Reasons for and benefits of continuing connected transactions under Financial Services Framework Agreement

The reasons for the Group to enter into the Financial Services Framework Agreement are as follows:

(a) the terms (including the interest rates) on the Deposit Services, the Loan Services, the AVIC Finance Factoring Services and the Other Financial Services offered by AVIC Finance to the Group will be equal to or more favourable than those offered to the Group by major commercial banks in the PRC;

(b) AVIC Finance is regulated by the PBOC and the NAFR and provides its services in accordance with and in satisfaction of the rules and operational requirements of these regulatory authorities. In addition, so far as the Group is aware, AVIC Finance has internal control measures in place, the details of which are disclosed in paragraph 4 under Section V of the Letter from the Board, which ensure the safety of the Group's deposits with AVIC Finance;

(c) AVIC Finance's understanding of the Group's operations will enable it to provide more expedient and efficient services than major commercial banks in the PRC;

(d) pursuant to the relevant regulations of the PBOC and the NAFR, the customers of AVIC Finance are limited to the group members of AVIC Group, which will ensure more control by AVIC Finance of the risks that it may be exposed to as compared with other financial entities; and

(e) the Group could satisfy its demands for financial services in daily business operations from the Financial Services Framework Agreement.

2.3 Reasons for and benefits of continuing connected transactions under Finance Lease and Factoring Framework Agreement

The reasons for the Group to enter into the Finance Lease and Factoring Framework Agreement are as follows:

(a) the Finance Lease and Factoring Framework Agreement and the transactions contemplated thereunder will help to reduce capital occupation by accounts receivable; satisfy the funding requirement for business development and optimise its financial management and improve its capital usage efficiency and reduce financing costs and risks and thus will facilitate and smooth the business development and operations of the Company; and

(b) as compared to other financial institutions such as commercial banks, AVIC Lease is able to offer greater flexibility on the financing terms and provide financing services more efficiently with streamlined procedures.

These advantages make AVIC Lease Factoring Services a suitable financing channel complementary to other channels available to the Group.

2.4 Reasons for and benefits of entering into the Supplemental Financial Services Framework Agreement and the Proposed Revised Cap for the AVIC Finance Factoring Services

Reference is made to the announcement of the Company dated 10 June 2022 and the circular of the Company dated 29 September 2022 in relation to the Share Swap and Absorption. Upon completion of the Share Swap and Absorption, there was an increase in the scope and the amount of services to be obtained by the Group under the Existing Financial Services Framework Agreement arising from an increase in subsidiaries of the Company. Furthermore, it is expected that there will be an increase in transaction amounts under the Existing Financial Services Framework Agreement for the year ending 31 December 2023 as a result of the continued growth and increase in scale of operation of the Group. Therefore, the entering into the Supplemental Financial Services Framework Agreement and the Proposed Revised Cap for the AVIC Finance Factoring Services are beneficial to and necessary for the business operation of the Group.

Having considered the above, we concur with the Directors' view that the Non-exempt Transactions are conducted in the ordinary and usual course of business of the Group and in the interests of the Company and the Shareholders as a whole.

3. Principal terms of the Non-Exempt Renewal Agreements and the Supplemental Financial Services Framework Agreement

3.1 Mutual Product Supply Agreement

Date	:	22 August 2023
Parties	:	AVIC (for and on behalf of AVIC Group) The Company (for itself and on behalf of its subsidiaries)
Term	:	Three years from 1 January 2024 to 31 December 2026
Mutual supply of products	:	AVIC Group and the Group will supply the manufacturing raw materials, parts and components, finished and semi-finished aviation products involved in the production and operations of the respective aviation products of each other (including but not limited to aviation entire aircraft and aviation parts and components to the Group, and the helicopters, airplanes and aviation parts and component to AVIC Group) and the related sales and ancillary services.
Key transaction principles	:	If any independent third party can supply the same type of products on the same terms, AVIC Group or the Group (as the case may be) shall give preference to use products supplied by the Group or AVIC Group (as the case may be). If any independent third party can supply the same type of products at a better price than AVIC Group or the Group (as the case may be) offers, the Group or AVIC Group (as the case may be) shall be entitled to procure products from that independent third party. The quality standard of the products and the terms and conditions of supply given by AVIC Group to the Group shall not be less favourable than those offered by the independent third parties under comparable conditions.

Pricing principles	:	The price of the products and ancillary services will be determined as follows: (i) as most products under the Mutual Product Supply Agreement are designated aviation products, the Government- prescribed Price shall apply; (ii) if there is no Government-prescribed Price, the Market Price as determined by tender procedures or other means, such as price inquiry and price comparison by fee quotations if tender procedures are not adopted (as the case may be) shall apply; and (iii) if there is no Market Price, the Contractual Price shall apply.
Payment	:	Specific payment terms (including time and method of payment) are to be agreed between the parties by entering into the specific product supply agreement under each transaction.

3.2 Mutual Service Supply Agreement

Date	:	22 August 2023
Parties	:	AVIC (for and on behalf of AVIC Group) The Company (for itself and on behalf of its subsidiaries)
Term	:	Three years from 1 January 2024 to 31 December 2026
Mutual supply of services	:	AVIC Group will supply certain services relating to the production and business operations of the Group including, without limitation, (i) supply of power such as electricity, water and steam; (ii) property management and maintenance; (iii) labour services; (iv) equipment purchase, maintenance, repair and leasing services; (v) construction and transportation; (vi) design, consultation and network related services; (vii) cultural, educational, hygienic, social security and logistic services; (viii) import and export agency services; (ix) test flight and technology and quality monitoring services; (x) engineering and equipment subcontracting services; and (xi) other related services.

The Group will supply certain services relating to the production and business operations of AVIC Group including, without limitation, (i) supply of power such as electricity, water and steam; (ii) property management and maintenance; (iii) labour services; (iv) equipment maintenance, repair and leasing services; (v) construction and transportation; (vi) design, consultation and network related services; (vii) enterprise entrustment services; (viii) engineering technology (including but not limited to planning, consultation, design and supervision), project engineering main contracting (including aviation engineering services) and equipment main contracting services; and (ix) other related services.

Considering the large number of subsidiaries of the Group and AVIC Group and each of them having different businesses across different regions, despite the types of services supplied by AVIC Group to the Group and the services supplied by the Group to AVIC Group are similar, the services in fact are not the same as they are supplied to different entities in different regions. These services are related to the business operations of the Group, in particular, (i) labour services are mainly required for the manufacturing processes; (ii) supply of power such as electricity, water and steam, (iii) equipment maintenance, repair and leasing services, (iv) design, consultation and network related services, are mainly support services to support the Group's different business segments especially when the entity(ies) demanding and supplying such services are located within the same manufacturing zone; (v) property management and maintenance, and (vi) construction and transportation, are general support services to the Group.

As mentioned above, there is a large number of subsidiaries under the Group and AVIC Group and they are spread across different regions. Within a production base (生產園區), certain subsidiaries of the Group and AVIC Group are located in it. Therefore, within such production base, depending on the specific needs and the capability of the subsidiaries of the Group, they would provide/obtain certain of the above services to/from AVIC Group, or vice versa. As these services are related to the business operation of the Group and are essential to facilitate the smooth running of the Group, therefore, the procurement of services by the Group under the Mutual Service Supply Agreement is in the interest of the Company and its shareholders.

Key transaction principles	:	If any independent third party can supply the same type of services on the same terms, AVIC Group or the Group (as the case may be) shall give preference to use the services supplied by the Group or AVIC Group (as the case may be). If any independent third party can supply the same type of services at a better price than AVIC Group or the Group (as the case may be) offers, the Group or AVIC Group (as the case may be) shall be entitled to opt for the services supplied by that independent third party. The quality standard of the services and the terms and conditions of supply given by AVIC Group to the Group shall not be less favorable than those offered by the independent third parties under comparable conditions.
Pricing principles	:	The price of the services under the agreement will be determined as follows: (i) for power supply services such as the provision of electricity, water, steam, etc., if such power was originally procured at the Government-prescribed Price or the Government-guidance Price, the Government-prescribed Price or the Government- guidance Price shall apply; (ii) for services such as construction, transportation, design, consultation and network design, equipment leasing and other services where the Market Price is available, the Market Price as determined by tender procedures or other means, such as price inquiry and price comparison by fee quotations if tender procedures are not adopted (as the case may be) shall apply; (iii) for the engineering technology services to be supplied by the Group to AVIC Group (including design, consultation and supervision services), and the engineering and equipment subcontracting services supplied by AVIC Group to the Group, the Market Price or (where applicable) Market Price as determined by tender procedures shall apply. Such tender procedures shall be in compliance with the relevant PRC laws and regulations relating to tender and bidding (which set out, among other things, specific requirements for the bidders and construction projects which require tender and bidding); and

(iv) if there is no Market Price (for the provision of property management and maintenance services; equipment maintenance, repair and leasing services; cultural, educational, hygienic, social security and logistic services; import and export agency services; test flight and technology and quality monitoring services; and entrustment services), the Contractual Price shall apply.

Payment : Specific payment terms (including time and method of payment) are to be agreed between the parties by entering into specific services agreement under each transaction.

