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**PARKSON RETAIL GROUP LIMITED**

*(a company incorporated in the Cayman Islands with limited liability)*

**(Stock Code: 3368)**

**DISCLOSEABLE AND CONNECTED TRANSACTION  
PRELIMINARY FRAMEWORK AGREEMENT  
IN CONNECTION WITH THE POSSIBLE ACQUISITION  
OF 44% OF BEIJING PARKSON**

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



**SOMERLEY LIMITED**

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A letter from the Independent Board Committee is set out on page 22 of this circular. A letter from Somerley Limited, the independent financial adviser, containing its advice to the Independent Board Committee and the Independent Shareholders is set out on pages 23 to 36 of this circular.

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## DEFINITIONS

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

“Anshan Parkson”	鞍山天興百盛購物中心有限公司 (Anshan Tianxing Parkson Shopping Centre Co., Ltd.), a limited liability company established under the laws of the PRC and an indirect subsidiary of the Company, which is owned as to 51% by the Group and as to 49% by Anshan Tianxing
“Anshan Tianxing”	鞍山天興國際置業發展有限公司 (Anshan Tianxing International Properties Development Co., Ltd.), a sino-foreign equity joint venture enterprise established under the laws of the PRC, a joint venture partner of the Group, which is owned as to 50% by 鞍山市金羽經貿有限公司 (Anshan Jin Yu Economic and Trade Co., Ltd.) and as to 50% by Praise Shine Company Limited (賀明有限公司)
“Arts & Crafts Exhibition”	中國工藝美術品展銷公司 (Arts & Crafts Exhibition Company), an enterprise owned by the whole people established under the laws of the PRC
“associate(s)”	has the meaning ascribed to it in the Listing Rules
“Beijing Equity Exchange”	the Beijing Equity Exchange of the PRC (北京產權交易所)
“Beijing Parkson”	百盛商業發展有限公司 (Parkson Retail Development Co., Ltd.), a sino-foreign equity joint venture enterprise established under the laws of the PRC, and an indirect subsidiary of the Company, which is owned as to 42% by Parkson Investment, as to 14% by Rosenblum, as to 43% by China Arts & Crafts, as to 0.9% by China Arts & Crafts Culture and as to 0.1% by Arts & Crafts Exhibition
“Board”	the board of Directors
“China Arts & Crafts”	中國工藝美術(集團)公司 (China Arts & Crafts (Group) Company), a state-owned enterprise established under the laws of the PRC
“China Arts & Crafts Companies”	China Arts & Crafts, China Arts & Crafts Culture and Arts & Crafts Exhibition
“China Arts & Crafts Culture”	中工美藝美術文化公司 (China Arts & Crafts Culture Company), a state-owned enterprise established under the laws of the PRC

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## DEFINITIONS

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“Chongqing Parkson”	重慶萬友百盛廣場有限公司 (Chongqing Wanyu Parkson Plaza Co., Ltd.), a sino-foreign equity joint venture enterprise established under the laws of the PRC and an indirect subsidiary of the Company, which is owned as to 70% by the Group and as to 30% by Chongqing Wanyou
“Chongqing Wanyou”	重慶萬友經濟發展有限責任公司 (formerly known as “重慶萬友經濟技術發展總公司”) (Chongqing Wanyou Economic Development Co., Ltd.), a wholly state-owned limited liability company established under the laws of the PRC and a joint venture partner of the Group
“Company”	Parkson Retail Group Limited (百盛商業集團有限公司), a company incorporated under the laws of the Cayman Islands with limited liability on 3 August 2005, the shares of which are listed on the Stock Exchange
“connected person(s)”	has the meaning ascribed to it in the Listing Rules
“Dalian Tianhe”	大連天河百盛購物中心有限公司 (Dalian Tianhe Parkson Shopping Center Co., Ltd.), a sino-foreign equity joint venture enterprise established under the laws of the PRC
“Deposit”	a refundable deposit of RMB 110 million payable by Shanghai Lion Investment to the China Arts & Crafts Companies
“Director(s)”	the director(s) of the Company
“Group”	the Company, its subsidiaries and joint ventures
“Guizhou Shenqi Enterprise”	貴州神奇實業有限公司 (Guizhou Shenqi Enterprise Co., Ltd.), a limited liability company established under the laws of the PRC and a joint venture partner of the Group, which is owned as to 30% by Zhang Pei, as to 40% by Zhang Zhi Jun and as to 30% by Zhang Ya
“Guizhou Parkson”	貴州神奇百盛商業發展有限公司 (formerly known as “貴州神奇百貨發展有限公司”) (Guizhou Shenqi Parkson Retail Development Co., Ltd.), a sino-foreign equity joint venture enterprise established under the laws of the PRC and an indirect subsidiary of the Company, which is owned as to 60% by the Group and as to 40% by Guizhou Shenqi Enterprise
“HK\$”	Hong Kong dollar(s), the lawful currency of Hong Kong
“Hong Kong”	the Hong Kong Special Administrative Region of the People’s Republic of China

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## DEFINITIONS

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“Independent Board Committee”	a board committee of the Company comprising all the independent non-executive Directors, namely Mr. Fong Ching, Eddy, Mr. Studer Werner Josef and Mr. Ko Tak Fai, Desmond, who are not interested in the Preliminary Framework Agreement
“Independent Shareholder(s)”	Shareholders other than persons who are required to abstain from voting on the resolution to approve the Preliminary Framework Agreement
“Inner Mongolia Leader”	內蒙古力達百盛廣場有限公司 (Inner Mongolia Leader Parkson Plaza Co., Ltd), a sino-foreign equity joint venture enterprise established under the laws of the PRC
“Latest Practicable Date”	10 February 2006, being the latest practicable date prior to the printing of this circular for ascertaining certain information referred to in this circular
“LDHB”	Lion Diversified Holdings Berhad, a public limited liability company incorporated and domiciled in Malaysia, the shares of which are listed on the Main Board of Bursa Malaysia and the controlling shareholder of the Company
“Liquidated Damages Events”	has the meaning ascribed to it in the section headed “Termination Rights” in this circular
“Listing Rules”	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited
“Mianyang Parkson”	綿陽富臨百盛廣場有限公司 (Mianyang Fulin Parkson Plaza Co., Ltd.), a sino-foreign equity joint venture enterprise incorporated under the laws of the PRC and an indirect subsidiary of the Company, which is owned as to 60% by the Group and as to 40% by Sichuan Fulin
“MOC”	the Ministry of Commerce of the PRC
“Nanning Brilliant”	南寧柏聯百盛商業有限公司 (Nanning Brilliant Parkson Commercial Co., Ltd.), a sino-foreign equity joint venture enterprise established under the laws of the PRC
“Parkson Investment”	Parkson Investment Pte. Ltd., a private company limited by shares incorporated under the Companies Act (Chapter 50 of the Statutes of the Republic of Singapore) and an indirect wholly-owned subsidiary of the Company
“PRC”	the People’s Republic of China

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## DEFINITIONS

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“PRG Corporation”	PRG Corporation Limited, a limited liability company established under the laws of the British Virgin Islands, the immediate holding company of the Company and a wholly-owned subsidiary of LDHB
“Preliminary Framework Agreement”	the preliminary framework agreement entered into between Shanghai Lion Investment and the China Arts & Crafts Companies dated 23 January 2006 as further described in this circular
“Qingdao No. 1”	青島第一百盛有限公司 (Qingdao No. 1 Parkson Co., Ltd.), a sino-foreign equity joint venture enterprise established under the laws of the PRC
“RM”	Ringgit Malaysia, the lawful currency of Malaysia
“RMB”	Renminbi, the lawful currency of the PRC
“Rosenblum”	Rosenblum Investments Pte. Ltd., a private company limited by shares incorporated under the Companies Act (Chapter 50 of the Statutes of the Republic of Singapore) and an indirect wholly-owned subsidiary of the Company
“SASAC”	the State-owned Assets Supervision and Administration Commission of the State Council of the PRC
“SFO”	the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong)
“Shaanxi Chang’an Information”	陝西長安信息置業投資有限公司 (formerly known as “陝西天寶置業投資有限公司”) (Shaanxi Chang’an Information Property Investment Co., Ltd.), a limited liability company established under the laws of the PRC and a joint venture partner of the Group, which is owned as to 65.45% by 長安信息產業(集團)股份有限公司 (Chang’an Information Property (Group) Co., Ltd.), as to 20.73% by 西安亞盛實業開有限公司 (Xi’an Ya Sheng Industrial Development Co., Ltd.), as to 6.91% by 陝西眾興企業集團有限公司 (Shaanxi Zhong Xing Enterprise Group Co., Ltd.)
“Shanghai Lion Investment”	上海獅貿投資諮詢有限公司 (Shanghai Lion Parkson Investment Consultant Co., Ltd.), a wholly foreign-owned enterprise established under the laws of the PRC and an indirect wholly-owned subsidiary of the Company

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## DEFINITIONS

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“Shanghai Lion Property”	上海九海金獅物業管理有限公司 (Shanghai Nine Sea Lion Properties Management Co., Ltd.), a sino-foreign co-operative joint venture enterprise established under the laws of the PRC between the Group and Shanghai Nine Sea Industry and an associated company of the Company
“Shanghai Nine Sea Parkson”	上海九海百盛廣場有限公司 (formerly known as “上海九海金獅廣場有限公司”) (Shanghai Nine Sea Parkson Plaza Co., Ltd.), a sino-foreign co-operative joint venture enterprise established under the laws of the PRC between the Group and Shanghai Nine Sea Industry and an indirect subsidiary of the Company
“Shanghai Nine Sea Industry”	上海九海實業有限公司 (formerly known as “上海九海實業公司”) (Shanghai Nine Sea Industry Co., Ltd.), a limited liability company established under the laws of the PRC and a joint venture partner of the Group
“Share(s)”	the ordinary share(s) of the Company with a nominal value of HK\$0.10 each
“Share Pledge”	the pledge of the 44% Interest granted by the China Arts & Crafts Companies in favour of Shanghai Lion Investment dated 23 January 2006, subject to approval by, and registration with, the relevant PRC regulatory authorities
“Shareholder(s)”	the holder(s) of the Share(s)
“Sichuan Fulin”	四川富臨實業集團有限公司 (Sichuan Fulin Industrial Group Co., Ltd.), a limited liability company established under the laws of the PRC, a joint venture partner of the Group, which is owned as to 51% by An Zhi Fu, as to 20% by An Dong, as to 20% by Nie Dan, as to 5% by An Zhou and as to 4% by Xu Bo
“Somerley”	Somerley Limited, a corporation licensed under the SFO to conduct types 1 (dealing in securities), 4 (advising on securities), 6 (advising on corporate finance) and 9 (asset management) regulated activities and the independent financial adviser to the Independent Board Committee and the Independent Shareholders in relation to the Preliminary Framework Agreement
“Stock Exchange”	The Stock Exchange of Hong Kong Limited
“subsidiary”	has the meaning ascribed to it in section 2 of the Companies Ordinance (Chapter 32 of the Laws of Hong Kong)

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## DEFINITIONS

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“Xi'an Chang'an Parkson”	西安長安百盛百貨有限公司 (Xi'an Chang'an Parkson Store Co., Ltd.), a limited liability company established under the laws of the PRC and an indirect subsidiary of the Company, which is owned as to 51% by the Group and as to 49% by Shaanxi Chang'an Information
“Xi'an Shidai Parkson”	西安時代百盛百貨有限公司 (Xi'an Shidai Parkson Store Co., Ltd.), a limited liability company established under the laws of the PRC and an indirect subsidiary of the Company, which is owned as to 51% by the Group and as to 49% by Xi'an Xinrun
“Xi'an Xinrun”	西安新潤置業有限公司 (Xi'an Xinrun Property Co., Ltd.), a limited liability company established under the laws of the PRC, a joint venture partner of the Group, which is owned as to 39.1% by (Shaanxi Shuang Yi Petrochemical Co., Ltd.) and as to 23.46% by Song Xin Tian and as to 37.44% by 47 other individual shareholders
“Xinjiang Youhao”	新疆友好(集團)股份有限公司 (Xinjiang Friendship (Group) Co., Ltd.), a public limited liability company established under the laws of the PRC, the shares of which are listed on the Shanghai Stock Exchange, and a joint venture partner of the Group
“Xinjiang Parkson”	新疆友好百盛商業發展有限公司 (Xinjiang Youhao Parkson Development Co., Ltd.), a limited liability company established under the laws of the PRC and an indirect subsidiary of the Company, which is owned as to 51% by the Group and as to 49% by Xinjiang Youhao
“Wuxi Distribution”	無錫市供銷合作總社 (Wuxi Distribution Corporation), a collectively-owned enterprise established under the laws of the PRC and a joint venture partner of the Group
“Wuxi Parkson”	無錫三陽百盛廣場有限公司 (Wuxi Sanyang Parkson Plaza Co., Ltd.), a sino-foreign equity joint venture enterprise established under the laws of the PRC and an indirect subsidiary of the Company, which is owned as to 60% by the Group and as to 40% by Wuxi Distribution
“Yangzhou Commercial”	揚州商業大廈 (Yangzhou Commercial Plaza), a state-owned enterprise established under the laws of the PRC and a joint venture partner of the Group



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## DEFINITIONS

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“Yangzhou Parkson”

揚州百盛商業大廈有限公司 (Yangzhou Parkson Plaza Co., Ltd.), a sino-foreign equity joint venture enterprise established under the laws of the PRC and an indirect subsidiary of the Company, which is owned as to 55% by the Group and as to 45% by Yangzhou Commercial

“44% Interest”

the 44% equity interest in Beijing Parkson

“%”

per cent.



