China Essence Group Ltd.
嵩天集团有限公司

(the "**Company**")
(Incorporated in the Cayman Islands)
(Registration No. CT-152302)

JOINT AUDITORS' DISCLAIMER OF OPINION ON FINANCIAL STATEMENTS FOR THE FINANCIAL YEAR ENDED 31 MARCH 2014

The Board of Directors of China Essence Group Ltd (the "Company", or together with its subsidiaries, the "Group") wishes to announce that the Company's Independent Joint Auditors, Messrs BDO LLP, Public Accountants and Chartered Accountants, Singapore and Messrs BDO Limited, Certified Public Accountants, Hong Kong have issued their report with a disclaimer of opinion on the Group's financial statements for the financial year ended 31 March 2014.

A copy of the Independent Joint Auditors' Report together with Note 3.2 to the financial statements is annexed to this announcement.

By Order of the Board

Zhao Libin
Executive Chairman and Chief Executive Officer
4 July 2014

INDEPENDENT JOINT AUDITORS' REPORT

To the Shareholders of China Essence Group Ltd.
(incorporated in the Cayman Islands with limited liability)

We were engaged to audit the financial statements of China Essence Group Ltd. (the "Company") and its subsidiaries (together the "Group") set out on pages 41 to 91, which comprise the consolidated statement of financial position of the Group and the statement of financial position of the Company as at 31 March 2014, and the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows of the Group and the statement of changes in equity of the Company for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' Responsibility for the Financial Statements

The directors of the Company are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards, and for such internal control as directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on conducting the audit in accordance with International Standards on Auditing. Because of the matters described in the Basis for Disclaimer of Opinion paragraphs, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for Disclaimer of Opinion

i) **Impairment of the Group's property, plant and equipment, land use rights and long term deposits and the Company's interests in subsidiaries and amounts due from subsidiaries and determination of carrying amount of the Group's deferred tax assets**

(a) **The Group's property, plant and equipment and land use rights and the Company's interests in subsidiaries**

As at 31 March 2014, included in the consolidated statement of financial position of the Group are property, plant and equipment and land use rights of approximately RMB449,272,000 and RMB246,050,000 respectively, and included in the statement of financial position of the Company are interests in subsidiaries of approximately RMB29,739,000. And for the year ended 31 March 2014, impairment loss on property, plant and equipment of approximately RMB230,000,000 is charged to the Group's consolidated statement of comprehensive income and impairment loss on interests in subsidiaries of approximately RMB6,674,000 is charged to the Company's profit or loss. For the purpose of assessing impairment of the Group's property, plant and equipment and land use rights and the Company's interests in subsidiaries, the management has prepared a discounted cash flow to determine the value in use of these assets based on the profit and cash flow forecasts (the "Forecasts") as detailed in note 13 to the financial statements.

(b) **The amounts due from subsidiaries of the Company**

As at 31 March 2014, included in the statement of financial position of the Company are amounts due from subsidiaries of approximately RMB513,414,000. For the purpose of assessing impairment of amounts due from subsidiaries of the Company, the management has carried out an impairment assessment with reference to the expected repayment ability of the subsidiaries which in turn is based on the Forecasts.

(c) **The Group's long term deposits**

As at 31 March 2014, included in the consolidated statement of financial position of the Group are long term deposits for the purchase of machinery and equipment of approximately RMB16,030,000 which are non-refundable and non-transferable in nature. The management has carried out an assessment on the Group's requirement of additional production capacity and on the Group's ability for funding the remaining amount of the purchase consideration in order to substantiate the carrying amount of the long term deposits as at 31 March 2014.

i) **Impairment of the Group's property, plant and equipment, land use rights and long term deposits and the Company's interests in subsidiaries and amounts due from subsidiaries and carrying amount of the Group's deferred tax assets - Continued**

(d) The Group's deferred tax assets

As at 31 March 2014, included in the consolidated statement of financial position of the Group are deferred tax assets of approximately RMB11,577,000. The management has carried out an assessment on the sufficiency of the estimated future taxable profits of the Group with reference to the Forecasts against which the deferred tax assets could be realised in order to substantiate the carrying amount of the deferred tax assets as at 31 March 2014.