3.3 AVIC Airborne Mutual Product and Service Supply Framework Agreement

Date : 22 August 2023

Parties : The Company (for itself and on behalf of its subsidiaries, excluding AVIC Airborne Group)

AVIC Airborne (for itself and on behalf of its subsidiaries)

Term : Three years from 1 January 2024 to 31 December 2026

Mutual supply of products and services : The Group will supply to AVIC Airborne Group aviation parts and components, raw materials, related manufacturing, labour services, and engineering technology (including but not limited to planning, consultation, design and supervision), project engineering main contracting and equipment main contracting services, etc.

AVIC Airborne Group will supply to the Group aviation electronic products, mechanical electronics, parts and components, related manufacturing and labour services, and engineering and equipment subcontracting services.

Pricing principles : The price of products and/or services under the agreement will be determined as follows:

(i) as most products under the AVIC Airborne Mutual Product and Service Supply Framework Agreement are designated aviation products, the Government-prescribed Price shall apply;

(ii) if there is no Government-prescribed Price, the Market Price as determined by tender procedures or other means, such as price inquiry and price comparison by fee quotations if tender procedures are not adopted (as the case may be) shall apply;

(iii) if there is no Market Price, the Contractual Price shall apply;

(iv) for production and labour services where Market Price is available, the Market Price as determined through tender procedures or other means, such as price inquiry and price comparison by fee quotations if tender procedures are not adopted (as the case may be) shall apply; if there is no Market Price, the Contractual Price shall apply; and

(v) for engineering technology services (including design, consultation and supervision services), project engineering main contracting and equipment main contracting services, and engineering and equipment subcontracting services, the Market Price or (if applicable) the Market Price as determined by tender procedures shall apply. The tender procedures mentioned above shall be in compliance with the relevant PRC laws and regulations relating to tender and bidding (which set out, among other things, specific requirements for the bidders and construction projects which require tender and bidding).

Payment : The parties will make payment according to the AVIC Airborne Mutual Product and Service Supply Framework Agreement and the specific contracts entered into by the relevant member of the Group and AVIC Airborne Group for the provision of products or services.

Other major terms : If any independent third party can supply the same type of products or services at a better price than AVIC Airborne Group or the Group (as the case may be) offers, the Group or AVIC Airborne Group (as the case may be) shall be entitled to opt for the products or services supplied by that independent third party.

Subject to the terms of the AVIC Airborne Mutual Product and Service Supply Framework Agreement, if the product or service supplied by and the terms and conditions of supply given by AVIC Airborne Group or the Group (as the case may be) does not satisfy the needs of the Group or AVIC Airborne Group (as the case may be) in any aspect, the latter can procure identical or similar products or services from an independent third party.

3.4 Financial Services Framework Agreement

Date	:	22 August 2023
Parties	:	The Company (for itself and on behalf of its subsidiaries) AVIC Finance
Term	:	Three years from 1 January 2024 to 31 December 2026
Financial services	:	Pursuant to the Financial Services Framework Agreement, AVIC Finance has agreed to provide the Group with the Deposit Services, the Loan Services, the Settlement Services, the Non-financing Guarantee Letter Services, the AVIC Finance Factoring Services and the Other Financial Services (i.e. such other financial services (including but not limited to bill acceptance and discount services) as approved by the NAFR). The Group is entitled to elect the financial institutions providing the financial services, the amount of deposit and borrowings and the time of withdrawal of deposit based on its business needs.
Pricing principles	:	The pricing principles of the Deposit Services, the AVIC Finance Factoring Services and the Other Financial Services are as follows: (1) Deposit Services Interest rates for the Group's deposits with AVIC Finance shall not be lower than the benchmark interest rates during the same period as promulgated by the PBOC for the same type of deposit. The interest rates for the Group's RMB deposits with AVIC Finance shall not be lower than the listed average interest rates for the same type of deposits offered by major commercial banks of the PRC.

(2) AVIC Finance Factoring Services

The fees charged by AVIC Finance for the provision of the AVIC Finance Factoring Services shall not be higher than (a) the average fees charged by AVIC Finance to any third party with the same price determination factors as the Group during the same period (including credit rating, term, business category, enterprise category); and (b) the average fees charged by the major commercial banks in the PRC for the same type of services.

(3) Other Financial Services

The fees charged by AVIC Finance for the provision of the Other Financial Services shall not be higher than (a) the maximum fees determined by the PBOC for the same type of financial services (if applicable); (b) the fees charged by major commercial banks in the PRC for the same type of services during the same period; and (c) the fees charged for the same type of financial services offered by AVIC Finance to any other member of AVIC Group with the same credit rating.

Other major terms : When AVIC Finance provides the Deposit Services and the Settlement Services to the Group, AVIC Finance is obliged to ensure the safety and normal use of the Group's deposits under the funds of the AVIC Finance. If AVIC Finance is unable to repay the Group's deposits due to various reasons, the Company is entitled to terminate the Financial Services Framework Agreement and to offset the same amount of the outstanding loan due to AVIC Finance against the deposit due to the Group from AVIC Finance. In the event that the Group suffers financial loss by reason of the default of AVIC Finance, AVIC Finance shall indemnify the Group the full amount of the loss suffered by the Group and the Group shall be entitled to terminate the Financial Services Framework Agreement. If AVIC Finance is unable to indemnify the Group the full amount of the loss suffered by the Group, upon the Group's request, the shortfall shall be offset by the loans provided by AVIC Finance to the Group.

3.5 Finance Lease and Factoring Framework Agreement

Date : 22 August 2023

Parties : The Company (for itself and on behalf of its subsidiaries)

AVIC Lease (for itself and on behalf of its subsidiaries)

Term : Three years from 1 January 2024 to 31 December 2026

Services : Pursuant to the Finance Lease and Factoring Framework Agreement, AVIC Lease has agreed to provide the Group with the Finance Lease Services by itself and to provide the Group with the AVIC Lease Factoring Services through the AVIC Lease Factoring Subsidiary.

(1) Finance Lease Services

(i) AVIC Lease will provide the Finance Lease Services to the Group by way of direct lease and sale and leaseback, etc. The leased assets include buildings, erections, mechanical equipment and other assets.

(ii) Under the direct lease service, AVIC Lease (as lessor) will purchase from suppliers the leased assets based on the demands and choice of the Company (as lessee) at a price negotiated between the Group and the supplier, and AVIC Lease will then lease the leased assets to the Company for its use in return for periodic lease payments.

(iii) Under the sale and leaseback service, the Company (as lessee) will sell the leased assets to AVIC Lease (as lessor) at a negotiated purchase price with reference to the book value and/or original acquisition costs and/or appraised value of the leased assets, and AVIC Lease will then lease the leased assets back to the Company for its use in return for periodic lease payments.

(iv) During the lease period, the leased assets will be solely owned by AVIC Lease. Subject to the relevant requirements of the Hong Kong Listing Rules, the Company may purchase the leased assets after or (upon the consent of AVIC Lease) prior to the expiry of the lease.

(2) AVIC Lease Factoring Services

Where the Group needs the AVIC Lease Factoring Services, the Group will transfer its outstanding principal amount of the accounts receivable which has not been due, the related interest and other rights as a creditor to the AVIC Lease Factoring Subsidiary, and receive the factoring proceeds.

Pricing principles	:	The lease payment relating to the Finance Lease Services and the fees relating to the AVIC Lease Factoring Services will be determined as follows: AVIC Lease Factoring Subsidiary shall pay the outstanding principal amount of accounts receivable which has not been due as the factoring amount. The factoring interest shall be determined by the parties with reference to factors including the average factoring interest rate charged by AVIC Lease to its customers and the funding costs. AVIC Lease Factoring Subsidiary will charge service fees with respect to AVIC Lease Factoring Services, which shall not be higher than the fees charged by similar financial factoring companies in the PRC for the same type of factoring services.
Payment	:	For the Finance Lease Services, the Company and AVIC Lease will agree on the manner of payment flexibly based on the actual cash flows, including not limited to the payment of principal by equal or unequal instalments on a quarterly basis, payment of principal and interest by equal instalments on a quarterly basis, payment of principal by equal instalments on a semi-annual basis or payment of principal and interest by equal instalments on an annual basis, etc. For the AVIC Lease Factoring Services, the Company and AVIC Lease shall agree on the manner of payment flexibly based on the specific factoring project, including but not limited to payment by the Group or the debtor of the accounts receivable or both.
Separate Contracts	:	AVIC Lease and the Group shall enter into specific contracts to set out the specific terms and conditions (including the specific payment terms) for the provision of services according to the principles and scope provided for under the Finance Lease and Factoring Framework Agreement and the relevant legal requirements.

The contract period of the specific contracts with respect to Finance Lease Services may exceed three years, depending on the type of leased assets involved. Specific contracts with respect to Finance Lease Services and AVIC Lease Factoring Services duly executed shall remain to have full force and effect for their respective contract periods and shall be subject to the Finance Lease and Factoring Framework Agreement for the three years from 1 January 2024 to 31 December 2026.

3.6 Supplemental Financial Services Framework Agreement

Date	:	22 August 2023
Parties	:	The Company AVIC Finance
Subject Matter	:	AVIC Finance has agreed to provide the Group with the AVIC Finance Factoring Services with a maximum daily outstanding factoring financing balance of AVIC Finance Factoring Services (including factoring prepayment, factoring fee and factoring handling charges) shall not exceed RMB2,500 million. Save as the Proposed Revised Cap for the AVIC Finance Factoring Services, all other terms and conditions under the Existing Financial Services Framework Agreement shall remain the same.
Major Terms	:	The Supplemental Financial Services Framework Agreement shall become effective on the date of completion of internal approval procedures by both parties to the agreement in accordance with relevant laws (including the applicable listing rules) and the articles of association of both parties to the agreement and shall end on 31 December 2023.