**PARKSON RETAIL GROUP LIMITED**

*(a company incorporated in the Cayman Islands with limited liability)*

**(Stock Code: 3368)**

*Executive Directors:*

Mr. Cheng Yoong Choong

Mr. Chew Fook Seng

*Non-executive Director:*

Tan Sri Cheng Heng Jem

*Independent non-executive Directors:*

Mr. Fong Ching, Eddy

Mr. Studer Werner Josef

Mr. Ko Tak Fai, Desmond

*Registered office:*

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P.O. Box 309GT

Ugland House

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*Principal place of business in Hong Kong:*

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1 Queen's Road East

Hong Kong

16 February 2006

*To the Shareholders*

Dear Sir or Madam,

**DISCLOSEABLE AND CONNECTED TRANSACTION  
PRELIMINARY FRAMEWORK AGREEMENT  
IN CONNECTION WITH THE POSSIBLE ACQUISITION  
OF 44% OF BEIJING PARKSON**

**INTRODUCTION**

On 25 January 2006, the Board announced that Shanghai Lion Investment, an indirect wholly-owned subsidiary of the Company, and the China Arts & Crafts Companies entered into the Preliminary Framework Agreement on 23 January 2006, which is legally binding, under which the China Arts & Crafts Companies agreed to offer their 44% Interest in Beijing Parkson for sale, and to seek the approval for such sale from the relevant regulatory authorities in the PRC.

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## LETTER FROM THE BOARD

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The Company currently owns 56% of the equity interest in Beijing Parkson through its wholly-owned subsidiaries. The remaining 44% Interest is currently jointly held by the China Arts & Crafts Companies. The Company wishes to acquire the 44% Interest. However, as the China Arts & Crafts Companies are PRC state-owned enterprises, any sale of the 44% Interest is subject to a valuation process, public tender process and the obtaining of approvals from the relevant PRC regulatory authorities.

In consideration of the initiation by the China Arts & Crafts Companies of the PRC approval process, Shanghai Lion Investment agreed to pay the China Arts & Crafts Companies a refundable deposit of RMB 110 million. Security for the Deposit will be granted by the China Arts & Crafts Companies in favour of Shanghai Lion Investment.

In the event that Shanghai Lion Investment fails in its bid for the 44% Interest and/or the necessary PRC approvals are not obtained, the Deposit (together with accrued interest) will be refunded to Shanghai Lion Investment. In the event that Shanghai Lion Investment is awarded the bid for the 44% Interest, the parties will enter into a sale and purchase agreement for the acquisition of the 44% Interest and the Deposit will form part of the consideration for the acquisition. If Shanghai Lion Investment wins the bid, any acquisition by the Company of the 44% Interest will be subject to Independent Shareholders' approval. If Independent Shareholders' approval is not obtained, the Deposit paid to the China Arts & Crafts Companies will be refunded to Shanghai Lion Investment as further described below.

As at the Latest Practicable Date, the minimum consideration for the 44% Interest has not yet been determined and remains subject to the valuation process to be carried out by a valuer appointed by the China Arts & Crafts Companies and approved by SASAC in accordance with PRC laws and regulations.

As at the date of the Preliminary Framework Agreement and the Latest Practicable Date, China Arts & Crafts, together with its wholly-owned subsidiaries China Arts & Crafts Culture and Arts & Crafts Exhibition, were substantial shareholders of Beijing Parkson, which is a subsidiary of the Company, and therefore connected persons of the Company for the purposes of Chapter 14A of the Listing Rules. Accordingly, the Preliminary Framework Agreement constitutes a connected transaction for the Company under the Listing Rules. As each of the relevant percentage ratios (as defined in Rule 14.07 of the Listing Rules) for the amount of the Deposit is more than 2.5% and therefore exceeds the threshold under Rule 14A.32, the Preliminary Framework Agreement is subject to reporting and announcement requirements, as well as approval by the Independent Shareholders by poll in general meeting.

The Company has, however, applied for a waiver pursuant to Rule 14A.43 of the Listing Rules under which written Independent Shareholders' approval may be accepted in lieu of holding a general meeting on the basis that (1) there are no Shareholders who are required to abstain from voting if the Company were to convene a general meeting for the approval of the Preliminary Framework Agreement and (2) the written approval from PRG Corporation, which holds 361,560,000 Shares representing approximately 65.50% in nominal value of the securities of the Company giving the right

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## LETTER FROM THE BOARD

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to attend and vote at a general meeting, approving the Preliminary Framework Agreement was obtained on 15 February 2006. If the waiver is not obtained from the Stock Exchange on or before 28 February 2006, the Company will make a further announcement with respect to the convening of a general meeting for Independent Shareholders to approve the Preliminary Framework Agreement.

Relevant details of the Preliminary Framework Agreement will also be included in the next published annual report and accounts of the Company in accordance with Rule 14A.45 of the Listing Rules.

According to the Listing Rules, the Preliminary Framework Agreement also constitutes a discloseable transaction of the Company which is subject to the notification and disclosure requirements as set out in Rules 14.34 to 14.36 and 14.38 to 14.39 of the Listing Rules.

The purposes of this circular are to provide you with details of the Preliminary Framework Agreement, to set out the recommendation of the Independent Board Committee in relation to the Preliminary Framework Agreement and to set out the letter of advice from Somerley to the Independent Board Committee and the Independent Shareholders in respect of the terms of the Preliminary Framework Agreement.

Shareholders should note that the possible acquisition of the 44% Interest is subject to a valuation process, public tender process and the obtaining of approvals from the relevant PRC authorities. The obligation to acquire the 44% Interest only becomes legally binding on the Company upon the entry of the formal sale and purchase agreement (if Shanghai Lion Investment wins the bid). No assurance can be given that the Group will acquire the 44% Interest.

### THE PRELIMINARY FRAMEWORK AGREEMENT

#### Date

23 January 2006

#### Parties

- (a) China Arts & Crafts;
- (b) China Arts & Crafts Culture;
- (c) Arts & Crafts Exhibition; and
- (d) Shanghai Lion Investment.

#### Assets proposed to be disposed by the China Arts & Crafts Companies (by public tender)

The 44% equity interest in Beijing Parkson.

### Deposit

RMB 50 million of the Deposit was paid by Shanghai Lion Investment upon the signing of the Preliminary Framework Agreement and RMB 60 million of the Deposit will be paid subsequently, as detailed below. The Deposit will be secured by the Share Pledge. As the granting of the Share Pledge requires the approval of MOC, the China Arts & Crafts Companies have undertaken to seek such approval and procure the registration of the Share Pledge with the relevant PRC authorities. The approval and registration process normally takes approximately 30 to 60 days. The Deposit has been paid and is payable in the following manner:

- (a) RMB 50 million of the Deposit was paid by Shanghai Lion Investment directly to the China Arts & Crafts Companies upon the signing of the Preliminary Framework Agreement. With respect to such RMB 50 million, the China Arts & Crafts Companies have issued an enforcement-of-debt undertaking in favour of Shanghai Lion Investment. In the event that the China Arts & Crafts Companies fail to obtain the requisite MOC approval for, and registration of, the Share Pledge within 45 days (or such later date as Shanghai Lion Investment may specify) from the date of the Preliminary Framework Agreement, Shanghai Lion Investment may request for the Deposit to be refunded. If the China Arts & Crafts Companies fail to refund the Deposit, Shanghai Lion Investment may exercise its right to enforce the enforcement-of-debt undertaking by applying to the PRC courts for specific performance, to compel the China Arts & Crafts Companies to sell their available assets (including the 44% Interest but excluding interests in assets which are subject to encumbrances) by public tender. Shanghai Lion Investment may participate in any such public tender. RMB 50 million of such sale proceeds will be used to first repay Shanghai Lion Investment.
- (b) RMB 60 million of the Deposit shall be paid by Shanghai Lion Investment within two business days upon registration of the Share Pledge.

The Deposit monies are being financed from internal resources of the Company, and not from the proceeds of the initial public offering of the Company.

### Security arrangements

#### *Share Pledge and Enforcement-of-Debt Undertaking*

As mentioned above, the Deposit will be secured by the Share Pledge. Pending approval by, and registration with, the relevant PRC authorities, the China Arts & Crafts Companies have, as an interim measure, issued an enforcement-of-debt undertaking in favour of Shanghai Lion Investment. Under PRC laws, a share pledge is subject to relevant PRC approvals, whereas an enforcement-of-debt undertaking is not.

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## LETTER FROM THE BOARD

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The Company has been advised by Jingtian & Gongcheng, the Group's PRC legal advisers, as follows. The enforcement-of-debt undertaking and, if approved and registered, the Share Pledge are both valid and legally enforceable under PRC laws. The enforcement-of-debt undertaking has been notarised by a PRC licensed notary. Notarisation, under PRC law, is an act or procedure carried out by the licensed notary upon the application of the parties concerned, which serves the purpose of certifying the authenticity and legality of a legal act, a document or a fact of legal significance according to the PRC statutory procedures. No registration or other requirements need to be carried out or obtained. The enforcement-of-debt undertaking entitles Shanghai Lion Investment to petition before the PRC courts for enforcement of debt against the assets of the China Arts & Crafts Companies in the event that the China Arts & Crafts Companies fail to refund the Deposit, without having to first apply to the courts for judgment on the debt action. The PRC courts may order the China Arts & Crafts Companies to repay the Deposit. If they fail to comply with such court order, the courts could order the China Arts & Crafts Companies to put any assets (including the 44% Interest) for sale by public tender and Shanghai Lion Investment may also participate in the public tender. Any such public tender may, at that stage in time, require PRC regulatory approvals. However, the undertaking itself and its exercise do not, and will not, require PRC regulatory approvals as it relates to the procedure of seeking court enforcement. The Share Pledge will entitle Shanghai Lion Investment to compel the China Arts & Crafts Companies to put the 44% Interest up for public tender and Shanghai Lion Investment may participate in that public tender.

In practical terms, the Share Pledge is the better form of security for the Company because it will give the Company priority over other creditors of the China Arts & Crafts Companies with respect to the 44% Interest. Until the Share Pledge is approved and registered, Shanghai Lion Investment only ranks as an unsecured creditor.

The enforcement-of-debt undertaking covers all assets (including the 44% Interest) of the China Arts & Crafts Companies. The enforcement-of-debt undertaking is an interim measure pending approval and registration of the Share Pledge. The undertaking also serves a contingent purpose: if approval for the Share Pledge is not obtained, the interests of the Company will still be protected by the enforcement-of-debt undertaking because the China Arts & Crafts Companies could be compelled by the PRC courts to put their assets for sale if they are in default. Accordingly, it was agreed between the parties that the enforcement-of-debt undertaking will cease to be of effect once the Share Pledge is registered. For reasons which are described above (and in particular because the Share Pledge gives the Company priority over other creditors), the Directors believe that the Share Pledge itself (without the enforcement-of-debt undertaking) provides sufficient security to the Company and that the Group's interests, in terms of protection afforded by the security arrangements, will not be adversely affected when the enforcement-of-debt undertaking ceases to be of effect upon registration of the Share Pledge.