However, as further explained in point (ii) below, we were not provided with sufficient evidence from the management regarding the reasonableness of the assumptions made (including the estimated amount of cash inflows that would be generated from the Group's operation in view of the Group's present scale of operation and the Group's ability to secure the necessary funding to expand its operating scale to generate the estimated amount of cash inflows) and the discount rate applied (for the value in use calculation) in the Forecasts (the "Assumptions").

There were no other satisfactory audit procedures that we could perform in order to satisfy ourselves that the Assumptions have been properly determined and therefore the impairment losses recognised for the year and the carrying amounts of the assets of (a) to (d) above as at 31 March 2014 have been fairly stated. Any adjustments considered necessary to the carrying amounts of the Group's property, plant and equipment, land use rights, long term deposits and deferred tax assets and the Company's interests in subsidiaries and amounts due from subsidiaries would have a consequential effect on the Group's consolidated statement of financial position as at 31 March 2014 and the Group's loss and total comprehensive income for the year ended 31 March 2014 and the Company's statement of financial position as at 31 March 2014 and the Company's loss and total comprehensive income for the year ended 31 March 2014, respectively.

ii) **Going concern**

The following circumstances give rise to uncertainties as to the appropriateness of the use of the going concern assumption in the preparation of the financial statements of the Group for the current year:

(a) there have been significant adverse changes in the business environment and operating conditions of the Group, and the Group incurred a significant loss amounting to approximately RMB279,268,000, RMB555,686,000 and RMB661,622,000 for three consecutive years ended 31 March 2014;

(b) as at 31 March 2014, the Group's current liabilities exceeded its current assets by approximately RMB844,830,000 and the Group had net liabilities and capital deficiency of RMB121,901,000;

(c) for the year ended 31 March 2014, the Company incurred a loss of approximately RMB35,790,000 and, as at that date, the Company's current liabilities exceeded its current assets (excluding the amounts due from subsidiaries as mentioned in point (i) (b) above) by approximately RMB446,254,000 and the Company had net liabilities and capital deficiency of approximately RMB446,254,000 (excluding the interests in subsidiaries and the amounts due from subsidiaries as mentioned in point (i) (a) and point (i) (b) above respectively);

(d) the third, fourth and fifth redemption instalments of the convertible bonds of principal amount of HK$100,000,000 (equivalent to approximately RMB79,000,000), in aggregate, and the coupon interest of approximately HK$19,934,000 (equivalent to approximately RMB14,565,000) which are due and payable on 31 December 2012, 30 June 2013 and 31 December 2013, respectively, remain overdue as at 31 March 2014 and as at the date of approval of the financial statements;

(e) on 27 September 2013, the Group has entered into a renewal loan agreement with a PRC bank to renew a borrowing amounting to RMB120,000,000 for one year. As a result, the aggregate amount of all the bank loans arising from PRC banks amounted to RMB500,000,000 which exceeded the limit of RMB450,000,000 set in the Supplemental Trust Deed (as defined in note 25 to the financial statements) of the convertible bonds. This default has not been remedied up to the date of approval of the financial statements;

ii) <u>Going concern - Continued</u>

(f) as a result of the defaults detailed in (d) and (e) above, the bondholders have the rights to serve a notice to the Company that the remaining convertible bonds of principal amount of HK$100,000,000 (equivalent to approximately RMB79,000,000), which will be due for redemption within the next twelve months from 31 March 2014, have become immediately due and payable; up to the date of approval of these financial statements, the Group has not received such notices;

(g) a loan from a bank in Singapore of US$38,500,000 (equivalent to approximately RMB240,012,000) as at 31 March 2014 was matured on 19 December 2012 and became immediately due and payable after the maturity date; and

(h) the other bank borrowings of the Group of RMB500,000,000 and a borrowing of RMB80,000,000 from a third party in the PRC as at 31 March 2014 are due for repayment within the next twelve months from 31 March 2014. Subsequent to the reporting date of 31 March 2014, the Group renewed part of these bank borrowings of RMB280,000,000 upon the maturity of these bank borrowings. As a result, the Group would need financing to settle RMB220,000,000 of the bank borrowings and RMB80,000,000 from the third party when they are due for repayment within the next twelve months from 31 March 2014.