3.7 Assessment of the terms of Non-Exempt Renewal Agreements and Supplemental Financial Services Framework Agreement

In assessing the fairness and reasonableness of the terms in the Non-Exempt Renewal Agreements and Supplemental Financial Services Framework Agreement, we have obtained and reviewed (i) the Existing Mutual Product Supply Agreement; (ii) the Existing Mutual Service Supply Agreement; (iii) the Existing Mutual Product and Service Supply and Guarantee Agreement; (iv) the Existing Financial Services Framework Agreement; and (v) the Existing Finance Lease and Factoring Framework Agreement (collectively, the "**Existing Non-Exempt Agreements**"). We noted that the major terms in the Non-Exempt Renewal Agreements and Supplemental Financial Services Framework Agreement are similar with those in the Existing Non-Exempt Agreements which were approved by the independent shareholders at the extraordinary general meetings of the Company held on 20 November 2020 and 10 February 2023.

We noted that the price of the products and services under Non-Exempt Renewal Agreements shall be determined with reference to (i) the Government-prescribed Price or the Government-guidance Price; (ii) Market Price and (iii) Contractual Price.

Government-prescribed Price

Government-prescribed Price is the price jointly determined by the relevant price control authorities, the industry regulators in the PRC and the relevant manufacturing enterprises involved in the particular transactions, which mainly comprise the relevant costs plus profit margin. The relevant costs will be proposed by the relevant manufacturing enterprises, and confirmed by the relevant price control authorities and the industry regulators in the PRC. The profit margin shall be determined by the relevant authorities.

We have discussed with the Management and understood that majority of products of the Group are specific aviation products and Government-prescribed Price is usually adopted for specific aviation products of the Group, while such Government-prescribed Price will not be published and is not publicly available. The Government-prescribed Price shall be determined by the relevant authorities according to their internal procedures, requirements and standards, and such Government-prescribed Price shall be applicable to the transactions for specific aviation products in the industry.

Government-guidance Price

Government-guidance Price is the price determined by the parties within the range as provided under the laws, regulations, decisions or orders or in respect of particular types of services promulgated by the central government, provincial government or other regulatory authorities in the PRC.

Market Price

Market Price is the price as determined in the following sequence: (i) where there are comparable market prices or charging rates standards determined by independent third parties under normal commercial terms for the transaction, the transaction price shall be determined at such price or standard (the Company will obtain at least two to three such price or standard from Independent Third Parties); or (ii) if there are no such comparable market prices of independent third parties, the transaction price shall be fixed by the price of non-connected transactions between the Company and independent third parties: (a) where the Company is the buyer, through tender procedures in accordance with the relevant PRC laws and regulations relating to tender and bidding or by choosing the most favorable price among at least two to three selected suppliers after taking into account the suppliers' manufacturing qualifications and delivery time, and business relationship between the Company and suppliers according to the Company's internal procurement policy; or (b) where the Company is the supplier, agreeing with the clients within prescribed price range, which is determined according to the Company's internal sales policy with reference to: (i) the transaction volume and business relationship between the Company and the purchaser; and (ii) the prices of similar products and services purchased from the Company by not less than two Independent Third Parties. The Market Price will be determined or approved by the authorised departments/persons of the specific entities within the Group in particular transactions.

We have discussed with the Management and understood that where the Company is the supplier, the Company will normally participate in the public tender procedures announced by its potential clients and the price offered by the Company will be determined according to its internal sales policy and procedures, which is the same to connected parties and independent third parties. We have reviewed the tender result announcements published on the website of AVIC CAPDI (https://www.avic-apc.com/) and noted that AVIC CAPDI participated and won the bids for 17 projects as a supplier in 2022. We have also reviewed the bidding document prepared by another subsidiary of the Company for provision of certain products in 2022 which followed the tender procedures of the client. Therefore, we consider the Company has followed the internal sales policy in determining the Market Price, where the Company is the supplier.

As advised by the Management, for the Market Price to be determined by tender procedures, the Group strictly follows the relevant PRC laws and regulations in relation to tender procedures, in particular the Law of the People's Republic of China on Tenders and Bids (中華人民共和國招標投標法). The Market Price may also be determined by other means, such as price inquiry and price comparison by fee quotations if tender procedures are not adopted. We have reviewed the Company's internal procurement policy and price administrative measures applied to all suppliers and noted there is the relevant description of tender procedures, price inquiry and price comparison, which is in line with the statements made by the Management. In view of the above, we consider that the Market Price determined by tender procedures or other means is fair and reasonable, on the normal commercial terms and in the interest of the Company and its Shareholders as a whole, and there are adequate procedures in place to ensure the fairness and reasonableness of the transactions conducted under the reference of the Market Price.

Contractual Price

Contractual Price is the price to be agreed between the relevant parties for the supply of the aviation products, raw materials and related services (as the case may be), which shall be the reasonable costs incurred in supplying the same plus not more than 8% of such costs, which is determined after taking into account (i) the average profit margin of approximately 7% among industrial enterprises; (ii) the average profit margin in the aviation industry; and (iii) the profits previously received by the Group or AVIC Group for similar products, raw materials or services. The specified percentage used to determine the Contractual Price is the maximum profit margin under the relevant continuing connected transactions agreements and specific prices will be determined under separate agreements in each transaction, and the profit margin is in line with industry practice. The above Contractual Price mechanism is applicable to not only the supply of products or services by the Group, but also vice versa by AVIC Group.

We have reviewed the industry data released by the National Bureau of Statistics in the PRC and noted that the industrial enterprises above designated size (i.e., with an annual revenue of RMB20 million or above) recorded an average profit margin of approximately 6.1% for FY2022 and 6.8% for FY2021. We noted (i) the Company is mainly engaged in the research and development, manufacture and sales of aviation products, and relevant engineering services, which falls within the scope of industrial enterprises; and (ii) the Group recorded revenue of approximately RMB63,639.43 million for FY2022, which exceeds the threshold of the designated size, and therefore we consider such industry data is a relevant reference for our assessment of the profit margin used to determine the Contractual Price. We have also reviewed the 2021 annual report and 2022 annual report of the Company and noted that the Group recorded stable net profit margin of approximately 8.0% and 7.8% for FY2021 and FY2022, which is higher than the average profit margin of industrial enterprises above designated size. In view of the above and given the Group can charge AVIC and AVIC Airborne on the same basis that AVIC and AVIC Airborne can charge the Group, we consider the Contractual Price is fair and reasonable.

In respect of the Deposit Services under the Financial Services Framework Agreement, we have reviewed the latest interest rates offered by AVIC Finance for different types of deposit and compared the latest interest rates for the same type of deposit announced by major commercial banks of the PRC and the latest benchmark interest rates promulgated by the PBOC for each deposit service. We noted that the interest rate offered by AVIC Finance for each type of deposit is not lower than the latest benchmark interest rates as promulgated by the PBOC for the same type of deposit and the latest listed average interest rates for the same type of deposits offered by major commercial banks of the PRC.

In respect of the AVIC Finance Factoring Services under the Financial Services Framework Agreement, we have discussed with the Management and understood that the third parties or major commercial banks, which are not as familiar as AVIC Finance with the business of the Group to estimate the risk of the Group's account receivables, normally require more strict conditions than AVIC Finance when providing the same factoring services, and hence the Group would prefer to select AVIC Finance as the service provider in such situation. We have also obtained and reviewed a set of quotation for factoring services provided by AVIC Finance and a major commercial bank in the PRC and we noted that the fee charged by AVIC Finance is lower than the fee charged by the major commercial bank in the PRC for the same type of services.

In respect of the Other Financial Services under the Financial Services Framework Agreement, we have discussed with the Management understood that Other Financial Services provided by AVIC Finance to the Group currently are mainly bill acceptance services while major commercial banks in the PRC normally request for deposits in addition to the fee charged for the same type of services, and the Group therefore would prefer to select AVIC Finance as the service provider in such situation. We have obtained and reviewed a set of receipts in relation to the bill acceptance services provided to the same subsidiary of the Company by AVIC Finance and a major commercial bank and we noted that AVIC Finance did not require for a deposit for the same type of service as the major commercial bank requested while charge fees not less favourable than the major commercial bank to the Group.

Based on the above, given that (i) the Government-prescribed Price and Government-guidance Price are determined, or subject to approval, by the relevant price control authorities and the industry regulators in the PRC; (ii) the Market Price is determined with reference to the terms of comparable transactions with independent third parties or by tender procedures in accordance with the relevant PRC laws and regulations or other means; (iii) the Contractual Price will be determined with reference to the historical profit margin of the Group and the average profit margin of industrial enterprises; (iv) interest rates for the Group's deposits with AVIC Finance shall not be lower than the benchmark interest rates during the same period as promulgated by the PBOC for the same type of deposit and the interest rates for the Group's RMB deposits with AVIC Finance shall not be lower than the listed average interest rates for the same type of deposits offered by major commercial banks of the PRC; (v) the fees charged by AVIC Finance for the provision of the AVIC Finance Factoring Services shall not be higher than (a) the average fees charged by AVIC Finance to any third party with the same price determination factors as the Group during the same period (including credit rating, term, business category, enterprise category); and (b) the average fees charged by the major commercial banks in the PRC for the same type of services; (vi) the fees charged by AVIC Finance for the provision of the Other Financial Services shall not be higher than (a) the maximum fees determined by the PBOC for the same type of financial services (if applicable); (b) the fees charged by major commercial banks in the PRC for the same type of services during the same period; and (c) the fees charged for the same type of financial services offered by AVIC Finance to any other member of AVIC Group with the same credit rating; and (vii) the service fees charged by AVIC Lease Factoring Subsidiary with respect to AVIC Lease Factoring Services shall not be higher than the fees charged by similar financial factoring companies in the PRC for the same type of factoring services, we are of the view that the pricing principles are fair and reasonable, on the normal commercial terms and in the interest of the Company and its Shareholders as a whole.