The enforcement-of-debt undertaking and Share Pledge do not in themselves entitle the Company to acquire the 44% Interest. The sale proceeds from any public tender of assets following enforcement will be used to repay Shanghai Lion Investment. Note, however, that if the assets that are put up for public tender are secured assets, any sale proceeds will be first applied to repay the secured creditors. In this respect, the China Arts & Crafts Companies have warranted to Shanghai Lion Investment that the 44% Interest is not subject to any encumbrances. Further, other creditors of the China Arts & Crafts Companies who have obtained court judgments with respect to their debt actions may make an

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## LETTER FROM THE BOARD

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application to the courts to share in the sale proceeds of such public tender, and if such application is made before completion of the enforcement proceedings initiated by Shanghai Lion Investment, the sale proceeds of the public tender (if insufficient to repay the indebtedness owed to all such creditors and Shanghai Lion Investment) may be required by the courts to be shared, on a pro rata basis, between Shanghai Lion Investment and such creditors.

### *Right to withhold dividends*

In addition, Shanghai Lion Investment will have the right to receive from Beijing Parkson, by way of deduction from the dividends to which the China Arts & Crafts Companies are otherwise entitled for the financial year of 2006 and thereafter, such amounts which represent the Deposit paid by Shanghai Lion Investment (together with accrued interest) and liquidated damages of an amount representing 20% of the Deposit paid. The interest rate mentioned above is the one-year base rate of interest for financial institutions to lend out RMB loans, as published by the People's Bank of China. Effective 29 October 2004, the interest rate has been 5.58% although the People's Bank of China may change the rate in the future.

An instruction letter has been issued by the China Arts & Crafts Companies to Beijing Parkson to effect the above. This right is exercisable upon the occurrence of any Liquidated Damages Event or in the event that MOC approval for the Share Pledge is not obtained within 45 days and if the China Arts & Crafts Companies fail to pay such amounts as described above.

The declaration of dividends requires the unanimous board approval of Beijing Parkson (the board of Beijing Parkson comprises of 4 directors nominated by the Group and 3 directors nominated by the China Arts & Crafts Companies). However, the China Arts & Crafts Companies have undertaken that Shanghai Lion Investment will have the right to receive dividends for the purpose of recovering the Deposit and liquidated damages.

### **Valuation process**

In connection with the public tender process, the minimum consideration for the sale of the 44% Interest is to be determined by the valuation process to be carried out by a valuer appointed by the China Arts & Crafts Companies and approved by SASAC in accordance with PRC laws and regulations and as such remains undetermined as at the date of this circular. The costs and expenses involved in the valuation process and public tender process will be borne by the China Arts & Crafts Companies.

If Shanghai Lion Investment is awarded the bid, it would be required to enter into a formal sale and purchase agreement with the China Arts & Crafts Companies within such period of time as may be stipulated by the China Arts & Crafts Companies and the SASAC. The regulations of the Beijing Equity Exchange stipulate that such period of time shall be 5 business days from the date of award of the bid; however, in practice, the China Arts & Crafts Companies can stipulate a different period of time during the public tender process. If Shanghai Lion Investment does not agree on such time period, the Company will nevertheless participate in the public tender process. In the event that the formal sale and purchase agreement cannot be entered into within that specified time period, the Company will be entitled to be refunded the Deposit together with accrued interest.

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## LETTER FROM THE BOARD

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A formal sale and purchase agreement for state-owned assets is usually required to be unconditional (i.e., any shareholders' approval to be sought after the award of the bid should be obtained prior to the signing of the agreement). However, the parties may seek the consent of SASAC if they wish to include conditions (e.g., shareholders' approval) in the formal sale and purchase agreement.

In any event, if Shanghai Lion Investment wins the bid, any acquisition by the Company of the 44% Interest will be subject to Independent Shareholders' approval. If the relevant sale and purchase agreement does not contain any such conditions, Independent Shareholders' approval on the acquisition will be sought and obtained before the entering into of the sale and purchase agreement. If Independent Shareholders' approval is not obtained, the Deposit paid to the China Arts & Crafts Companies shall be refunded to Shanghai Lion Investment as further described below.

### Conditions

Any acquisition by Shanghai Lion Investment of the 44% Interest is subject to a number of conditions:

- (a) the obtaining of approval from SASAC;
- (b) Shanghai Lion Investment being the successful bidder for the 44% Interest pursuant to the public tender process;
- (c) the obtaining of approval from MOC; and
- (d) the obtaining of approval from the Shareholders (if required) pursuant to requirements of the Listing Rules with respect to the Preliminary Framework Agreement and any sale and purchase agreement to be entered into between Shanghai Lion Investment and the China Arts & Crafts Companies

(together the "Conditions").

Upon satisfaction of all of the Conditions and the issuance of a certificate of approval by the MOC with respect to the change in status of Beijing Parkson from a sino-foreign equity joint venture enterprise to a wholly foreign-owned enterprise (including the entering into of the relevant sale and purchase agreement as mentioned above), the parties shall proceed to complete the transfer of the 44% Interest from the China Arts & Crafts Companies to Shanghai Lion Investment. The Deposit of RMB 110 million which would have been paid by Shanghai Lion Investment to the China Arts & Crafts Companies will be off-set against the total consideration amount.



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## LETTER FROM THE BOARD

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### Termination Rights

If:

- (a) Shanghai Lion Investment disagrees with the China Arts & Crafts Companies on the result of the valuation; or
- (b) any Condition is not satisfied within 180 days of the signing of the Preliminary Framework Agreement (or such later date as may be approved by Shanghai Lion Investment),

Shanghai Lion Investment may terminate the Preliminary Framework Agreement by giving written notice to the China Arts & Crafts Companies. The China Arts & Crafts Companies shall refund the Deposit (together with accrued interest at the same rate as mentioned above) to Shanghai Lion Investment within 3 business days of issuance of such termination notice. If the China Arts & Crafts fail to refund such amount, Shanghai Lion Investment may enforce the Share Pledge or, if the Share Pledge has not been obtained, the enforcement-of-debt undertaking.

In the event that the transfer of the 44% Interest is not effected for any of the following reasons:

- (i) failure to obtain the PRC regulatory approvals;
- (ii) failure to obtain the approval from the Shareholders (if required);
- (iii) termination of the agreement by Shanghai Lion Investment on grounds of disagreement on the result of the valuation; or
- (iv) failure to obtain the board approval of Beijing Parkson with respect to such transfer (other than where such board approval was not obtained by reason of the directors appointed by the China Arts & Crafts Companies not voting in favour of the transfer),

the Company will be entitled to be refunded the Deposit paid (together with accrued interest).

In the event that the transfer of the 44% Interest is not effected for reasons other than those mentioned above (e.g., if the bid is awarded to a third party or if the public tender process is unilaterally terminated by China Arts & Crafts) (“Liquidated Damages Events”), the Company will be entitled to be refunded the Deposit paid (together with accrued interest at the same rate as mentioned above) and paid liquidated damages of such amount representing 20% of the Deposit which has been paid. This aggregate amount may be received by the Company from Beijing Parkson by way of deduction from the dividends which the China Arts & Crafts Companies are otherwise entitled to receive for and from the financial year of 2006. If the China Arts & Crafts Companies fail to refund such amount, Shanghai Lion Investment may enforce the Share Pledge or, if the Share Pledge has not been obtained, the enforcement-of-debt undertaking.

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## LETTER FROM THE BOARD

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### INFORMATION ON THE CHINA ARTS & CRAFTS COMPANIES

China Arts & Crafts is principally engaged in the business of international trading, retail, exhibition and trading of special commodities such as arts and crafts. China Arts & Crafts Culture and Arts & Crafts Exhibition are wholly-owned subsidiaries of China Arts & Crafts. China Arts & Crafts Culture is principally engaged in the business of cultural consultation and trading of arts and crafts, and Arts & Crafts Exhibition is principally engaged in the business of exhibition and trading of arts and crafts and ornaments.

### INFORMATION ON THE COMPANY, SHANGHAI LION INVESTMENT AND BEIJING PARKSON

The Company, Shanghai Lion Investment and Beijing Parkson, as part of the Group, are principally engaged in the operation of 37 “Parkson” branded department stores and two “Xtra” branded supercentres situated in prime locations in 26 cities in the PRC. The Group offers a wide range of merchandise in those department stores and supercentres, including fashion and apparel, cosmetics and accessories, household, electrical goods and groceries.

### HISTORICAL FINANCIAL INFORMATION ABOUT BEIJING PARKSON

Beijing Parkson, an indirect subsidiary of the Company which is held as to 56% by the Group, is the owner and operator of the Parkson department store located at Fuxingmennei Street, Beijing. Its branch offices, Beijing Haidian branch, Taiyuan branch, Zhengzhou branch and Haerbin branch, are the operators of the Company’s department stores located in Haidian District in Beijing, Taiyuan, Zhengzhou and Haerbin respectively.

Beijing Parkson also owns 51% of the equity interest in Xinjiang Parkson, the operator of the Company’s department store in Xinjiang.

## LETTER FROM THE BOARD

Set out below is the historical financial information about Beijing Parkson and Xinjiang Parkson for each of the years ended 31 December 2003 and 2004 and the six months ended 30 June 2005.

	Unaudited financial information under PRC generally accepted accounting principles (“GAAP”) on an unconsolidated basis		
	Audited financial information under PRC generally accepted accounting principles (“GAAP”) on an unconsolidated basis		
	Year ended 31 December 2003 <i>(in RMB '000)</i>	Year ended 31 December 2004 <i>(in RMB '000)</i>	Six months ended 30 June 2005 <i>(in RMB '000)</i>
<b>Beijing Parkson</b>			
Turnover	862,255	1,091,809	677,605
Profit before tax	121,670	135,527	78,803
Net profit after tax	81,185	90,639	49,376
Total assets	678,075	639,623	715,090
Net current liabilities	(281,341)	(276,073)	(510,276)
Net asset value	150,455	154,987	204,336
<b>Xinjiang Parkson</b>			
Turnover	212,494	188,185	120,182
Loss before tax	(14,475)	(5,360)	(564)
Net loss after tax	(14,475)	(5,360)	(564)
Total assets	39,768	38,231	44,678
Net current liabilities	(17,685)	(18,876)	(45,078)
Net asset value	5,525	164	(399)

*Note:* Turnover figures above include gross sales proceeds from direct sales and concessionaire sales.

The distributable reserve of Beijing Parkson as at 30 June 2005, according to the unaudited financial statements prepared under PRC GAAP by the Company, was RMB 49,376,000. Nevertheless, the Directors believe, as described above, that the Group will be sufficiently protected by the Share Pledge. The dividends-withholding arrangements serve to provide additional comfort to the Group, in addition to the security provided by the Share Pledge.

### REASONS FOR AND BENEFITS OF THE PRELIMINARY FRAMEWORK AGREEMENT

Beijing Parkson is strategically located in the capital of the PRC and is a major contributor in terms of revenue and profits to the Group. Accordingly, the Board considers that Beijing Parkson, as a wholly-owned subsidiary of the Company, would enhance the growth and profitability of the Group. Moreover, if Beijing Parkson were to be wholly-owned by the Company, the decision-making process of Beijing Parkson would become more efficient and there would be greater flexibility in the implementation of Beijing Parkson's business expansion plan. The Board considers that the above would be in line with the Group's expansion plans and would complement its long-term growth strategy.

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## LETTER FROM THE BOARD

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Accordingly, the Company had been seeking to ascertain if China Arts & Crafts was willing to dispose of its 44% Interest. While enquiries were made by the Company prior to the Company's initial public offering, China Arts & Crafts did not wish to dispose of the 44% Interest at the time. In other words, therefore, at the time of the initial public offering of the Company, China Arts & Crafts did not wish to dispose of the 44% Interest and, accordingly, no negotiations took place on the matter.

In the weeks leading up to the announcement on 25 January 2006, China Arts & Crafts indicated to the Company that it was willing to consider disposing of its 44% Interest on terms acceptable to it, which included the payment of a deposit.