These conditions along with the other matters as explained in note 3.2 to the financial statements indicate the existence of a material uncertainty which may cast significant doubt on the Group's ability to continue as a going concern, and hence whether the Group would be able to realise it assets and discharge its liabilities in the normal course of business. Nevertheless, the management has prepared the financial statements based on the assumption that the Group can be operated as a going concern and are of the view that the Group will have sufficient working capital to finance its operations in the next twelve months from 31 March 2014, after taking into consideration of the financing and business plans and operational measures.

The management has provided us with the Forecasts. However,

1) we were not provided with sufficient evidence from the management that the Group will have sufficient financing resources to satisfy any demand for repayment of the convertible bonds, the loan from a bank in Singapore and the bank and other borrowings which are due for repayment within the next twelve months from 31 March 2014 as mentioned in points (d) to (h) above, and to provide working capital in future;

2) we were not provided with any documentary evidence from the management regarding the status of their negotiations with the banker in Singapore and the bondholders to satisfy ourselves that the defaults will be remedied and that the terms of the bank loan and the convertible bonds will be revised as ongoing negotiations are conducted verbally although no agreement has been reached as at 31 March 2014 and as at the date of our report; and

3) the Forecasts are prepared based on the Group's financing and business plans. However, there is a lack of evidence in resolving the funding requirements as detailed in (1) and (2) above. We were not provided with other evidence or explanation of how the financing and business plans would be achievable in view of the significant adverse changes in business environment and operating conditions of the Group and without the funding requirements having been resolved.

Owing to these limitations on our scope of work, we are unable to obtain sufficient appropriate audit evidence to assess the reasonableness of the Assumptions of the Forecasts and hence whether it is appropriate to use the going concern basis in preparing the financial statements of the Group. There were no other satisfactory audit procedures that we could adopt in this regard.

Should the use of the going concern basis in preparing the financial statements be determined to be inappropriate, adjustments might have to be made to reduce the carrying amounts of assets to their recoverable amounts, to provide for any further liabilities which might arise and to reclassify non-current assets as current assets.

Our independent joint auditors' report on the financial statements of the Group for the previous year ended 31 March 2013 contained a disclaimer of opinion on the appropriateness of going concern assumption of the Group.

INDEPENDENT JOINT AUDITORS' REPORT

To the Shareholders of China Essence Group Ltd.
(incorporated in the Cayman Islands with limited liability)

Disclaimer of Opinion

Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraphs, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the financial statements for the year ended 31 March 2014.

BDO LLP
Public Accountants and
Chartered Accountants
21 Merchant Road
#05-01
Singapore 058267

3 July 2014

BDO Limited
Certified Public Accountants
25th Floor, Wing On Centre
111 Connaught Road Central
Hong Kong

3 July 2014

3.2 Basis of preparation

In preparing the financial statements, the directors considered the operations of the Group as a going concern notwithstanding that:

1. there has been significant adverse changes in the business environment and operating conditions of the Group, the Group incurred a significant loss amounting approximately RMB279,268,000, RMB555,686,000 and RMB661,622,000 for three consecutive years ended 31 March 2014;

2. as at 31 March 2014, the Group's current liabilities exceeded its current assets by approximately RMB844,830,000 (2013: approximately RMB486,450,000) and the Group has net liabilities and capital deficiency of approximately RMB121,901,000 (2013: the Group has net assets and capital of approximately RMB540,665,000);

3. for the year ended 31 March 2014, the Company incurred a loss of approximately RMB35,790,000 (2013: approximately RMB172,436,000) and, as at that date, the Company's current liabilities exceeded its current assets (excluding the amounts due from subsidiaries) by approximately RMB446,254,000 (2013: approximately RMB416,809,000) and the Company had net liabilities and capital deficiency of approximately RMB446,254,000 (2013: approximately RMB416,809,000) (excluding the interests in subsidiaries and the amounts due from subsidiaries);

4. the third, fourth and fifth redemption instalments of the convertible bonds of principal amount totalling of HK$100,000,000 (equivalent to a carrying amount of approximately RMB79,000,000) and the coupon interest of approximately HK$19,934,000 (equivalent to approximately RMB14,565,000) which are due and payable on 31 December 2012, 30 June 2013 and 31 December 2013, respectively, remain overdue as at 31 March 2014 and the date of approval of these financial statements;