Having considered (i) the principal business of the Group; (ii) the background of the Share Swap and Absorption; (iii) our assessment on the pricing principles; and (iv) the analysis performed on the Non-Exempt Annual Caps in the section headed "4.3 Assessment to the Non-Exempt Annual Caps" of this letter, we are of the view that the terms of the Non-Exempt Transactions are fair and reasonable, on the normal commercial terms and in the interest of the Company and its Shareholders as a whole.

4. Non-Exempt Annual Caps

4.1 Historical amounts, Non-Exempt Annual Cap

The following table sets forth the historical amounts, the Proposed Revised Cap for the AVIC Finance Factoring Services for the year ending 31 December 2023 (the "**FY2023**") and the Non-Exempt Annual Caps (except for the Proposed Revised Cap for the AVIC Finance Factoring Services) for each of the year ending 31 December 2024, 2025 and 2026 (the "**FY2024**", "**FY2025**" and "**FY2026**") of the Non-exempt Transactions.

(RMB' million)	Historical amount for FY2021	Historical amount for FY2022	Historical amount for 1H2023	Proposed Revised Cap for FY2023	Proposed caps for FY2024	Proposed caps for FY2025	Proposed caps for FY2026
Expenditure transactions of the Group							
Mutual Product Supply Agreement	10,567	11,471	7,149	–	20,980	24,320	26,000
Mutual Service Supply Agreement	375	414	99	1,200	1,610	1,400	1,500
AVIC Airborne Mutual Product and Service Supply Framework Agreement	671	783	674	–	2,800	3,000	3,100
Revenue transactions of the Group							
Mutual Product Supply Agreement	15,674	18,152	13,741	–	43,350	45,220	51,760
Mutual Service Supply Agreement	2,605	2,644	1,180	–	5,600	5,000	5,300
Transactions under the Financial Services Framework Agreement							
Maximum daily outstanding balance of deposits (including accrued interests) for deposit services	19,100	24,432	16,220	–	45,000	45,000	45,000
Maximum daily outstanding factoring financing balance (including factoring prepayment, factoring fee and factoring handling charges) of AVIC Finance Factoring Services	355	1,050	725	2,500	5,000	5,000	5,000
Other Financial Services	37	47	72	–	3,000	3,000	3,000
Transactions under the Finance Lease and Factoring Framework Agreement							
Maximum daily outstanding factoring financing balance (including factoring prepayment, factoring fee and factoring handling charges) of AVIC Lease Factoring Services	30	25	5	–	1,000	1,000	1,000

4.2 *Basis of determining the Non-Exempt Annual Caps*

(1) Mutual Product Supply Agreement

Under the Mutual Product Supply Agreement, the Group primarily provides the aviation entire aircraft and avionics products to AVIC Group, and AVIC Group primarily provides the relevant parts and components to the Group which are necessary for the manufacturing of the aforesaid aviation entire aircraft and avionics products.

The proposed caps for the revenue transactions for the three years ending 31 December 2026 are determined with reference to, among other things, the following factors:

(i) historical transaction amount and expected growth

The proposed caps for the three years ending 31 December 2026 are determined after taking into account (i) the historical transaction amount of approximately RMB15,674 million and RMB18,152 million respectively for the year ended 31

December 2021 and 31 December 2022; (ii) the expected sales volume of products of the Group, in particular, the expected additional sales volume of electromechanical products as a result of the Share Swap and Absorption for the year ending 31 December 2023, and the Company has revised and increased the proposed annual cap for the revenue transactions under the Existing Mutual Product Supply Agreement for the year ending 31 December 2023 to RMB34,516 million (for details please refer to the Company's circular dated 16 January 2023); and (iii) the expected growth of relevant business in 2024 based on the current operation plan which is expected to lead to significant increase of sales volume of aviation products, and after taking into account the orders from AVIC Group and the commercial negotiations ongoing with AVIC Group in relation to potential orders.

(ii) adequate buffer for potential demands of AVIC Group

The Company also sets a 5% to 10% buffer for the proposed caps to cover the potential product demands of AVIC Group. The 5% to 10% buffer is added based on the development in national economy and aviation industry, the research, development and manufacturing of the Group's possible new products, and the potential business development and expansion of the Group in the future.

The proposed caps for the expenditure transactions for the three years ending 31 December 2026 are determined with reference to, among other things, the following factors:

(i) expected growth in demand of the Group

The Group will purchase relevant parts and components from AVIC Group for the manufacturing of the aviation entire aircraft and avionics products. The proposed caps for the three years ending 31 December 2026 are determined after taking into account (i) the historical transaction amount of approximately RMB10,567 million and RMB11,471 million respectively for the year ended 31 December 2021 and 31 December 2022; (ii) the expected increase in procurement of parts and components according to the production plan and the expected additional purchase costs for the production of electromechanical products as a result of the Share Swap and Absorption for the year ending 31 December 2023, and the Company has revised and increased the proposed annual cap for the expenditure transactions under the Existing Mutual Product Supply Agreement for the year ending 31 December 2023 to RMB23,640 million (for details please refer to the Company's circular dated 16 January 2023). As the procurement of products has become more stable, the expenditure transactions for 2024 is expected to be lower than in the annual cap for the year 2023. The annual growth rate of the expenditure transactions for each of 2025 to 2026 is expected to be 16% and 7%, respectively.

(ii) adequate buffer for potential demands of the Group

The Company also sets a 5% to 10% buffer for the proposed caps to cover the potential product demands of the Group. The 5% to 10% buffer is added based on the development in national economy and aviation industry, the research, development and manufacturing of the Group's possible new products, and the potential business development and expansion of the Group in the future.

(2) *Mutual Service Supply Agreement*

The proposed caps for the revenue transactions for the three years ending 31 December 2026 are determined with reference to, among other things, the following factors:

(i) provision of aviation engineering services to AVIC Group

Under the Mutual Service Supply Agreement, the Group mainly provides aviation engineering services to AVIC Group through AVIC CAPDI. The proposed caps for the three years ending 31 December 2026 are determined after taking into account the steady annual growth of the aviation engineering industry. It is expected that the revenue of aviation engineering services of the Group will grow at an annual rate of around 6% from 2024 to 2026 taking into account the compound annual growth rate of around 7% in the past three years.

(ii) Provision of labour services and other services to AVIC Group

The Group expects that the revenue from labour services due to the Share Swap and Absorption will increase by around RMB270 million for the year ending 31 December 2024. Besides, based on the signed contracts, orders and the Group's manufacturing plan and business development, the expected revenue from manufacturing-related labour services for aviation entire aircraft business is approximately RMB1,300 million for the year ending 31 December 2024.

As the Group expects a decrease in provision of labour services to AVIC Group in 2025 and 2026 under the signed contracts, orders and the Group's manufacturing plan, hence there is a slight decrease in the proposed annual caps for the year ending 31 December 2025 and 31 December 2026 as compared to the proposed annual cap for the year ending 31 December 2024.

The Group did not have a high utilisation rate for the annual caps for revenue transactions under the Existing Mutual Service Supply Agreement for the years ended 31 December 2021 and 31 December 2022 mainly due to the decrease in contracts and orders as affected by the market and the revenue growth of the engineering services provided by the Group was lower than expected at the time when setting the original caps in the Existing Mutual Service Supply Agreement.

(iii) adequate buffer for potential demands of AVIC Group

The Company also sets a 5% to 10% buffer for the proposed caps to cover the potential services demands of AVIC Group. The 5% to 10% buffer is added based on the development in national economy and aviation industry (based on the expected growth of around 5% in the 2023 gross domestic product in the PRC and the growth rate in revenue of aviation industry was around 7% in 2022), and the potential business development and expansion of AVIC Group in the future.

The proposed caps for the three years ending 31 December 2026 for the expenditure transactions are determined with reference to, among other things, the following factors:

(i) provision of labour services by AVIC Group

AVIC Group mainly provides labour services such as corresponding outsourcing and comprehensive services to the Group. For the year ending 31 December 2024, the Group expects to incur additional labour expenditure of approximately RMB240 million due to the Share Swap and Absorption. Along with the business development and increase of the Group's sales volume, the labour expenditures (such as outsourcing labour services) are expected to increase substantially in 2024 as compared to 2023. However, as the Group expects a decrease in its demand for certain types of labour services from AVIC Group in 2025 and 2026 based on the signed contracts, orders and the Group's manufacturing plan, hence the Group expects a decrease in the proposed annual caps for the year ending 31 December 2025 and 31 December 2026 as compared to the proposed annual cap for the year ending 31 December 2024. When determining the proposed annual caps for 2024 to 2026, the Group also took into account the historical and expected growth rates in labour wages.