The Directors considered that it was important that the Company should express a genuine interest in the acquisition of the 44% Interest and that it was equally important to commit the China Arts & Crafts Companies to commencing the PRC approval process. Accordingly, the Preliminary Framework Agreement was entered into pursuant to which (a) the China Arts & Crafts Companies must commence the PRC approval process and (b) the Group would put up the Deposit.

The amount of the Deposit was arrived at after arm's length negotiations between the Company and the China Arts & Crafts Companies as consideration for the initiation by the China Arts & Crafts Companies of the PRC approval process.

The Directors have taken into account the following principal factors in considering the amount of the Deposit paid and payable to the China Arts & Crafts Companies:

- (i) the strategic benefits of the Company owning 100% of Beijing Parkson (as mentioned above);
- (ii) the fact that the opportunity for the possible acquisition by the Group of the 44% Interest can only materialise if the PRC approvals and public tender process is carried out and that, under the terms of the Preliminary Framework Agreement, the China Arts & Crafts Companies are obliged to initiate such process;
- (iii) the potential performance of retail business in Beijing, in particular that of department stores, as well as the historical financial performance and growth of Beijing Parkson; and
- (iv) the unaudited adjusted net asset value of Beijing Parkson, details of which are described below.

With respect to the Company's exposure in relation to the Deposit payment, the Directors believe that the Share Pledge and, as an interim measure, the enforcement-of-debt undertaking would adequately protect the Company and that the amounts realisable on any enforcement of the Share Pledge (having regard to the profitability of Beijing Parkson and the value of its underlying assets) would be sufficient to cover the amount of the Deposit. Beijing Parkson's major asset is its property interests in the main wing of the flagship Beijing store which the Directors believe to be a quality asset. Moreover, China Arts & Crafts is an established and reputable group which is also a PRC state-owned enterprise. As set out in the table above, the net asset value of Beijing Parkson is

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## LETTER FROM THE BOARD

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approximately RMB 204 million as at 30 June 2005. However, the market value of the property of its self-owned flagship Beijing store is, as at 31 August 2005 (based on the valuation report, the text of which is set out in the Company's prospectus dated 17 November 2005), is approximately RMB 836 million which is approximately RMB 487 million above its carrying value of approximately RMB 349 million in the books of Beijing Parkson. Note also that dividends of RMB 112 million in respect of the year ended 31 December 2005 have been declared in December 2005 and January 2006.

The net asset value of Xinjiang Parkson is not significant as compared to that of Beijing Parkson and there are no significant intra group transactions between Beijing Parkson and Xinjiang Parkson. On this basis, the Directors believe that there is no material difference between the adjusted net asset value of Beijing Parkson on an unconsolidated basis and that on a consolidated basis.

On the basis of all these factors, the Directors (including the independent non-executive Directors) believe that the amount and the payment terms of the Deposit and the other terms of the Preliminary Framework Agreement are fair and reasonable, and that the entering into the Preliminary Framework Agreement and the payment of the Deposit are in the interests of the Company and the Shareholders as a whole.

### DISCLOSEABLE AND CONNECTED TRANSACTION

As at the date of the Preliminary Framework Agreement, China Arts & Crafts, together with its wholly-owned subsidiaries China Arts & Crafts Culture and Arts & Crafts Exhibition, are substantial shareholders of Beijing Parkson, which is a subsidiary of the Company. China Arts & Crafts, together with its wholly-owned subsidiaries China Arts & Crafts Culture and Arts & Crafts Exhibition, are therefore connected persons of the Company under the Listing Rules. Accordingly, the Preliminary Framework Agreement constitutes a connected transaction for the Company under the Listing Rules. As each of the relevant percentage ratios (as defined in Rule 14.07 of the Listing Rules) for the amount of the Deposit is more than 2.5% and therefore exceeds the threshold under Rule 14A.32, the Preliminary Framework Agreement is subject to reporting and announcement requirements, as well as approval by the Independent Shareholders by poll in general meeting.

To the best of the Directors' knowledge, information and belief having made all reasonable enquiry, neither the China Arts & Crafts Companies, their ultimate beneficial owners or their associates hold any Share(s) in the Company. To the best of the Directors' knowledge, information and belief having made all reasonable enquiry, none of the Shareholders or their respective associates have any interest in the transaction which is different from other Shareholders.

The Company has applied for a waiver pursuant to Rule 14A.43 of the Listing Rules under which written Independent Shareholders' approval may be accepted in lieu of holding a general meeting, on the basis that (1) there are no Shareholders who are required to abstain from voting if the Company were to convene a general meeting for the approval of the Preliminary Framework Agreement and (2) the written approval from PRG Corporation, which holds 361,560,000 Shares representing approximately 65.50% in nominal value of the securities of the Company giving the right to attend and

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## LETTER FROM THE BOARD

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vote at a general meeting, approving the Preliminary Framework Agreement was obtained on 15 February 2006. If the waiver is not obtained from the Stock Exchange on or before 28 February 2006, the Company will make a further announcement with respect to the convening of a general meeting for Independent Shareholders to approve the Preliminary Framework Agreement.

The China Arts & Crafts Companies and their ultimate beneficial owners have no relationship with the Company and its connected persons other than as set out above.

Relevant details of the Preliminary Framework Agreement will also be included in the next published annual report and accounts of the Company in accordance with Rule 14A.45 of the Listing Rules.

According to the Listing Rules, the Preliminary Framework Agreement also constitutes a discloseable transaction of the Company which is subject to the notification and disclosure requirements as set out in Rules 14.34 to 14.36 and 14.38 to 14.39 of the Listing Rules.

As stated above, the 44% Interest must undergo a valuation process and be put up for public tender. As such, the Company is unable to estimate with any certainty the timing for the entering into and the completion of any formal sale and purchase agreement, as this depends on the timing for the valuation process and the public tender process and the Company is also unable to ascertain the actual amount of the consideration for the 44% Interest. If the Company succeeds in its bid for the 44% Interest, the transaction may constitute a major and connected transaction, and Independent Shareholders' approval would be required for completion of the acquisition. The Company will comply with the requirements under the Listing Rules (if any) before completion of any acquisition of the 44% Interest, including but not limited to the despatch of the relevant circular together with a letter from the independent financial adviser, a recommendation from the Independent Board Committee, a valuation report (where appropriate) and the obtaining of relevant Independent Shareholders' approval.

Shareholders should note that the possible acquisition of the 44% Interest is subject to a valuation process, public tender process and the obtaining of approvals from the relevant PRC authorities. The obligation to acquire the 44% Interest only becomes legally binding on the Company upon the entry of the formal sale and purchase agreement (if Shanghai Lion Investment wins the bid). No assurance can be given that the Group will acquire the 44% Interest.

### **FINANCIAL EFFECT OF THE PRELIMINARY FRAMEWORK AGREEMENT ON THE GROUP**

#### **Total assets**

As the Deposit was financed from internal resources of the Group, it will not have any material impact on the total assets of the Group.

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## LETTER FROM THE BOARD

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### **Liability**

As the Deposit was paid in cash and financed from internal resources of the Group, there is no impact on liability of the Group as a result of such payment.

### **Earnings**

As the Preliminary Framework Agreement will not generate any income to the Group, it will not have any impact on its earnings.

### **Liquidity**

Taking into account the Group's cash and cash-equivalent balance (which was approximately RMB 483 million as at 30 June 2005) and the positive operating cashflows of the Group's business, the Directors consider that the payment of the Deposit would have no material adverse effect on the liquidity of the Group.

Accordingly, the Preliminary Framework Agreement would not have any material impact on the financial position of the Group.

### **ADVICE**

Your attention is drawn to the letter from the Independent Board Committee as set out on page 22 of this circular which contains its advice to the Independent Shareholders in respect of the Preliminary Framework Agreement.

Your attention is also drawn to the letter of advice received from Somerley, the independent financial adviser to the Independent Board Committee and the Independent Shareholders as set out on pages 23 to 36 of this circular which contains, among other things, its advice to the Independent Board Committee and the Independent Shareholders in relation to the terms of the Preliminary Framework Agreement and the principal factors and reasons considered by it in arriving at its advice.

Your attention is also drawn to the general information as set out in the appendix of this circular.

By Order of the Board  
**Parkson Retail Group Limited**  
**Cheng Yoong Choong**  
*Managing Director*



**PARKSON RETAIL GROUP LIMITED**

*(a company incorporated in the Cayman Islands with limited liability)*

**(Stock Code: 3368)**

16 February 2006

*To the Independent Shareholders*

Dear Sir or Madam,

**DISCLOSEABLE AND CONNECTED TRANSACTION  
PRELIMINARY FRAMEWORK AGREEMENT  
IN CONNECTION WITH THE POSSIBLE ACQUISITION  
OF 44% OF BEIJING PARKSON**

We refer to the circular issued by the Company to its shareholders and dated 16 February 2006 (the “Circular”) of which this letter forms part. Terms defined in the Circular have the same meanings when used in this letter unless the context otherwise requires.

We have been appointed as the Independent Board Committee to consider the terms of the Preliminary Framework Agreement and to advise the Independent Shareholders in connection with the Preliminary Framework Agreement as to whether, in our opinion, its terms are fair and reasonable so far as the Independent Shareholders are concerned and whether the Preliminary Framework Agreement is in the interests of the Company and the Shareholders as a whole. Somerley has been appointed as the independent financial adviser to advise us in this respect.

We wish to draw your attention to the letter from the Board and the letter from Somerley as set out in the Circular.

Having considered the principal factors and reasons considered by, and the advice of, Somerley as set out in its letter of advice, we consider that the terms of the Preliminary Framework Agreement are fair and reasonable so far as the interests of the Independent Shareholders are concerned and that the Preliminary Framework Agreement is in the interests of the Company and the Shareholders as a whole.

Yours faithfully,  
**FONG Ching, Eddy**  
**STUDER Werner Josef**  
**KO Tak Fai, Desmond**  
*Independent Board Committee*



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## LETTER FROM SOMERLEY

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*The following is the full text of the letter of advice from Somerley in respect of the Preliminary Framework Agreement and is prepared for the purpose of incorporation into this circular.*



Somerley Limited  
Suite 2201, 22nd Floor  
Two International Finance Centre  
8 Finance Street  
Central  
Hong Kong

16 February 2006

*To: The Independent Board Committee and  
the Independent Shareholders*

Dear Sirs,

**DISCLOSEABLE AND CONNECTED TRANSACTION  
PRELIMINARY FRAMEWORK AGREEMENT  
IN CONNECTION WITH THE  
POSSIBLE ACQUISITION OF 44% OF BEIJING PARKSON**

### INTRODUCTION

We refer to our appointment to advise the Independent Board Committee and the Independent Shareholders in connection with the Preliminary Framework Agreement regarding a possible acquisition by the Group of the remaining 44% interest in Beijing Parkson not already owned by it. Details of the Preliminary Framework Agreement entered into between Shanghai Lion Investment, an indirect wholly-owned subsidiary of the Company, and the China Arts & Crafts Companies (comprising China Arts & Crafts and its wholly-owned subsidiaries, namely China Arts & Crafts Culture and Arts & Crafts Exhibition) are contained in the circular to the Shareholders dated 16 February 2006 (the “Circular”), of which this letter forms part. Unless otherwise defined, terms used in this letter shall have the same meanings as defined in the Circular.

The Preliminary Framework Agreement constitutes a discloseable transaction of the Company under the Listing Rules. The China Arts & Crafts Companies are connected persons of the Company (as defined under the Listing Rules) as China Arts & Crafts is a substantial shareholder of a subsidiary of the Company, Beijing Parkson, and China Arts & Crafts Culture and Arts & Crafts Exhibition are wholly-owned subsidiaries of China Arts & Crafts. Accordingly, the Preliminary Framework Agreement also constitutes a connected transaction of the Company and is subject to the approval of the Independent Shareholders.