5. on 27 September 2013, the Group has entered into a renewal loan agreement with a PRC bank to renew a borrowing amounting to RMB120,000,000 for one year. As a result, the aggregate amount of all the bank loans from PRC banks amounted to RMB500,000,000 which exceeded the limit of RMB450,000,000 set in the Supplemental Trust Deed (as defined in note 25) of the convertible bonds. This default has not been remedied up to the date of approval of these financial statements;

6. as result of the defaults explained in (4) and (5) above, the Bondholders (as defined in note 25) have the rights to serve a notice to the Company that the remaining convertible bonds of principal amount of HK$100,000,000 (equivalent to a carrying amount of approximately RMB79,000,000), which will be due for redemption within the next twelve months from 31 March 2014, have become immediately due and payable up to the date of approval of these financial statements, the Group has not received such notices;

7. a loan from a bank in Singapore of US$38,500,000 (equivalent to approximately RMB240,012,000) as at 31 March 2014 was matured on 19 December 2012 and became immediately due and payable after the maturity date;

8. the other bank borrowings of the Group of RMB500,000,000 and a borrowing of RMB80,000,000 from a third party in the PRC as at 31 March 2014 are due for repayment within the next twelve months from 31 March 2014. Subsequent to the reporting date of 31 March 2014, the Group renewed part of these bank borrowings of RMB280,000,000 upon the maturity of these bank borrowings. As a result, the Group would need financing to settle RMB220,000,000 of bank borrowings and RMB80,000,000 from the third party when they are due for repayment with the next twelve months from 31 March 2014; and

9. Subsequent to 31 March 2014, the Group has not paid the sixth redemption instalment of the convertible bonds of principal amount of HK$40,000,000 as (equivalent to approximately RMB31,600,000) and the coupon interest of approximately HK$2,232,000 (equivalent to approximately RMB1,631,000), which are due and payable on 30 June 2014. These amounts remain overdue as at the date of approval of these financial statements.

These events and conditions indicate the existence of a material uncertainty which may cast significant doubts on the Group's ability to continue as a going concern and hence, its ability to realise its assets and discharge its liabilities in the normal course of business. Nevertheless, the directors prepare the financial statements based on the assumption that the Group can be operated as a going concern and are of the view that the Group will have sufficient working capital to finance its operations in the next twelve months from 31 March 2014, after taking into consideration of the following:

1. the Group is actively exploring the availability of alternative sources of financing and/or refinancing via both money and capital markets;

2. the Group continues (i) to implement various sales strategies to increase the sales turnover and to improve margins of the products and (ii) to implement measures to tighten cost controls over various operating expenses in order to improve its profitability and to generate positive cash inflow from its operations in the future;

3. the Group is actively negotiating with its bankers in the PRC to seek for renewal of the outstanding bank borrowings and to obtain new banking facilities. Subsequent to the reporting date of 31 March 2014, the Group successfully renewed bank borrowings of RMB280,000,000 upon maturity of these bank loans and obtained a new borrowing of RMB100,000,000 from a local lender; and

4. the Group is actively negotiating with its banker in Singapore and the Bondholders to remedy the defaults and to revise the terms of the bank loan and the convertible bonds. The directors are optimistic in reaching agreement with its banker in Singapore and the Bondholders. The directors of the Company believe that the aforementioned financing and business plans and operational measures will be successful, based on the continuous efforts and commitment given by the management

Having regard to the Forecasts (as defined in note 13) of the Group, which are prepared assuming that these measures are successful, the directors of the Company are of the opinion that, in the light of the actions taken to-date, together with the expected results of the other measures in progress, the Group will have sufficient cash resources to satisfy its future working capital and other financing requirements. Should the Group be unable to continue its business as a going concern, adjustments would have to be made in the financial statements to reduce the carrying amounts of the assets to their recoverable amounts, to provide for any further liabilities which might arise, and to reclassify non-current assets as current assets. The effect of these adjustments has not yet been reflected in the financial statements. The financial statements have been prepared under the historical cost basis except for financial instrument classified as derivative financial instrument, which is measured at fair value as explained in the accounting policies set out below. It should be noted that accounting estimates and assumptions are used in the preparation of the financial statements. Although these estimates are based on management's best knowledge and judgement of current events and actions, actual results may ultimately differ from those estimates. The area involving a high degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in note 5.