The Group did not have a high utilisation rate for the annual caps for expenditure transactions under the Existing Mutual Service Supply Agreement for the years ended 31 December 2021 and 31 December 2022 mainly because the sales of certain aircraft models did not experience growth as expected when determining the original annual caps in the Existing Mutual Service Supply Agreement, thereby resulting in a cut down of the corresponding labour expenditure.

(ii) adequate buffer for potential demands of the Group

The Company also sets a 5% to 10% buffer for the proposed caps to cover the potential services demands of the Group. The 5% to 10% buffer is added based on the development in national economy and aviation industry (based on the expected growth of around 5% in the 2023 gross domestic product in the PRC and the growth rate in revenue of AVIC Group was around 7% in 2022) and the potential business development and expansion of the Group in the future, as well as the historical growth rate in the Group's operating revenue of approximately 5.5% for the year ended 31 December 2022 as compared to that of the year ended 31 December 2021.

(3) AVIC Airborne Mutual Product and Service Supply Framework Agreement

The proposed caps for the three years ending 31 December 2026 for the expenditure transactions are determined with reference to, among other things, the following factors:

(i) intragroup transactions of the Group

The transactions under the AVIC Airborne Mutual Product and Service Supply Framework Agreement are intragroup transactions of the Group, and are mostly product pairing transactions between the AVIC Airborne Group (mainly the avionic products and electromechanical products) and the Group's entire aircraft companies (mainly the helicopters and trainers). Avionics products and electromechanical products are necessary aviation parts and components for the manufacturing of the aviation entire aircraft. AVIC Airborne Group is the major supplier for the related avionics products and electromechanical products in the Group's helicopters and trainers.

Therefore, when determining the proposed caps for the transactions contemplated under the AVIC Airborne Mutual Product and Service Supply Framework Agreement, the Company has also taken into account the growth rates of the revenue transactions of AVIC Airborne Group under the Mutual Product Supply Agreement.

(ii) historical transaction amount and annual growth trend

Under the Existing Mutual Product and Service Supply and Guarantee Agreement, the expenditure transactions amount for the year ended 31 December 2022 has increased by approximately 17% when compared to that of 31 December 2021. Along with the growth in production and sales of the Group's aviation entire aircraft products, the Group has a corresponding higher demand for purchase of avionics products, which is expected to have a substantial increase for the year ending 31 December 2024 when compared to that for the year ended 31 December 2022, and an expected growth rate of approximately 7% to 9% between 2025 and 2026. Further, upon completion of the Share Swap and Absorption, it is expected that the Group will incur additional purchase costs for electromechanical products as a result. The Company has revised and increased the proposed annual caps for the expenditure transactions under the Existing Mutual Product and Service Supply and Guarantee Agreement for the year ending 31 December 2023 (for details please refer to the Company's circular dated 16 January 2023). It is expected that the additional purchase costs for electromechanical products for 2024 to 2026 would be around RMB1,400 million in total.

(iii) adequate buffer for potential demands of the Group

The Company also sets a 10% buffer for the proposed caps to cover the potential demands of the Group for the relevant products and services. The 10% buffer is added based on the development in national economy and aviation industry (based on the expected growth of around 5% in the 2023 gross domestic product in the PRC and the growth rate in revenue of AVIC Group was around 7% in 2022), the potential business development and expansion of the Group in the future, as well as the historical growth rate in the Group's operating revenue of approximately 5.5% for the year ended 31 December 2022 as compared to that of the year ended 31 December 2021.

(4) Financial Services Framework Agreement

Deposit Services

The proposed cap for the Deposit Services under the Financial Services Framework Agreement is the same as the annual cap under the Existing Financial Services Framework Agreement, which is determined with reference to, among other things, the following factors: (i) the maximum daily outstanding balance of deposits (including accrued interests) of approximately RMB19,100 million, RMB24,432 million and RMB16,220 million placed by the Group in AVIC Finance in the year ended 31 December 2021 and 2022 and the six months ended 30 June 2023; (ii) the cash and bank balances of the Group of approximately RMB30,378 million as at 30 June 2023; (iii) the expected payments as may be made by major customers in the aviation entire aircraft business segment and the expected payment schedule for the products provided by the Group during the relevant period; (iv) the expected growth in the business of the Group, leading to an increasing demand for the Deposit Services with higher level of funds; and (v) the fund management strategy of the Group of allocating a certain percentage of funds to AVIC Finance for more efficient use of funds available.

Besides, the proposed cap for the Deposit Services under the Financial Services Framework Agreement has also taken into account the increase in the number of subsidiaries of the Company after completion of the Share Swap and Absorption. Prior to completion of the Share Swap and Absorption, AVIC Electromechanical was listed on the Shenzhen Stock Exchange (stock code: 002013.SZ) and its market capitalization immediately prior to completion of the Share Swap and Absorption was approximately RMB41,632.36 million, and it had more than 20 subsidiaries. The consolidated total assets of the AVIC Electromechanical Group as at 31 December 2020 and 31 December 2021 amounted to approximately RMB30,247.22 million and RMB34,893.66 million respectively. The consolidated revenue of the AVIC Electromechanical Group for the year ended 31 December 2020 and 31 December 2021 was approximately RMB12,224.10 million and RMB14,992.20 million respectively. After completion of the Share Swap and Absorption, the expected demand for the Deposit Services of the Group will increase considering the increase in the number of subsidiaries of the Company.

AVIC Finance Factoring Services

The proposed caps for the AVIC Finance Factoring Services are determined with reference to, among other things, the following factors: (i) the historical maximum daily outstanding factoring financing balance of the AVIC Finance Factoring Services for the year ended 31 December 2021 and 31 December 2022 and the six months ended 30 June 2023 respectively; (ii) the increase in the number of subsidiaries of the Company after completion of the Share Swap and Absorption as well as the expected demand of the Group for accounts receivable financing services from AVIC Finance after taking into account the forecast in the Group's business for 2024 to 2026 which considers the expected growth in the Group's revenue and accounts receivables; (iii) the total accounts receivable of the Group in the latest financial statements; and (iv) the Group may increase its demand for AVIC Finance Factoring Services towards the end of the year for the investment needs for the next financial year and the need to maintain certain level of working capital.

Other Financial Services

The proposed caps for the Other Financial Services under the Financial Services Framework Agreement are determined with reference to, among other things, the following factors: (i) the historical transaction amount of Other Financial Service received by the Group for the year ended 31 December 2021 and 31 December 2022 and the six months ended 30 June 2023; (ii) the expected increase in demand for Other Financial Services due to an increase in subsidiaries of the Company after completion of the Share Swap and Absorption, and each subsidiary with its own business needs and financial demands; (iii) in accordance with the 14^{th} Five-Year Plan, certain subsidiaries of the Company have been enhancing its research and development input for new airplane models, which may affect the short-term liquidity of the Group in 2024 to 2026, thereby increasing the Group's demand in using bill acceptance and discount services to raise funds and for greater efficiency and flexibility in utilising the financing methods for additional funds; (iv) towards the end of the year, the Group has the need to maintain certain level of working capital, therefore, the Group may use more bill acceptance and discount services for greater efficiency in the use of funds; and (v) as disclosed in the 2022 annual report of the Company, as at 31 December 2022, the Group's notes payable amounted to approximately RMB10,417.3 million (comprising banker's acceptance bill of approximately RMB5,381.7 million and commercial acceptance bill of RMB5,035.6 million), the Group expects to increase its use of bill acceptance and discount services provided by AVIC Finance instead of other commercial banks in 2024 to 2026 when settling payment taking into account the advantages of engaging services provided by AVIC Finance as compared to other commercial banks as set out in section 5.3(b) of the Letter from the Board. The Company considers that it will not over-rely on the bill acceptance and discount services provided by AVIC Finance because the Company has adopted certain internal control mechanism to ensure the implementation of pricing policies in the continuing connected transactions agreements of the Group (as set out in section IV of the Letter from the Board).

The Group did not have a high utilisation rate for the annual caps for Other Financial Services for the years ended 31 December 2021 and 31 December 2022 because the Group did not utilise bill acceptance and discount services or other financial services of AVIC Finance as originally planned after considering its cash flow status and financing needs during such period.

(5) *Financial Lease and Factoring Framework Agreement*

AVIC Lease Factoring Services under the Finance Lease and Factoring Framework Agreement

The proposed caps for the AVIC Lease Factoring Services under the Finance Lease and Factoring Framework Agreement are determined with reference to, among other things, the following factors: (i) the expected demand of the Group for accounts receivable financing services from AVIC Lease after taking into account the forecast in the Group's business for 2024 to 2026 which considers (a) the expected growth in the Group's revenue and accounts receivables, and (b) the long settlement cycle of main aircraft body manufacturing business which may create pressure on the Group's liquidity; (ii) the total accounts receivable of the Group in the latest financial statements and the historical trend of the level of accounts receivable in the Group's financial statements; and (iii) the Group may increase its demand for AVIC Lease Factoring Services towards the end of the year (a) due to the enhancement in research and development input for new airplane models of certain subsidiaries of the Company in line with the 14th Five-Year Plan which may affect the short term liquidity of the Group, (b) for the investment needs for the next financial year (which are estimated based on the potential orders, signed contracts, historical investment amount and quantity of fixed assets), and (c) for the need to maintain certain level of working capital.

The Group did not have a high utilisation rate for the annual caps for AVIC Lease Factoring Services for the years ended 31 December 2021 and 31 December 2022 because the Group did not utilise the AVIC Lease Factoring Services as originally planned after considering its cash flow status, its financing needs and the various financing channels during such period.