The Company has applied for a waiver to accept written Independent Shareholders’ approval in lieu of holding a general meeting (the “Waiver”) on the basis that (1) no Shareholders will be required to abstain from voting if the Company were to convene a general meeting for the approval of the Preliminary Framework Agreement and (2) the Company has obtained the written approval of the

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## LETTER FROM SOMERLEY

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Preliminary Framework Agreement from PRG Corporation, which holds 361,560,000 Shares representing approximately 65.50% of the issued share capital of the Company. We are informed by the Company that if the Waiver is not obtained on or before 28 February 2006, the Company would convene a general meeting of Shareholders for the purpose of considering and, if thought fit, approving the Preliminary Framework Agreement.

An Independent Board Committee comprising Messers Fong Ching, Eddy, Studer Werner Josef and Ko Tak Fai, Desmond, the three independent non-executive Directors, has been formed to advise the Independent Shareholders in respect of the Preliminary Framework Agreement and the transaction contemplated thereunder. We, Somerley Limited, have been appointed as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in this regard.

In formulating our advice, we have relied on the information and facts supplied, and the opinions expressed, by the executive Directors and the management of the Company, which we have assumed to be true, accurate and complete. We have sought and received confirmation from the executive Directors and the management of the Company that all material relevant information has been supplied to us and to the best knowledge of the executive Directors and the management of the Company, no material facts have been omitted from the information supplied and opinions expressed by them. We consider that the information we have received is sufficient for us to reach our advice and recommendation as set out in this letter and it is justified for us to rely on such information. We have no reason to doubt the truth and accuracy of the information provided to us, or to believe that any material information has been omitted or withheld. However, we have not conducted any independent investigation into the business and affairs of the Group or the Beijing Parkson Group (as defined below). We have assumed that all information and representations contained or referred to in the Circular are true at the date of the Circular.

### EXECUTIVE SUMMARY

The Group currently holds 56% of equity interest in Beijing Parkson and the remaining 44% Interest is held jointly by the China Arts & Crafts Companies. The Group wishes to acquire the remaining 44% Interest. However, as the China Arts & Crafts Companies are PRC state-owned enterprises, any sale of the 44% Interest is subject to valuation and a public tender process and the obtaining of approvals from the relevant PRC regulatory authorities. The Board considers that it is important that the Company should express a genuine interest in the acquisition of the 44% Interest (the “Possible Acquisition”) and that it was equally important to commit the China Arts & Crafts Companies to commencing the PRC approval process. Accordingly, the Preliminary Framework Agreement was entered into between Shanghai Lion Investment and the China Arts & Crafts Companies pursuant to which (a) the China Arts & Crafts Companies agree to commence the PRC approval process and (b) Shanghai Lion Investment agrees to pay the China Arts & Crafts Companies a refundable deposit of RMB110 million (the “Deposit”). The purpose of this letter is to set out our advice in respect of the Preliminary Framework Agreement.

If the Group succeeds in its bid for the 44% Interest, a formal sale and purchase agreement in respect of the Possible Acquisition would be entered into. The Possible Acquisition will constitute a separate connected transaction of the Company for which we will give separate advice and analysis to the Independent Board Committee and the Independent Shareholders. The Company will make a further announcement and issue a separate circular (containing another letter of advice from us) to its Shareholders if the Group succeeds in its bid for the 44% Interest. However, as the 44% Interest is subject to a public tender process, it is uncertain whether the Possible Acquisition would eventually materialise.

### PRINCIPAL FACTORS AND REASONS TAKEN INTO ACCOUNT

In arriving at our opinion, we have taken into account the following principal factors and reasons:

#### 1. **Background information on the Group and the Beijing Parkson Group**

##### (i) *Business of the Group*

The Company was listed on the Stock Exchange in November 2005 by way of public offer and placing. The Group is principally engaged in the ownership and operation of department stores and supercentres in the PRC under the brands of “Parkson” and “Xtra” respectively. Currently, the Group has 37 department stores and 2 supercentres in 26 cities in the PRC including major cities such as Beijing, Shanghai, Chongqing and Xi’an. Of these department stores and supercentres, 23 department stores are owned and operated by the Group and the remaining 14 department stores and the 2 supercentres are managed by the Group for third parties and connected persons (as defined under the Listing Rules) of the Company. The Group has positioned itself at the middle to middle-upper end of the retail market in the PRC and offers a wide range of consumer merchandise.

The Group’s revenue are generated from direct sales and concessionaire sales. Direct sales are sales of merchandise sourced and sold directly by the Group. As regards concessionaire sales, the Group has entered into concessionaire agreements with certain suppliers (known as concessionaires) for the supply of branded goods. The Group would receive a percentage of the revenue generated from the sales of these products as a commission income.

In addition to income generated from its self-owned stores, the Group also receives consultancy and management fees from department stores and supercentres that it manages on behalf of third parties and connected persons (as defined under the Listing Rules) of the Company.

## LETTER FROM SOMERLEY

### (ii) *Financial performance of the Group*

Set out below is a summary of the key pro forma financial information of the Group for the year ended 31 December 2004 and the six months ended 30 June 2005 (the “Review Period”) which is prepared under the International Financial Reporting Standards (“IFRS”) and extracted from the prospectus of the Company dated 17 November 2005 (the “Prospectus”):

	Year ended 31 December 2004			Six months ended 30 June 2005		
	RMB'000	RMB'000	%	RMB'000	RMB'000	%
	(unaudited)	(unaudited)		(unaudited)	(unaudited)	
<b>Turnover</b>						
<i>Self-owned stores</i>						
Sales of goods — direct sales	483,875			307,503		
Commission from concessionaire sales	<u>574,240</u>	1,058,115	86.2	<u>365,374</u>	672,877	84.7
<i>Managed stores</i>						
Consultancy and management fees		38,458	3.1		24,514	3.1
<i>Other operating revenue</i>		<u>131,217</u>	<u>10.7</u>		<u>97,582</u>	<u>12.2</u>
		1,227,790	100.0		794,973	100.0
<b>Profit from operations</b>		283,459			219,745	
<b>Net profit attributable to the Shareholders for the year/period</b>		150,629			135,552	

*Note:* The above is pro forma financial information of the Group prepared on the assumption that the stores, operating entities or businesses acquired by the parent group of the Company have been transferred to the Group effective from 1 January 2004 as part of the reorganisation undergone by the Group in preparation for its listing, details of which are included in the Prospectus.

As illustrated in the above summary, direct sales and concessionaire sales generated from the Group’s self-owned department stores accounted for over 80% of the Group’s turnover during the Review Period. The remaining turnover is attributable to consultancy and management fees received by the Group from its managed department stores and other operating revenue which include, among others, rental income, promotion income, credit card handling fees and display space leasing fees. Among other stores in different cities in the PRC, the Group’s department stores in Beijing and Shanghai are the major revenue contributors to the Group.

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## LETTER FROM SOMERLEY

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### (iii) *Business and financial performance of Beijing Parkson*

#### *Beijing Parkson*

Beijing Parkson was established in 1993 in the PRC as a sino-foreign co-operative joint venture enterprise and was converted into a sino-foreign equity joint venture enterprise in 2003. The joint venture term of Beijing Parkson is 30 years commencing from October 1993.

Beijing Parkson is the owner and operator of the flagship Beijing store located at No. 101, Fuxingmennei Street, Xicheng District, Beijing, the PRC which is a key revenue contributor of the Group. Apart from the flagship Beijing store, Beijing Parkson also operates through its branch offices four other department stores located in Haidian district in Beijing, Taiyuan, Zhengzhou and Haerbin.

Beijing Parkson is a major contributor to the Group in terms of revenue and profit. Set out below is the historical financial information of Beijing Parkson for the two years ended 31 December 2004 and the six months ended 30 June 2005 provided by the Company:

	<b>Year ended 31 December 2003</b>	<b>Year ended 31 December 2004</b>	<b>Six months ended 30 June 2005</b>
	(audited)	(audited)	(unaudited)
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
<b>Turnover</b>	862,255	1,091,809	677,605
<b>Profit before tax</b>	121,670	135,527	78,803
<b>Net profit after tax for the year/period</b>	81,185	90,639	49,376
<b>Total assets</b>	678,075	639,623	715,090
<b>Net asset value</b>	150,455	154,987	204,336

#### *Notes:*

- (1) the above financial information is extracted from accounts of Beijing Parkson prepared under the generally accepted accounting principles in the PRC (the "PRC GAAP") as accounts of Beijing Parkson that are prepared in accordance with the IFRS are not currently available;
- (2) the above financial information does not include those of Xinjiang Parkson which is Beijing Parkson's sole operating subsidiary; and
- (3) the above turnover figures include gross sales proceeds from direct sales and concessionaire sales. For the concessionaire sales, the Group is entitled to a percentage of the revenue as commission income.

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## LETTER FROM SOMERLEY

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### *Adjusted Net Assets*

As at 30 June 2005, Beijing Parkson had net assets of approximately RMB204.3 million based on its unaudited management accounts for the six months ended 30 June 2005. Beijing Parkson's major asset is the property interests (including the land use rights) it holds in its flagship Beijing store. The property was valued at approximately RMB836 million as at 31 August 2005, which represents approximately RMB487 million in excess of the property's carrying value in the unaudited balance sheet of Beijing Parkson as at 30 June 2005. Beijing Parkson has declared dividends in the sum of approximately RMB112 million for the year ended 31 December 2005. After adjusting for the market value of the property of the flagship Beijing store and the dividends declared in respect of the year ended 31 December 2005, Beijing Parkson would have adjusted net assets of approximately RMB579 million, of which approximately RMB255 million is attributable to the 44% Interest, as illustrated below:

	<i>RMB' million</i>
<b>Net asset value as at 30 June 2005</b>	204
Revaluation surplus on property ( <i>note</i> )	487
Dividends declared in respect of the year ended 31 December 2005	(112)
Adjusted net asset value ("Adjusted NAV")	579
 <b>Attribution to 44% Interest</b>	 255

*Note:* The revaluation surplus is attributable to the property of the main wing of the flagship Beijing store, which was valued at RMB836 million as at 31 August 2005, full text of the property valuation report including description of the valuation method is included in the Prospectus. Beijing Parkson has pledged such property as security for bank borrowings of Beijing Parkson, which outstanding balance was approximately RMB240 million as at the Latest Practicable Date.

The RMB255 million has not taken into account the results of Beijing Parkson for the period from 1 July 2005 to 31 December 2005.

### *Xinjiang Parkson*

Xinjiang Parkson is Beijing Parkson's sole subsidiary. Xinjiang Parkson is a limited liability company formed under the laws of the PRC on 11 November 2002. Beijing Parkson holds a 51% equity interest in Xinjiang Parkson (which together with Beijing Parkson is known as the "Beijing Parkson Group"). The remaining 49% interest in Xinjiang Parkson is held by Xinjiang Friendship (Group) Co. Ltd., which shares are listed on the Shanghai Stock Exchange in the PRC. Xinjiang Parkson owns and operates a department store in Xinjiang which opened in December 2002.

## LETTER FROM SOMERLEY

Set out below is the historical financial information of Xinjiang Parkson for the two years ended 31 December 2004 and the six months ended 30 June 2005 provided by the Company:

	<b>Year ended 31 December 2003</b>	<b>Year ended 31 December 2004</b>	<b>Six months ended 30 June 2005</b>
	(audited)	(audited)	(unaudited)
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
<b>Turnover</b>	212,494	188,185	120,182
<b>Loss before tax</b>	(14,475)	(5,360)	(564)
<b>Net loss after tax for the year/period</b>	(14,475)	(5,360)	(564)
<b>Total assets</b>	39,768	38,231	44,678
<b>Net asset/(liability)</b>	5,525	164	(399)

*Notes:*

- (1) the above financial information is extracted from accounts of Xinjiang Parkson prepared under the PRC GAAP as accounts of Xinjiang Parkson that are prepared under the IFRS are not currently available; and
- (2) the above turnover figures include gross sales proceeds from direct sales and concessionaire sales. For the concessionaire sales, the Group is entitled to a percentage of the revenue as commission income.

Xinjiang Parkson is a start-up operation and is still making losses. As illustrated by the above financial data, the scale of operation of Xinjiang Parkson is relatively small as compared to that of Beijing Parkson.

We have not been provided with the consolidated financial information of the Beijing Parkson Group. However, the management of the Company has confirmed that there is no significant intra-group transactions between Beijing Parkson and Xinjiang Parkson. On this basis, it is expected that there would not be any significant intra-group adjustments if the consolidated accounts of the Beijing Parkson Group were to be prepared. In addition, as the net liability of Xinjiang Parkson is not significant as compared to that of Beijing Parkson, the Directors believe that there is no material difference between the Adjusted NAV of Beijing Parkson and the adjusted consolidated net asset value of the Beijing Parkson Group.