(6) Supplemental Financial Services Framework Agreement

The Proposed Revised Cap for the AVIC Finance Factoring Services for the year ending 31 December 2023 is determined based on the historical maximum daily outstanding factoring financing balance for the year ended 31 December 2021 and 31 December 2022 and the expected increase in the demand for the AVIC Finance Factoring Services by AVIC Airborne Group after considering (i) the maximum daily outstanding factoring financing balance (including factoring prepayment, factoring fee and factoring handling charges) of the factoring services under the Existing Financial Services Framework Agreement for the year ended 31 December 2022 (i.e. RMB1,050 million) almost reached the original annual cap for the financial year ending 31 December 2023 (i.e. RMB1,200 million); and (ii) upon completion of the Share Swap and Absorption, the number of the Company's subsidiaries has increased, which would lead to an increase in demand for the AVIC Finance Factoring Services by AVIC Airborne Group in the second half of 2023 (being approximately RMB600 million), and it is expected that the original annual cap will be insufficient to satisfy the Group's demand for AVIC Finance Factoring Services for the year ending 31 December 2023. Further, due to the Group's business nature, the Group generates a higher level of revenue and accounts receivables in the second half of the year compared to the first half of the year; coupled with the investment needs for the next financial year and the needs of the Group to maintain certain level of working capital towards the end of the year, the Group would have a higher demand for AVIC Finance Factoring Services in late 2023.

4.3 Assessment to the Non-Exempt Annual Caps

In assessing the fairness and reasonableness of the Non-Exempt Annual Caps, we have reviewed the calculation of the Non-Exempt Annual Caps and noted that the Non-Exempt Annual Caps are calculated as the sum of estimated transaction amounts for respective transactions under certain agreements prepared by the relevant subsidiaries of the Group in FY2024, FY2025 and FY2026 with certain buffers. We have discussed with the Management and it is confirmed that the estimated transaction amounts are calculated based on several factors, including but not limited to existing and expected orders, manufacturing plans, expected business growth, expected growth of financial demand and expected growth of account receivables of the Group.

4.3.1 Mutual Product Supply Agreement

In respect of the proposed annual caps for the expenditure transactions of the Group, we have reviewed the historical transaction amounts of expenditure transactions of the Group for FY2021, FY2022 and 1H2023, which represent the utilisation rates of the existing annual caps for the expenditure transactions of approximately 59.1%, 60.9% and 30.2% for the corresponding periods, respectively. We have discussed with the Management and understood that the settlement of the expenditure transactions usually concentrates in the second half of the year and therefore the transaction amount of expenditure transactions in the second half of 2023 is expected to be higher as compared to that for 1H2023. We have obtained and reviewed the 2022 interim connected transactions monitor sheet of the Company and noted that the transaction amount of expenditure transactions of the Group for 1H2022 represented approximately 43.7% of such transaction amount for FY2022. The proposed annual caps for the expenditure transaction for FY2025 and FY2026 represent annual growth rates of approximately 15.9% and 6.9% respectively. As advised by the Management, the increase of the proposed annual cap for the expenditure transaction for FY2024 of approximately 82.9% as compared to the historical expenditure transaction amounts for FY2022 is mainly due to the expected additional purchase cost for the production of electromechanical products as a result of an increase in more than 20 subsidiaries of the Company after completion of the Share Swap and Absorption (the "**Absorbed Subsidiaries**"). We have also obtained and reviewed the estimated transaction amounts for expenditure transactions of such absorbed subsidiaries and noted that (i) the estimated transaction amounts for expenditure transactions of Absorbed Subsidiaries for FY2024 are approximately 10.9% of the proposed annual cap for the expenditure transaction for FY2024; and (ii) the proposed annual cap for the expenditure transaction for FY2024 deducting the estimated transaction amounts for expenditure transactions of Absorbed Subsidiaries for FY2024 represents a compound annual growth rate (the "**CAGR**") of approximately 27.7% as compared to the historical expenditure transaction amounts for FY2022. We further noted that (i) the proposed annual caps for the expenditure transaction for FY2024, FY2025 and FY2026 are in line with the expected transaction amounts with a buffer of 10% as shown in the calculation; (ii) the total operating cost of the Group for FY2022 and 1H2023 increased by approximately 5.53% and 22.04% as compared to that for FY2021 and 1H2022, respectively; and (iii) the annual growth rates of the proposed annual caps for the expenditure transactions for FY2025 and FY2026 are within the range of the growth rates of total operating cost of the Group for FY2022 and 1H2023; and (iv) the CAGR indicated by the proposed annual cap for FY2024 without the impact of the Absorbed Subsidiaries is close to the growth rates of total operating cost of the Group for 1H2023.

In respect of the proposed annual caps for the revenue transactions of the Group, we have reviewed the historical transaction amounts of revenue transactions of the Group for FY2021, FY2022 and 1H2023, which represent the utilisation rates of the existing annual caps for the revenue transactions of approximately 86.1%, 87.8% and 39.8% for the corresponding periods. We have discussed with the Management and understood that the settlement of the revenue transactions usually concentrates in the second half of the year and therefore the transaction amount of revenue transactions in the second half of 2023 is expected to be higher as compared to that for 1H2023. We have obtained and reviewed the 2022 interim connected transactions monitor sheet of the Company and noted that the transaction amount of revenue transactions of the Group for 1H2022 represented approximately 41.3% of such transaction amount for FY2022. The proposed annual caps for the revenue transactions for FY2025 and FY2026 represent annual growth rates of approximately 4.3% and 14.5% respectively. As advised by the Management, the increase of the proposed annual cap for the revenue transaction for FY2024 of approximately 138.8% as compared to the historical revenue transaction amounts for FY2022 is mainly due to the expected addition sales volume of electromechanical products as a result of an increase in Absorbed Subsidiaries. We have also obtained and reviewed the estimated transaction amounts for revenue transactions of such absorbed subsidiaries and noted that (i) the estimated transaction amounts for revenue transactions of Absorbed Subsidiaries for FY2024 are approximately 26.1% of the proposed annual cap for the revenue transaction for FY2024; and (ii) the proposed annual cap for the revenue transaction for FY2024 deducting the estimated transaction amounts for revenue transactions of Absorbed Subsidiaries for FY2024 represents a CAGR of approximately 32.9% as compared to the historical revenue transaction amounts for FY2022. We further noted that (i) the proposed annual caps for the revenue transaction for FY2024, FY2025 and FY2026 are in line with the expected transaction amounts with a buffer of 8% as shown in the calculation; (ii) the revenue of the Group for FY2022 and 1H2023 increased by approximately 5.54% and 21.95% as compared to that for FY2021 and 1H2022, respectively; and (iii) the annual growth rates of the proposed annual caps for the revenue transactions for FY2025 and FY2026 are within the range of the growth rates of revenue for FY2022 and 1H2023.

In view of the above, we consider the proposed annual caps under the Mutual Product Supply Agreement are fair and reasonable are fair and reasonable.

4.3.2 Mutual Service Supply Agreement

In respect of the proposed annual caps for the expenditure transactions of the Group, we have reviewed the historical transaction amounts of expenditure transactions of the Group for FY2021, FY2022 and 1H2023, which represent the utilisation rates of the existing annual caps for the expenditure transaction of approximately 48.7%, 49.3% and 10.6% for the corresponding periods. We noted that the historical utilisation rate of the existing cap for 1H2023 is relatively low. We have discussed with the Management in this regard and understood that the settlement of the expenditure transactions usually concentrates in the second half of the year and therefore the transaction amount of expenditure transactions in the second half of 2023 is expected to be higher as compared to that for 1H2023. We have obtained and reviewed the 2022 interim connected transactions monitor sheet of the Company and noted that the transaction amount of expenditure transactions of the Group for 1H2022 represented approximately 25.7% of such transaction amount for FY2022. The proposed annual caps for the expenditure transaction for FY2025 and FY2026 represent a reduction rate of approximately 13.0% and a growth rate of approximately 7.1% respectively. As disclosed in the Letter from the Board, the existing annual cap for expenditure transaction for FY2023 is proposed to revise to RMB1,200 million considering the expected increase of the Group's purchase amount as a result of the Share Swap and Absorption. As advised by the Management, the increase of the proposed annual cap for the expenditure transactions for FY2024 of approximately 34.17% as compared to the proposed revised cap for expenditure transactions for FY2023 is mainly due to the expected increase of labour expenditures of the Group of approximately 25%, which is mainly contributed by the expected increase of labour procurement plan for the aviation entire aircraft business of the Group. We further noted that (i) the proposed annual caps for the expenditure transaction for FY2024, FY2025 and FY2026 are in line with the expected transaction amounts with a buffer of 10% as shown in the calculation; (ii) the total operating costs of the Group for FY2022 and 1H2023 increased by approximately 5.53% and 22.04% as compared to that for FY2021 and 1H2022, respectively; and (iii) the annual growth rate of the proposed annual caps for the expenditure transaction for FY2026 are within the range of the growth rates of total operating costs for FY2022 and 1H2023.

In respect of the proposed annual caps for the revenue transactions, we have reviewed the historical transaction amounts of revenue transactions of the Group for FY2021, FY2022 and 1H2023, which represent the utilisation rates of the existing annual caps for the revenue transaction of approximately 52.9%, 46.9% and 17.4% for the corresponding periods. We noted that the historical utilisation rate of the existing cap for 1H2023 is relatively low. We have discussed with the Management in this regard and understood that the settlement of the revenue transactions usually concentrates in the second half of the year and therefore the transaction amount of revenue transactions in the second half of 2023 is expected to be higher as compared to that for 1H2023. We have obtained and reviewed the 2022 interim connected transactions monitor sheet of the Company and noted that the transaction amount of revenue transactions of the Group for 1H2022 represented approximately 38.4% of such transaction amount for FY2022. The proposed annual caps for the revenue transactions for FY2025 and FY2026 represent a reduction rate of approximately 10.7% and a growth rate of 6.0% respectively. As advised by the Management, the increase of the proposed annual cap for the revenue transaction for FY2024 of approximately 111.8% as compared to the historical revenue transaction amounts for FY2022 is mainly due to the expected additional supply of aviation engineering services and labour services as a result of the business development of the Group. We further noted that (i) the proposed annual caps for the revenue transaction for FY2024, FY2025 and FY2026 are in line with the expected transaction amounts with a buffer of 8% as shown in the calculation; (ii) the revenue of the Group for FY2022 and 1H2023 increased by approximately 5.54% and 21.95% as compared to that for FY2021 and 1H2022, respectively; and (iii) the annual growth rate of the proposed annual caps for the revenue transactions for FY2026 are within the range of the growth rates of revenue for FY2022 and 1H2023.

In view of the above, we consider the proposed annual caps under the Mutual Service Supply Agreement are fair and reasonable are fair and reasonable.

4.3.3 AVIC Airborne Mutual Product and Service Supply Framework Agreement

In respect of the proposed annual caps for the expenditure transactions of the Group, we have reviewed the historical transaction amounts of expenditure transactions of the Group for FY2021, FY2022 and 1H2023, which represent the utilisation rates of the existing annual caps for the expenditure transaction of approximately 54.6%, 52.6% and 17.6% for the corresponding periods. We noted that the historical utilisation rate of the existing cap for 1H2023 is relatively low. We have discussed with the Management in this regard and understood that the settlement of the expenditure transactions usually concentrates in the second half of the year and therefore the transaction amount of expenditure transactions in the second half of 2023 is expected to be higher as compared to that for 1H2023. We have obtained and reviewed the 2022 interim connected transactions monitor sheet of the Company and noted that the transaction amount of expenditure transactions of the Group for 1H2022 represented approximately 38.4% of such transaction amount for FY2022. The proposed annual caps for the expenditure transactions for FY2025 and FY2026 represent annual growth rates of approximately 7.1% and 3.3%, respectively. As advised by the Management, increase of the proposed annual cap for the expenditure transaction for FY2024 of approximately 257.6% as compared to the historical expenditure transactions for FY2022 are mainly due to the expected additional purchase cost for electromechanical products as a result of an increase in Absorbed Subsidiaries. We have also obtained and reviewed the estimated transaction amounts for expenditure transactions of such absorbed subsidiaries and noted that (i) the estimated transaction amounts for expenditure transactions of Absorbed Subsidiaries for FY2024 are approximately 48.3% of the proposed annual cap for the expenditure transaction for FY2024; and (ii) the proposed annual cap for the expenditure transaction for FY2024 deducting the estimated transaction amounts for expenditure transactions of Absorbed Subsidiaries for FY2024 represents a CAGR of approximately 36.0% as compared to the historical expenditure transaction amounts for FY2022. We further noted that (i) the proposed annual caps for the expenditure transaction for FY2024, FY2025 and FY2026 are in line with the expected transaction amounts with a buffer of 10% as shown in the calculation; (ii) the revenue of AVIC Airborne for FY2022 and 1H2023 increased by approximately 13.69% and 2.75% as compared to that for FY2021 and 1H2022, respectively; and (iii) the annual growth rates of the proposed annual caps for the expenditure transactions for FY2025 and FY2026 are within the range of the growth rates of the revenue of AVIC Airborne for FY2022 and 1H2023.

In view of the above, we consider the proposed annual caps for expenditure transactions of the Group under the AVIC Airborne Mutual Product and Service Supply Framework Agreement are fair and reasonable are fair and reasonable.

4.3.4 Financial Services Framework Agreement

In respect of the proposed annual caps for the Deposit Services, we have reviewed the historical maximum daily outstanding balance of deposits (including accrued interests) of the Group for FY2021, FY2022 and 1H2023, which represent the utilisation rates of the existing annual caps for the Deposit Services of approximately 54.6%, 69.8% and 36.0% for the corresponding periods. The proposed annual caps for the Deposit Services for FY2024, FY2025 and FY2026 will remain the same as the existing annual cap for the Deposit Services FY2023. As advised by the Management, the monetary funds held by the Group are subject to seasonal factors and are normally higher at the end of the year. We further noted that (i) the proposed annual caps for the Deposit Services for FY2024, FY2025 and FY2026 are in line with the expected maximum daily outstanding balance of deposits with certain buffer as shown in the calculation; (ii) the restated monetary funds of the Group reached RMB43,773.73 million as at 31 December 2022, which is close to the proposed annual caps for the Deposit Services for FY2024, FY2025 and FY2026; and (iii) the revenue of the Group for FY2022 and 1H2023 increased by approximately 5.54% and 21.95% as compared to that for FY2021 and 1H2022, respectively.

In respect of the proposed annual caps for the AVIC Finance Factoring Services, we have reviewed the historical maximum daily outstanding factoring financing balance of the AVIC Finance Factoring Services for FY2021, FY2022 and 1H2023, which represent the utilisation rates of the existing annual caps for the AVIC Finance Factoring Services of approximately 29.6%, 87.5% and 60.4% for the corresponding periods. As disclosed in the Letter from the Board, the existing annual cap for AVIC Finance Factoring Services for FY2023 is proposed to revise to RMB2,500 million considering the expected increase of the Group's demand for the AVIC Finance Factoring Services due to the increased number of the Company's subsidiaries upon completion of the Share Swap and Absorption. The proposed annual caps for the AVIC Finance Factoring Services for FY2024, FY2025 and FY2026 will further increase by 100.0% to RMB5,000 million as compared to the proposed revised cap for the AVIC Finance Factoring Services for FY2023. We noted that the proposed annual caps represent a substantial increase as compared to the historical maximum daily outstanding factoring financing balance of the AVIC Finance Factoring Services for 1H2023. We have discussed with the Management in this regard and understood that (i) the settlement of the transactions in relation to AVIC Finance Factoring Services usually concentrates in the fourth quarter of the year and therefore maximum daily outstanding factoring financing balance of the AVIC Finance Factoring Services for the second half of 2023 is expected to be higher as compared to that for 1H2023; and (ii) the Group may increase its demand for AVIC Finance Factoring Services towards the end of the year for the potential investment and working capital needs of the Group. We have obtained and reviewed the 2022 interim connected transactions monitor sheet of the Company and noted that maximum daily outstanding factoring financing balance of the AVIC Finance Factoring Services for 1H2022 represented approximately 11.6% of such maximum daily outstanding factoring financing balance for FY2022. The proposed annual caps for the AVIC Finance Factoring Services are calculated with reference to the expected demand of the Group for accounts receivable financing services from AVIC Finance and the expected growth of the accounts receivables of the Group for

FY2024 to FY2026. We further noted that (i) the proposed annual caps for the AVIC Finance Factoring Services for FY2024, FY2025 and FY2026 are in line with the expected maximum daily outstanding factoring financing balance with certain buffer as shown in the calculation; (ii) the accounts receivables of the Group reached RMB42,783.41 million as at 30 June 2023, representing an increase of approximately 39.81% as compared to that as at 31 December 2022; and (iii) the proposed annual caps of RMB5,000 million are approximately 11.7% of the accounts receivables of the Group as at 30 June 2023.

In respect of the proposed annual caps for the Other Financial Services, we have discussed with the Management and noted (i) the proposed annual caps for the Other Financial Services for FY2024, FY2025 and FY2026 will increase by 250.0% to RMB3,000 million as compared to that for FY2023; (ii) the proposed annual caps for the Other Financial Services for FY2024, FY2025 and FY2026 are in line with the expected transaction amounts with certain buffer as shown in the calculation; (iii) the proposed annual caps for the Other Financial Services for FY2024, FY2025 and FY2026 of RMB3,000 million are approximately 7.4%, 33.3% and 46.2% of the account payables, notes payables and notes receivables of the Group of RMB40,497.52 million, RMB8,999.36 million and RMB6,489.51 million as at 30 June 2023, respectively. We noted that the proposed annual caps represent a substantial increase as compared to the historical transaction amount for 1H2023. We have discussed with the Management in this regard and understood that (i) the settlement of the transactions in relation to the Other Financial Services usually concentrates in the fourth quarter of the year and therefore the transaction amount for the second half of 2023 is expected to be higher as compared to that for 1H2023; (ii) the Group may increase its demand for Other Financial Services towards the end of the year for the potential investment and working capital needs of the Group; and (iii) the enhancing of the research and development input in certain subsidiaries of the Company may affect the short-term liquidity of the Group in 2024 to 2026, thereby increasing the Group's demand in utilising Other Financial Services. We have obtained and reviewed the 2022 interim connected transactions monitor sheet of the Company and noted that the transaction amount of the Other Financial Services for 1H2022 represented approximately 10.7% of such transaction amount for FY2022. We have also noted from the 2022 annual report of the Company that the research and development expenses of the Company increased by approximately 28.7% to approximately RMB4,442.5 million for FY2022 as compared to that for FY2021.