### 2. Reasons and benefits of the Preliminary Framework Agreement

Beijing Parkson is strategically located in Beijing which is the capital of the PRC. As mentioned above, Beijing Parkson is a major profit and revenue contributor to the Group. Accordingly, the Board considers that the acquisition of the remaining 44% Interest would enhance the growth and profitability of the Group. Moreover, if Beijing Parkson were to be wholly-owned by the Company, the decision-making process of Beijing Parkson would become more efficient and there would be greater flexibility in the implementation of Beijing Parkson's business expansion plan.

Accordingly, the Company had been seeking to ascertain if the China Arts & Crafts Companies were willing to dispose of the 44% Interest. In the weeks leading up to the announcement on 25 January 2006, the China Arts & Crafts Companies indicated to the Company that they were willing to consider disposing the 44% Interest on terms acceptable to them. However, as the China Arts & Crafts Companies are PRC state-owned enterprises, any sale of the 44% Interest is subject to valuation and a public tender process and the obtaining of approvals from the relevant PRC regulatory authorities.

As mentioned above, the purpose of the Preliminary Framework Agreement entered into between Shanghai Lion Investment and the China Arts & Crafts Companies is to commit the China Arts & Crafts Companies to commence the PRC approval process which is a necessary first step that may lead to the Possible Acquisition. In consideration of the China Arts & Crafts Companies' agreeing to commencing the PRC approval process, the Group agrees to pay the China Arts & Crafts Companies a refundable Deposit of RMB110 million. Sale of the 44% Interest is subject to public tender and approval process. If the Possible Acquisition is not eventually materialised, the Group is entitled to the refund of such amount of the Deposit that has been paid under the terms of the Preliminary Framework Agreement.

The Possible Acquisition, if materialised, would constitute a separate connected transaction of the Company and will be subject to the following conditions ("Conditions"):

- (a) Shanghai Lion Investment being the successful bidder for the 44% Interest pursuant to the public tender process;
- (b) the obtaining of approval from SASAC;
- (c) the obtaining of approval from MOC; and
- (d) the obtaining of approval from the Shareholders (if required) pursuant to requirements of the Listing Rules with respect to the Preliminary Framework Agreement and any sale and purchase agreement to be entered into between Shanghai Lion Investment and the China Arts & Crafts Companies.

The Company will make a further announcement in respect of the Possible Acquisition as and when appropriate in accordance with the requirements of the Listing Rules. As at the date of the Latest Practicable Date, the minimum consideration for the 44% Interest has not yet been determined and remains subject to valuation to be carried out by a valuer appointed by the China Arts & Crafts Companies and approved by SASAC in accordance with PRC laws and regulations.



### 3. Terms of the Preliminary Framework Agreement

#### *The Deposit*

##### (i) *Basis*

As mentioned in the “Letter from the Board”, the amount of the Deposit was arrived at after arm’s length negotiations between the Company and the China Arts & Crafts Companies as consideration for the initiation by the China Arts & Crafts Companies of the PRC approval process. In determining the amount of the Deposit, the Directors have taken into consideration the following major factors:

- a) the strategic benefits of the Company owning 100% of Beijing Parkson;
- b) the fact that the opportunity for the possible acquisition by the Group of the 44% Interest can only materialise if the PRC approvals and public tender process is carried out and that, under the terms of the Preliminary Framework Agreement, the China Arts & Crafts Companies are obliged to initiate such process;
- c) the potential performance of retail business in Beijing, in particular that of department stores, as well as the historical financial performance and growth of Beijing Parkson; and
- d) the Adjusted NAV of Beijing Parkson.

##### (ii) *Payment term*

The Deposit has been paid and is payable in cash in the following manner:

- (a) RMB50 million of the Deposit (the “Initial Deposit”) was paid by the Group upon the signing of the Preliminary Framework Agreement on 23 January 2006; and
- (b) RMB60 million of the Deposit shall be paid by the Group within two business days upon registration of the Share Pledge (as discussed below).

If Shanghai Lion Investment wins the bid for the 44% Interest, the parties will enter into a formal sale and purchase agreement for such acquisition and the Deposit will form part of the consideration. The Deposit of RMB110 million which would have been paid by Shanghai Lion Investment to the China Arts & Crafts Companies will be off-set against the total consideration amount. Moreover, Shanghai Lion Investment will be entitled to dividends attributable to the 44% Interest which is declared between the date of the Preliminary Framework Agreement and the date of completion of the Possible Acquisition on a pro-rata basis, to be calculated by dividing the amount of the Deposit paid over the final price of the Possible Acquisition.

(iii) *When the Deposit will be refunded*

In the event that the transfer of the 44% Interest is not effected for any of the following reasons:

- (i) If Shanghai Lion Investment terminates the Preliminary Framework Agreement because:
  - (a) it disagrees with the result of the valuation; or
  - (b) any Conditions is not satisfied within 180 days of the signing of the Preliminary Framework Agreement (or such later date as may be approved by Shanghai Lion Investment);
- (ii) failure to obtain the PRC regulatory approvals;
- (iii) failure to obtain the approval from the Shareholders (if required);
- (iv) failure to obtain the board approval of Beijing Parkson with respect to such transfer (except in circumstances where the Beijing Parkson's board approval was not obtained because the directors appointed by the China Arts & Crafts Companies have not voted in favour of the transfer);

the Company will be entitled to the refund of the Deposit paid, together with accrued interest, but not the Liquidated Damages (as defined below). Interest will be calculated at the one-year base rate of interest (currently at 5.58%) for financial institutions to lend out RMB loans, as published by the People's Bank of China from time to time. We consider it fair and reasonable to the Independent Shareholders that the accrued interest shall be calculated at the market rate.

In the event that the transfer of the 44% Interest is not effected for reasons other than those mentioned above (e.g., if the bid is awarded to a third party or if the public tender process is unilaterally terminated by China Arts & Crafts) ("Liquidated Damages Events"), the Company will be entitled to the refund of the Deposit paid (together with the accrued interest at the same rate as mentioned above) and liquidated damages of an amount representing 20% of such amount of the Deposit that has been paid (the "Liquidated Damages").

(iv) *Security for the Deposit*

- (a) The Initial Deposit

The Group has paid the China Arts & Crafts Companies the Initial Deposit of RMB50 million pursuant to the Preliminary Framework Agreement. As security for the refund of the Initial Deposit, the China Arts & Crafts Companies have on 23 January 2006 issued to Shanghai Lion Investment an enforcement-of-debt undertaking (the "Undertaking"). The Undertaking is a notarised document and will entitle Shanghai Lion Investment to petition

to the relevant PRC court for enforcement of debt in case the China Arts & Crafts Companies fail to refund the Deposit, without having to first apply to the court for judgement of the existence and amount of the liabilities. It was agreed between the parties that the Undertaking will be replaced by the Share Pledge (which has also been executed on 23 January 2006) once the Share Pledge is approved by MOC and registered with the relevant PRC authorities and the entire process normally takes about 30 to 60 days. The approval and registration process is currently in progress and in the event that the China Arts & Crafts Companies fail to obtain the requisite MOC approval for, and registration of, the Share Pledge within 45 days (or such later date as Shanghai Lion Investment may specify if the delay is resulted from MOC requiring more time for the approval process) from the date of the Preliminary Framework Agreement and are unable to repay the Initial Deposit (for which the China Arts & Crafts Companies are jointly and severally liable) within the time specified under the Undertaking, Shanghai Lion Investment will have the right to apply to the relevant PRC court to order the China Arts & Crafts Companies to repay the Initial Deposit. In the event that the China Arts & Crafts Companies fail to comply with the court order, the relevant PRC court could order to put any of the China Arts & Crafts Companies' assets (including the 44% Interest) for sale by public tender. Shanghai Lion Investment may participate in the process of public tender. Any of such sale proceeds (the "Sale Proceeds") would be used to first repay the Initial Deposit to Shanghai Lion Investment except (i) if the assets that are put up for public tender are secured assets; in that circumstances, any sale proceeds will be first applied to repay the mortgagee or pledgee. In this respect, the China Arts & Crafts Companies have warranted in the Share Pledge that the 44% Interest is not subject to any encumbrances; and (ii) if there are other creditors of China Arts & Crafts Companies who have obtained the effective legal documents (including court judgements) and have successfully applied to the court to share the Sale Proceeds before completion of the enforcement procedures. In this respect, Shanghai Lion Investment would have the benefit of time as with a notarised Undertaking, Shanghai Lion Investment is not required to go through the court procedure to obtain a court judgement in respect of the liabilities of the China Arts & Crafts Companies which is expected to be time consuming.

China Arts & Crafts is principally engaged in the business of international trading, retail, exhibition and trading of special commodities such as arts and crafts. China Arts & Crafts Culture and Arts & Crafts Exhibition are wholly-owned subsidiaries of China Arts & Crafts. China Arts & Crafts Culture is principally engaged in the business of cultural consultation and trading of arts and crafts whilst Arts & Crafts Exhibition is principally engaged in the business of exhibition and trading of arts and crafts and ornaments. To the knowledge of the executive Directors and management of the Company, the China Arts & Crafts Companies is part of an established and reputable group and are also state-owned enterprises. The Company believes that the China Arts & Crafts Companies would be able to honour their obligations under the Undertaking.

In addition, Shanghai Lion Investment will have the right to receive from Beijing Parkson, by way of deduction from the dividends (the “Right of Withholding Dividends”) to which the China Arts & Crafts Companies are otherwise entitled and from the financial year of 2006, such amounts which represent the Deposit paid by Shanghai Lion Investment (together with the accrued interest) and the Liquidated Damages (as the case may be). However, in the event that the China Arts & Crafts Companies fail to comply with its obligations under the Undertaking, it is not likely that Beijing Parkson would declare dividends as any declaration of dividend would require unanimous board approval of Beijing Parkson. However, Shanghai Lion Investment may still rely on the other security arrangements as provided in the Preliminary Framework Agreement.

(b) the Deposit

As mentioned above, the Share Pledge has been executed and the approval and registration process for the Share Pledge is currently in progress. Upon receipt of the approval and registration with the relevant PRC authorities, the Share Pledge will become effective and the Undertaking will cease to be of effect. The Group has to pay the remaining balance of the Deposit in the sum of RMB60 million to the China Arts & Crafts Companies within two business days upon registration of the Share Pledge. The obligations of the China Arts & Crafts Companies to pay the refund of the Deposit (together with the accrued interest) and the Liquidated Damages (as the case may be) pursuant to the terms of the Preliminary Framework Agreement will be secured by the Share Pledge which will entitle Shanghai Lion Investment to put up the 44% Interest for public tender. In those circumstances, Shanghai Lion Investment may participate in that public tender. The Share Pledge does not cover voting rights attaching to the 44% Interest as the China Arts & Crafts Companies will not agree to such term. However, as the Group has 4 board representatives (out of a total of 7 board members) in Beijing Parkson, we do not consider the Group’s interest would be materially weakened by the fact that the Share Pledge does not cover such voting rights. Shanghai Lion Investment will remain entitled to the Right of Withholding Dividends for the purpose of recovering any amount of the Deposit paid (together with the accrued interest) and the Liquidated Damages, if Beijing Parkson declares any dividend in the financial year of 2006 and afterwards.

The Company has been advised by its PRC legal advisers, Jingtian & Gongcheng, that the Undertaking and the Share Pledge (if approved and registered) are both valid and legally enforceable under the PRC laws.

The Share Pledge provides better protection to the Group as it gives Shanghai Lion Investment a direct right to put up the 44% Interest for public tender in the event that China Arts & Crafts Companies fail to pay the refund of the Deposit (together with the accrued interest) and the Liquidated Damages (as the case may be) to Shanghai Lion Investment in accordance with the terms of the Preliminary Framework Agreement.

The Undertaking and Share Pledge do not in themselves entitle the Company to acquire the 44% Interest. Sale of the 44% Interest is subject to public tender and approval procedures and it is uncertain whether the Group can win the bid. Nevertheless, any sale proceeds from the public tender would be first applied to repay Shanghai Lion Investment (except in circumstances as discussed above).

In assessing the recoverability of the Deposit, accrued interest and Liquidated Damages, we have analysed the security given for the Deposit. The sale of the 44% Interest will be subject to a public tender process. Hence, the sale price for the 44% Interest as a business concern is not known for the time being. Having considered the earnings potential of Beijing Parkson, we are of the view that the value of the 44% Interest would be substantial. We have also considered the assets backing of Beijing Parkson. As mentioned above, the 44% Interest in Beijing Parkson has an attributable Adjusted NAV of approximately RMB255 million. Beijing Parkson's major asset is its property interests in the main wing of the flagship Beijing store and the Directors believe it to be a quality asset. We also understand from the management of the Company that Beijing Parkson generates strong cashflows from operation. Based on the unaudited balance sheet of Beijing Parkson as at 30 June 2005, Beijing Parkson had cash on hand of approximately RMB165.7 million, of which approximately RMB72.9 million is attributable to the 44% Interest. In view of the above, we consider that the security given pursuant to the Preliminary Framework Agreement is adequate.

### DISCUSSION AND ANALYSIS

The Possible Acquisition has important strategic value to the Group. Beijing Parkson is a major revenue and profit contributor to the Group. The Possible Acquisition would enable the Group to capture the benefits from the continued growth of the domestic retail industry. The Board considers that the Possible Acquisition of the remaining 44% Interest would enhance the growth and profitability of the Group. However, the Possible Acquisition is subject to a valuation and bidding process and requires approvals from relevant PRC authorities. In the circumstances, the Directors are of the view that it is in the interest of the Group to enter into the Preliminary Framework Agreement in order to commit the China Arts & Crafts Companies to initiating the PRC approval process which may lead to the Possible Acquisition. The 44% Interest is subject to public bidding and it is currently uncertain whether the Possible Acquisition could eventually materialise.

The terms of the Preliminary Framework Agreement would necessitate the Group paying a refundable Deposit of RMB110 million (or RMB50 million before the Share Pledge becomes effective). The obligations of the China Arts & Crafts Companies to pay the refund of the Deposit (together with the accrued interest) and the Liquidated Damages are adequately secured by the China Arts & Crafts Companies' economic interests in Beijing Parkson.

The Possible Acquisition is subject to valuation, a public tender process and other necessary approval which will take some time. However, the Group is reasonably compensated for locking up the Deposit as in any circumstances, refund of the Deposit will be on interest-bearing basis. In addition, the Group may at any time within 180 days terminates the Preliminary Framework Agreement under circumstances as provided in the Preliminary Framework Agreement and be entitled

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## LETTER FROM SOMERLEY

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to the refund of the Deposit. In circumstances where the transfer of the 44% Interest to Shanghai Lion Investment cannot be effected and where such failure to effect the transfer is due to the Liquidated Damages Events, the Group would also be entitled to an amount representing 20% of the Deposit paid as Liquidated Damages. If Shanghai Lion Investment wins the bid for the 44% Interest, the Deposit paid will be off-set against the consideration for the Possible Acquisition. In addition, Shanghai Lion Investment will also be entitled to dividends attributable to the 44% Interest that is declared between the date of the Preliminary Framework Agreement and completion of the Possible Acquisition on a pro-rata basis.

### RECOMMENDATION

Based on the above principal factors and reasons and taking these factors and reasons as a whole as summarised in the section headed “Discussion and Analysis” above, we consider the terms of the Preliminary Framework Agreement are fair and reasonable to the Independent Shareholders and the entering into of the Preliminary Framework Agreement in the interests of the Company and the Shareholders as a whole.

If a general meeting of the Shareholders is to be held for the purpose of considering and, if thought fit, approving the Preliminary Framework Agreement, we would recommend the Independent Shareholders to vote in favour of the ordinary resolution in respect of approving the Preliminary Framework Agreement.

Yours faithfully,  
for and on behalf of  
**SOMERLEY LIMITED**  
**Mei H. Leung**  
*Deputy Chairman*

RESPONSIBILITY STATEMENT

This circular includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Company. The Directors collectively and individually accept full responsibility for the accuracy of the information contained in this circular and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief, there are no other facts the omission of which would make any statement in this circular misleading.

DISCLOSURE OF INTERESTS

Directors and chief executive of the Company

(i) As at Latest Practicable Date, the interests and short positions of the Directors and chief executive of the Company in the shares, underlying shares and/or debentures (as the case may be) of the Company or any its associated corporations (within the meaning of the SFO) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which any such Director or chief executive is taken or deemed to have under such provisions of the SFO) or which were required to be entered into the register required to be kept by the Company under section 352 of the SFO or which were otherwise required to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers in the Listing Rules, were as follows:

(a) *Long positions of Tan Sri Cheng Heng Jem in the share capital of the Company:*

Name of corporation	Nature of Interest	Name of registered owner	Name of beneficial owner	Number and class of securities	Approximate percentage of shareholding
Company	Corporate interest	PRG Corporation <sup>1</sup>	PRG Corporation	361,560,000 ordinary shares	65.50%

*Note:*

1.
- Tan Sri Cheng Heng Jem, together with his wife, Puan Sri Chan Chau Ha, through their direct interest and a series of companies in which they have a substantial interest, are entitled to exercise or control the exercise of more than one third of the voting power at general meetings of LDHB. Since LDHB is entitled to exercise or control the exercise of 100% of the voting power at general meeting of PRG Corporation, pursuant to the SFO, he is deemed to be interested in the Shares held by PRG Corporation in the Company.

(b) *Long positions of Tan Sri Cheng Heng Jem in the share capital of the Company’s associated corporations (as defined in the SFO):*

Name of associated corporation	Nature of Interest	Name of registered owner	Name of beneficial owner	Number and class of securities	Approximate percentage of shareholding
PRG Corporation	Corporate interest	LDHB	LDHB	1 ordinary share	100%
Lion Mahkota Parade Sdn. Bhd.	Corporate interest	LDH Management Sdn. Bhd.	LDH Management Sdn. Bhd.	400,000 preference shares	100%
LDHB	Beneficial interest and corporate interest	Tan Sri Cheng Heng Jem and a series of controlled corporations	Tan Sri Cheng Heng Jem and a series of controlled corporations	416,392,561 ordinary shares	62.31% <sup>1</sup>

*Note:*

1. This represents Tan Sri Cheng Heng Jem’s interest as at the Latest Practicable Date. This figure will increase if any of the debentures referred in sub-paragraph (c) below are converted into shares in LDHB.

The following are the associated corporations (as defined in the SFO) of the Company in which Tan Sri Cheng Heng Jem is deemed interested solely as a result of his controlling interest in LDHB (the figures in brackets represent LDHB’s interests in these corporations): Qingdao No. 1 (52.60%), Hamba Research & Development Co., Ltd. (98%), Nanning Brilliant (51%), Dalian Tianhe (60%), Aktif-Sunway Sdn. Bhd. (80%) and Inner Mongolia Leader (25%).

In relation to the following associated corporations (as defined in the SFO) of the Company which are non wholly-owned subsidiaries of LDHB, Tan Sri Cheng Heng Jem is also deemed interested in the remaining minority interest in those corporations as follows:

Name of associated corporation	LDHB’s interest	Additional deemed interest
Lion Mahkota Parade Sdn. Bhd. <sup>D</sup>	99.99%	0.01% <sup>A</sup>
Likom CMS Sdn. Bhd.	99.98%	0.02% <sup>B</sup>
LDH Investment Pte. Ltd.	60%	40% <sup>C</sup>



*Notes:*

- A. Corporate interest through Ayer Keroh Resort Sdn. Bhd. Tan Sri Cheng Heng Jem, through a series of companies in which he has a substantial interest, is entitled to exercise or control the exercise of more than one third of the voting power at general meetings of this company. Accordingly, he is deemed to be interested in the shares held by Ayer Keroh Resort Sdn. Bhd. in Lion Mahkota Parade Sdn. Bhd.
- B. Corporate interest through Likom Computer Systems Sdn. Bhd.. Tan Sri Cheng Heng Jem is entitled to exercise or control the exercise of more than one third of the voting power at general meetings of this company. Accordingly, he is deemed to be interested in the shares held by Likom Computer Systems Sdn. Bhd. in Likom CMS Sdn. Bhd.
- C. Corporate interest through Lion Asia Investment Pte. Ltd. Tan Sri Cheng Heng Jem, through a series of companies in which he has a substantial interest, is entitled to exercise or control the exercise of more than one third of the voting power at general meetings of this company. Accordingly, he is deemed to be interested in the shares held by Lion Asia Investment Pte. Ltd. in LDH Investment Pte. Ltd.
- D. Interest refers to the class of ordinary shares of Lion Mahkota Parade Sdn. Bhd. Interest in the class of preference shares is disclosed in preceding table under sub-paragraph (b) above.

(c) *Long Positions of Tan Sri Cheng Heng Jem in the debentures of the Company and its associated corporations (as defined in the SFO):*

Through beneficial and corporate interests, Tan Sri Cheng Heng Jem is deemed to be interested in 99.35% of the RM49.9 million 2% redeemable convertible unsecured loan stock due 31 May 2009 issued by LDHB (“RCULS”) as follows:

- corporate interest<sup>1</sup> (through Amsteel Corporation Berhad) in 94.62% of the RCULS;
- corporate interest<sup>2</sup> (through Lion Industries Corporation Berhad) in 4.73% of the RCULS.

In addition, Tan Sri Cheng Heng Jem has a beneficial interest in the RCULS held by Amsteel Corporation Berhad and Lion Industries Corporation Berhad (amounting in aggregate to 72.14% of the RCULS in issue) as follows:

- option granted by Amsteel Corporation Berhad to Tan Sri Cheng Heng Jem to acquire 68.70% of the RCULS held by Amsteel Corporation Berhad;
- option granted by Lion Industries Corporation Berhad to Tan Sri Cheng Heng Jem to acquire 3.44% of the RCULS.

The above options are and will remain exercisable until 15 December 2006.

Through corporate interest, Tan Sri Cheng Heng Jem is interested in 99.99% of the RM9.44 million 2% irredeemable convertible unsecured loan stock due 31 May 2009 issued by LDHB (“ICULS”) as follows:

- corporate interest<sup>3</sup> (through Narajaya Sdn. Bhd.) in 99.99% of the ICULS.

*Notes:*

1. Corporate interest through Amsteel Corporation Berhad. Tan Sri Cheng Heng Jem is entitled to exercise or control the exercise of more than one third of the voting power at general meetings of this company. Accordingly, Tan Sri Cheng Heng Jem is interested in the RCULS held by Amsteel Corporation Berhad.
2. Corporate interest through Lion Industries Corporation Berhad. Tan Sri Cheng Heng Jem is entitled to exercise or control the exercise of more than one third of the voting power at general meetings of this company. Accordingly, Tan Sri Cheng Heng Jem is interested in the RCULS held by Lion Industries Corporation Berhad.
3. Corporate interest through Narajaya Sdn. Bhd. Tan Sri Cheng Heng Jem is entitled to exercise or control the exercise of more than one third of the voting power at general meetings of this company. Accordingly, Tan Sri Cheng Heng Jem is interested in the ICULS held by Narajaya Sdn. Bhd.
4. The percentage figures given above with respect to the RCULS and the ICULS are as at the Latest Practicable Date. These figures will change upon the exercise of any of these debentures.

Save as disclosed in this circular, as at the Latest Practicable Date, none of the Directors or chief executives of the Company had any interests or short positions in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO) which are required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provisions of the SFO), or are required, pursuant to Section 352 of the SFO, to be entered in the register referred to therein, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers.

- (ii) As at the Latest Practicable Date, none of the Directors had any direct or indirect interest in any assets which have since 30 June 2005 (being the date to which the latest published audited financial statements of the Company were made up) been acquired or disposed of by or leased to any member of the Group, or are proposed to be acquired or disposed of by or leased to any member of the Group.