In view of the above, we consider the proposed annual caps under the Financial Services Framework Agreement are fair and reasonable are fair and reasonable.

4.3.5 Finance Lease and Factoring Framework Agreement

In respect of the proposed annual caps for the AVIC Lease Factoring Services, we have discussed with the Management and noted that the proposed annual caps for the AVIC Lease Factoring Services are calculated with reference to the expected demand of the Group for accounts receivable financing services from AVIC Lease and the expected growth of the accounts receivables of the Group for FY2024 to FY2026. We noted that the proposed annual caps represent a substantial increase as compared to the historical maximum daily outstanding factoring financing balance of AVIC Lease Factoring Services for 1H2023. We have discussed with the Management in this regard and understood that (i) the settlement of the transactions in relation to the AVIC Lease Factoring Services usually concentrates in the fourth quarter of the year and therefore the maximum daily outstanding factoring financing balance of AVIC Lease Factoring Services for the second half of 2023 is expected to be higher as compared to that for 1H2023; and (ii) the Group may increase its demand for AVIC Lease Factoring Services towards the end of the year (a) due to the enhancement in research and development input for new airplane models of certain subsidiaries of the Company in line with the 14^{th} Five-Year Plan which may affect the short term liquidity of the Group; (b) for the investment needs for the next financial year (which are estimated based on the potential orders, signed contracts, historical investment amount and quantity of fixed assets); and (c) for the need to maintain certain level of working capital. We have obtained and reviewed the 2022 interim connected transactions monitor sheet of the Company and noted that the Company has not recorded any transaction amount of the AVIC Lease Factoring Services for 1H2022 while the historical maximum daily outstanding factoring financing balance of AVIC Lease Factoring Services for FY2022 was approximately RMB25 million. We have also noted from the 2022 annual report of the Company that the research and development expenses of the Company increased by approximately 28.7% to approximately RMB4,442.5 million for FY2022 as compared to that for FY2021. The proposed annual caps for the AVIC Lease Factoring Services for FY2024, FY2025 and FY2026 will decrease by 33.3% to RMB1,000 million as compared to the existing annual cap for AVIC Lease Factoring Services for FY2023. We further noted that (i) the proposed annual caps for the AVIC Lease Factoring Services for FY2024, FY2025 and FY2026 are in line with the expected maximum daily outstanding factoring financing balance with certain buffer as shown in the calculation; (ii) the accounts receivables of the Group reached RMB42,783.41 million as at 30 June 2023, representing an increase of approximately 39.81% as compared to that as at 31 December 2022; and (iii) the proposed annual caps of RMB1,000 million are approximately 2.3% of the accounts receivables of the Group as at 30 June 2023.

In view of the above, we consider the proposed annual caps for the AVIC Lease Factoring Services under the Financial Services Framework Agreement are fair and reasonable are fair and reasonable and in the interest of the Company and its Shareholders as a whole.

4.4 Assessment to the Proposed Revised Cap for the AVIC Finance Factoring Services

In assessing the fairness and reasonableness of the Proposed Revised Cap for the AVIC Finance Factoring Services, we have reviewed the historical maximum daily outstanding factoring financing balance (including factoring prepayment, factoring fee and factoring handling charges) of AVIC Finance Factoring Services of the Group for FY2021, FY2022 and 1H2023 and noted that the historical maximum daily outstanding factoring financing balance for FY2022 have increased by approximately 195.8% as compared with that for FY2021 and the utilisation rate of the existing annual caps of AVIC Finance Factoring Services for FY2022 and FY2023 reached 87.5% and 60.4%, respectively. We noted that the Proposed Revised Cap represents a substantial increase as compared to the historical maximum daily outstanding factoring financing balance of the AVIC Finance Factoring Services for 1H2023. We have discussed with the Management in this regard and understood that (i) the settlement of the transactions in relation to AVIC Finance Factoring Services usually concentrates in the fourth quarter of the year and therefore the maximum daily outstanding factoring financing balance of AVIC Finance Factoring Services for the second half of 2023 is expected to be higher as compared to that for 1H2023; and (ii) the Group may increase its demand for AVIC Finance Factoring Services towards the end of the year for the potential investment and working capital needs of the Group. We have obtained and reviewed the 2022 interim connected transactions monitor sheet of the Company and noted that maximum daily outstanding factoring financing balance of the AVIC Finance Factoring Services for 1H2022 represented approximately 11.6% of such balance for FY2022.

We have also reviewed the calculation of the Proposed Revised Cap for the AVIC Finance Factoring Services and understood that such cap is the sum of estimated transaction amounts prepared by the relevant subsidiaries of the Group in FY2023 with certain buffer. We have discussed with the Management and it is confirmed that the increase of estimated transaction amounts of AVIC Finance Factoring Services in FY2023 is mainly due to increase of demand for AVIC Finance Factoring Services caused by the increasing number of subsidiaries of the Group as a result of the Share Swap and Absorption. We further noted that (i) the accounts receivables of the Group reached RMB42,783.41 million as at 30 June 2023, representing an increase of approximately 39.81% as compared to that as at 31 December 2022; and (ii) the proposed annual cap of RMB2,500 million is approximately 5.8% of the accounts receivables of the Group as at 30 June 2023.

In view of the above, we consider the Proposed Revised Cap for the AVIC Finance Factoring Services is fair and reasonable and in the interest of the Company and its Shareholders as a whole.

4.5 Assessment to the Finance Lease Term

In assessing the reasons for the Finance Lease Term which requires a longer period than three years, we have taken into consideration the information set out in the Circular and the following principal factors based on the information provided by, and discussion with, the Management:

(i) The Group used to lease aviation related equipment from AVIC Lease under finance lease arrangement. The term of such finance lease transaction was determined with reference to the use life of the equipment (usually ranging from 10 years to 15 years).

(ii) The relevant aviation related equipment is used for manufacturing entire aircraft, avionics products and electromechanical products and is usually expensive to purchase. A longer term of such finance lease of specific aviation related assets is beneficial to the Group to optimise its capital structure and manage its liquidities throughout the expected term of the relevant finance leases without incurring material capital risk or changing the right of use and ultimate ownership of the leased assets.

We have also reviewed the finance lease transactions announced by companies in the aviation industry listed on the Hong Kong Stock Exchange during the one-year period (i.e. 22 August 2022 to 22 August 2023) prior to the date of the Finance Lease and Factoring Framework

Agreement (the "**Comparable Finance Leases**"), which represent the recent market practice in relation to aviation related assets. On best effort basis, we have identified an exhaustive list of three Comparable Finance Leases during such period, the principal terms of which are set out below:

Date of the announcement	**Company name & stock code**	**Leased assets**	**Finance lease term**
28-Aug-22	China Southern Airlines Company Limited (1055.HK)	Aircraft, simulators, aviation related equipment	5 to 10 years
26-Sep-22	China Eastern Airlines Corporation Limited (670.HK)	Aircraft and aircraft engines	May more than 3 years but less than 15 years
20-Sep-22	Air China Limited (753.HK)	Aircraft and engines, simulators, ground support equipment and special vehicles	Mostly more than three years but within the use life of leased assets (over 10 years for aircraft and engines, 3 to 12 years for simulators, ground support equipment and special vehicles)

Based on the above, we consider it is a normal business practice for finance leases in relation to aviation related assets with a term of more than 3 years.

5. **Internal control**

As advised by the Management and set out in the Letter from the Board, the Company will apply an internal control mechanism in respect of the Non-Exempt Transactions and the Non-Exempt Annual Caps, details of which are included in the sections headed "IV. INTERNAL CONTROL MECHANISM".

Pursuant to Rules 14A.55 and 14A.56 of the Hong Kong Listing Rules, the independent non-executive Directors and auditor of the Company will conduct annual review and provide confirmation letter regarding the continuing connected transactions of the Company each year. We have reviewed the annual reports of the Company for FY2021 and FY2022 and noted that the independent non-executive Directors and the auditor of the Company have reviewed the continuing connected transactions during such years and provided the relevant confirmation letter. As confirmed with the Company, the Company will continue to comply with the relevant annual review requirement under the Hong Kong Listing Rules on an on-going basis.

Based on the above, we are of the view that the Group has effective internal policies in place to continue to monitor the Non-Exempt Transactions and the Non-Exempt Annual Caps, therefore the interests of the Company and its Shareholders would be safeguarded.

RECOMMENDATION

Having considered the above factors and reasons, we are of the opinion that (i) the terms of the Non-Exempt Transactions and the Non-Exempt Annual Caps are fair and reasonable; and (ii) the Non-Exempt Transactions are on normal commercial terms, in the ordinary and usual course of business of the Group, and in the interests of the Company and its Shareholders as a whole. Accordingly, we advise the Independent Board Committee to recommend and we also recommend the Independent Shareholders to vote in favour of the resolutions in relation to the Non-Exempt Transactions and the Non-Exempt Annual Caps to be proposed at the EGM.

Yours faithfully
For and on behalf of
Maxa Capital Limited

Dian Deng
Managing Director

Ms. Dian Deng is a licensed person registered with the Securities and Futures Commission of Hong Kong and a responsible officer of Maxa Capital to carry out type 6 (advising on corporate finance) regulated activities under the SFO and has over 15 years of experience in corporate finance industry.