Substantial shareholders of the Group

As at Latest Practicable Date, so far as the Directors are aware, each of the following persons, not being a Director or chief executive of the Company, had an interest in the Company’s shares which falls to be disclosed to the Company and the Stock Exchange under the provisions of Division 2 and 3 of Part XV of the SFO:

Name of shareholder	Nature of interest	Percentage of shareholding	
		Number of shares	(direct or indirect)
PRG Corporation	Beneficial	361,560,000	65.50%
LDHB	Corporate	361,560,000 (Note 2)	65.50%
Tan Sri Cheng Heng Jem	Corporate	361,560,000 (Note 3)	65.50%
Puan Sri Chan Chau Ha alias Chan Chow Har (Note 4)	Interest of spouse	361,560,000	65.50%
Lion Development (Penang) Sdn. Bhd.	Corporate	361,560,000 (Note 5)	65.50%
Pangkor Investments (Cayman Islands) Limited	Beneficial	54,648,000	9.9%
Khazanah Nasional Berhad	Corporate	54,648,000 (Note 6)	9.9%

Notes:

- All of the above are long positions.
- PRG Corporation is a wholly-owned subsidiary of LDHB. By virtue of the SFO, LDHB is deemed to be interested in the Shares held by PRG Corporation in the Company.
- Tan Sri Cheng Heng Jem together with his wife, Puan Sri Chan Chau Ha, through their direct interest and a series of companies wherein they have a substantial interest, is entitled to exercise or control the exercise of more than one third of the voting power at general meetings of LDHB. Since LDHB is entitled to exercise or control the exercise of 100% of the voting power at general meetings of PRG Corporation, by virtue of the SFO, Tan Sri Cheng Heng Jem is deemed to be interested in the Shares held by PRG Corporation in the Company.
- Puan Sri Chan Chau Ha is the wife of Tan Sri Cheng Heng Jem and is deemed to be interested in 361,560,000 Shares which Tan Sri Cheng Heng Jem is deemed to be interested in for the purposes of the SFO.
- Lion Development (Penang) Sdn. Bhd., directly and through a series of controlled companies, is entitled to exercise or control the exercise of more than one third of the voting power at general meetings of LDHB. Since LDHB is entitled to exercise or control the exercise of 100% of the voting power at general meetings of PRG Corporation, by virtue of the SFO, Lion Development (Penang) Sdn. Bhd. is deemed to be interested in the Shares held by PRG Corporation in the Company.

6. Pangkor Investments (Cayman Islands) Limited is a wholly-owned subsidiary of Khazanah Nasional Berhad. As such Khazanah Nasional Berhad is deemed to be interested in the 54,648,000 Shares held by Pangkor Investments (Cayman Islands) Limited for the purposes of the SFO.

As at Latest Practicable Date, so far as the Directors are aware, each of the following persons, not being a Director or chief executive of the Company, was directly or indirectly interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any other member of the Group:

Substantial Shareholder	Member of the Group	Percentage of equity interest held
China Arts & Crafts	Beijing Parkson	44%
Xinjiang Youhao	Xinjiang Parkson	49%
Wuxi Distribution	Wuxi Parkson	40%
Yangzhou Commercial	Yangzhou Parkson	45%
Shaanxi Chang'an Information <sup>1</sup>	Xi'an Chang'an Parkson	49%
Xi'an Xinrun <sup>2</sup>	Xi'an Shidai Parkson	49%
Sichuan Fulin <sup>3</sup>	Mianyang Parkson	40%
Chongqing Wanyou	Chongqing Parkson	30%
Guizhou Shenqi Enterprise <sup>4</sup>	Guizhou Parkson	40%
Anshan Tianxing <sup>5</sup>	Anshan Parkson	49%
Shanghai Nine Sea Industry	Shanghai Lion Property	71% <sup>6</sup>
Shanghai Nine Sea Industry	Shanghai Nine Sea Parkson	29% <sup>6</sup>

Notes:

1. 長安信息(產業)集團股份有限公司 (Chang'an Information (Property) Group Holding Company Limited), a PRC joint stock company, the shares of which are being listed on the Shanghai Stock Exchange owns 65.45% of the equity interest of Shaanxi Chang'an Information, representing a 32.07% indirect equity interest in Xi'an Chang'an Parkson.
2. 陝西雙翼石油化工有限責任公司 (Shaanxi Shuangyi Petroleum and Chemical Company Limited) owns 39.1% of the equity interest in Xi'an Xinrun, representing a 19.16% indirect equity interest in Xi'an Shidai Parkson.
3. 安治富 (An Zhifu) owns 51% of the equity interest in Sichuan Fulin, representing a 20.40% indirect equity interest in Mianyang Parkson.
4. 張沛 (Zhang Pei), 張之君 (Zhang Zhi Jun) and 張姪 (Zhang Ya) own 30%, 40% and 30% of the equity interest in Guizhou Shenqi Enterprise, respectively, representing a 12%, 16% and 12% indirect equity interest in Guizhou Parkson.
5. Each of 鞍山市金羽經貿有限公司 (Anshan City Jinyu Jingmao Company Limited) and 香港貿明有限公司 (Praise Shine Company Limited) owns 50% of the equity interest in Anshan Tianxing, representing 24.5% indirect equity interest in Anshan Parkson.
6. Shanghai Lion Property and Shanghai Nine Sea Parkson are cooperative joint venture enterprises established under the laws of the PRC. The percentages are calculated based on the voting rights attributable to Shanghai Nine Sea Industry pursuant to the respective co-operative joint venture contracts. The percentages to distributable profits are different.

Mr. Cheng Yoong Choong and Mr. Chew Fook Seng are directors of PRG Corporation, which is a company which has an interest or short position in the shares and underlying shares of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO. Save as disclosed in this circular and so far as the Directors are aware, as at the Latest Practicable Date, no other person had an interest or short position in the Company's shares or underlying shares (as the case may be) which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO, or was otherwise directly or indirectly interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the Group.

## **DIRECTORS' INTEREST IN CONTRACT**

As at Latest Practicable Date, none of the Directors was materially interested in any contract or arrangement entered into by the Company subsisting as at the date of this circular which is significant in relation to the business of the Group.

## **SERVICE CONTRACTS**

Each of Mr. Cheng Yoong Choong and Mr. Chew Fook Seng has entered into a service contract with the Company on 9 November 2005 under which they agreed to act as executive Directors for a term of three years commencing from 9 November 2005. The appointment may be terminated before such expiry by not less than three months' written notice.

Under these service contracts, Mr. Cheng Yoong Choong will receive an annual Director's fee of approximately HK\$150,000. Mr. Chew Fook Seng will receive an initial annual salary of RMB 1,273,440. The annual salary may, subject to the discretion of the Board and the remuneration committee of the Company, be increased. Mr. Chew Fook Seng will also receive an annual Director's fee of HK\$150,000. Each of the executive Directors will also be entitled to a discretionary bonus as may be decided by the remuneration committee. The amount of the annual salary increment and the bonus payable under such service contracts are at the discretion of the board of Directors and the remuneration committee, provided that the respective parties to such service contracts shall abstain from voting and not be counted in the quorum in respect of any such determination of the board of Directors in relation to him.

Tan Sri Cheng Heng Jem has signed a letter of appointment dated 9 November 2005 with the Company under which he agreed to act as the non-executive Director for a period of three years commencing from 9 November 2005. The appointment may be terminated before such expiry by not less than three months' written notice. The initial annual Director's fee for the non-executive Director is HK\$150,000.

Each of Mr. Fong Ching, Eddy, Mr. Studer Werner Josef, Mr. Ko Tak Fai, Desmond has signed a letter of appointment dated 9 November 2005 with the Company under which they agreed to act as independent non-executive Directors for a period of one year and shall continue thereafter subject to a maximum of three years unless terminated in accordance with the terms of the appointment letters. The initial annual Director's fee for each independent non-executive Director is HK\$150,000.

As at the Latest Practicable Date, save as disclosed in this circular, none of the Directors of the Company had any existing or proposed service contract with any member of the Group (excluding contracts expiring or determinable by the Company within one year without payment of compensation (other than statutory compensation)).

DIRECTORS’ INTERESTS IN COMPETING BUSINESSES

As at the Latest Practicable Date, none of the Directors and directors of the Company’s subsidiaries, or their respective associates had interests in businesses, other than being a director of the Company and/or its subsidiaries and their respective associates, which compete or are likely to compete, either directly or indirectly, with the businesses of the Company and its subsidiaries as required to be disclosed pursuant to the Listing Rules, except for the interests held by Tan Sri Cheng Heng Jem in LDHB which owns 11 department stores in the PRC. These 11 excluded department stores are managed by the Group.

NO MATERIAL ADVERSE CHANGE

At the Latest Practicable Date, none of the Directors was aware of any material adverse change in the financial or trading position of the Group since 30 June 2005 (being the date to which the latest published audited financial statements of the Group were made up).

EXPERTS

- (a) The following sets out the qualifications of Somerley which has given its opinion or advice as contained in this circular:

Name	Qualifications
Somerley Limited	A corporation licensed under the SFO to conduct types 1 (dealing in securities), 4 (advising on securities), 6 (advising on corporate finance) and 9 (asset management) regulated activities and the independent financial adviser to the Independent Board Committee and the Independent Shareholders
Jingtian & Gongcheng	Registered law firm in the PRC

- (b) Each of Somerley and Jingtian & Gongcheng does not have any shareholding, direct or indirect, in any member of the Group or any right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Group.
- (c) Each of Somerley and Jingtian & Gongcheng does not have any interest, direct or indirect, in any assets which have been acquired or disposed of by or leased to any member of the Group, or which are proposed to be acquired or disposed of by or leased to any member of the Group since 30 June 2005, the date to which the latest published audited financial statements of the Company were made up.

- (d) Each of Somerley and Jingtian & Gongcheng has given and has not withdrawn its written consent to the issue of this circular with the inclusion of its letter (in the case of Somerley) and references to its name in the form and context in which they are included.
- (e) The letter and recommendation given by Somerley and the advice given by Jingtian & Gongcheng are given as of the date of this circular for incorporation herein.

**LITIGATION**

No member of the Group is at present engaged in any litigation or arbitration of material importance to the Group and no litigation or claim of material importance to the Group is known to the Directors or the Company to be pending or threatened by or against any member of the Group.

**MISCELLANEOUS**

- (a) The English text of this circular shall prevail over the Chinese text.
- (b) The registered office of the Company is situated at c/o M&C Corporate Services Limited, P.O. Box 309GT, Ugland House, South Church Street, George Town, Grand Cayman, Cayman Islands.
- (c) The head office and principal place of business of the Company is situated at 9th Floor, Parkson Plaza, No.101 Fuxingmennei Avenue, Xicheng District, Beijing 100031, PRC.
- (d) The principal place of business of the Company in Hong Kong is situated at Level 28, Three Pacific Place, 1 Queen's Road East, Hong Kong.
- (e) The Hong Kong share registrar and transfer office of the Company is Tricor Investor Services Limited, 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong.
- (f) The secretary of the Company is Ms. Seng Sze Ka Mee, Natalia, who is a Fellow of The Institute of Chartered Secretaries and Administrators (FCIS), The Hong Kong Institute of Chartered Secretaries (FCS), and The Hong Kong Institute of Directors (FHKIoD).
- (g) The qualified accountant of the Company is Mr. Wong Kang Yean Clarence, who is a registered member of the Association of Chartered Certified Accountants and a chartered accountant with the Malaysian Institute of Accountants.

**DOCUMENTS AVAILABLE FOR INSPECTION**

Copies of the following documents are available for inspection at the principal place of business in Hong Kong of the Company at Level 28, Three Pacific Place, 1 Queen's Road East, Hong Kong during normal business hours from the date of this circular up to and including 2 March 2006:

- (a) the Preliminary Framework Agreement;
- (b) the enforcement-of-debt undertaking;
- (c) the instruction letter;
- (d) the Share Pledge;
- (e) the service contracts and letters of appointments referred to in the section headed "Service Contracts";
- (f) the memorandum and articles of association of the Company;
- (g) the letter from the Independent Board Committee, the text of which is set out on page 22 of this circular;
- (h) the letter from Somerley to the Independent Board Committee and the Independent Shareholders, the text of which is set out on pages 23 to 36 of this circular; and
- (i) the written consent referred to under the paragraph headed "Expert" in this appendix; and
- (j) the written approval of PRG Corporation dated 15 February 2006 approving the Preliminary Framework Agreement.