CHINA EVERBRIGHT WATER LIMITED
Company Registration No.: 34074
(Incorporated in Bermuda)

Responses to Questions on China Everbright Water Limited from Securities Investors Association (Singapore)

The Board of Directors (the "**Board**") of China Everbright Water Limited (the "**Company**") wishes to update shareholders of the Company (the "**Shareholders**") that the Company has received questions from the Securities Investors Association (Singapore) (the "**SIAS**") relating to the Annual Report for the financial year ended 31 December 2018 ("**FY2018**"), which the SIAS wishes that the Company address to the Shareholders. The Company's responses to such questions are set out below.

Question 1

Corporate Strategy and Financial Performance

As highlighted in the chairman's statement, the concept of ecological conservation became a national objective in the People's Republic of China ("PRC") with the establishment of the Ministry of Ecology and Environment in 2018.

On the industry outlook, it was mentioned that an effective implementation of the Water Pollution Prevention and Control Plan (also known as the "Clean Water Action Plan") would give more opportunities in industrial waste water treatment and the upgrading of existing traditional municipal waste water treatment plants.

In the CEO's statement & Business review, revenue and gross profit surged by a third to HK$4.77 billion and HK$1.62 billion respectively. Profit attributable to shareholders also increased by 32% to HK$676 million. The earnings per share for FY2018 was HK$0.256.

As at 31 December 2018, the gearing ratio stood at 55.8%.

In FY2018, the group also securing 15 new projects and a further 4 supplementary agreements from existing projects.

(i) How has management adapted to the changes in the regulatory regime? Does the group have the bandwidth in its management and technical teams to seize the new opportunities?

The Company's Response:

The promulgation of various key ecological conservation measures, the gradual improvement of the overall policy framework, and the continued tightening of supervision and law enforcement provided clearer directions and more stringent regulatory guidance for future industry growth, ranging from the water environment management sector to the ecological and environmental protection industry. Presented with both opportunities and challenges, the Company has been proactively optimising its safety and environmental management departments at all levels, and continuously improving its operational transparency and discharge standards. The Safety and Environmental Management Department of the

Company, which was newly established in 2019, will create a more comprehensive and long-term environmental management mechanism.

*With new areas of the water business, such as water environment management, having become the new directions of the water industry, the Company has (i) developed a set of development strategies in recent years for the concurrent growth of its traditional and new business segments, (ii) carried out technology research and development ("**R&D**") on relevant areas, and (iii) strengthened its efforts in team building. As a result, the Company and its subsidiaries (the "**Group**") have transformed into an enterprise that focuses on the comprehensive management of water environment, the comprehensive utilisation of water resources and the comprehensive protection of water ecology. Its objectives are to build its business capabilities with "good quality, high standard and advanced technology" and to be able to response steadily to the tightened industry and regulatory trends. Separately, the Company has an experienced and stable senior management team, with an average of over ten years of experience in assessing, developing and managing projects in the water industry, and they also possess extensive industry knowledge, experience and operational expertise. The management teams at regional and project levels have strong professional expertise and rich experience in the local markets.*

(ii) Please clearly state the group's growth initiatives and strategic priorities for 2019-2020.

The Company's Response:

*The management team of the Company (the "**Management**") believes that the water environment management sector and the ecological and environmental protection industry will continue their rapid development in the next few years. The Group, while solidifying firmly in the traditional areas such as municipal waste water treatment and municipal water supply, has been and will be actively gaining advantageous positions in new business areas such as industrial park waste water treatment, urban water environment management and black-odor water body treatment. The Group will continue enhancing its efforts in in-house R&D and in the "industrial-academic" research collaboration, and further integrate its existing platforms relating to technology R&D and design, so as to enhance its core technological competitiveness and the commercialisation of its research results. In addition, the Group will improve its engineering and operational management proficiencies relating to safety, environment and occupational health, to ensure that all construction works will be carried out safely and orderly and all projects will be operated stably and in compliance with relevant standards. By taking various measures and adhering to its development path towards "marketisation and professionalism", the Company is striving to stand out among its peers in the competitive market environment.*

(iii) Would the company consider listing down all its plants (operational and under construction) and provide an overview that includes the capacity, utilisation, concession model (such as BT, BOT, TOT, BOO), etc?

The Company's Response:

The Company lists the particulars of all its projects in the sustainability report that is published in May of every year. It will also consider disclosing the project details in its annual reports in the future for the shareholders' reference.

(iv) What is the projected impact on the group's cash flow and earnings due to the hike? What are the criteria for tariff hikes and how frequently are the tariffs reviewed?

The Company's Response:

*In 2018, a total of 18 projects of the Group were approved for an increase in water treatment service fees ("**Tariff Hikes**") ranging from 1% to 165%, mainly attributable to project upgrading, increasing operating costs and changes in tax policies. The Tariff Hikes had a positive impact on the Group's revenue and cash flows in 2018 that the Group's revenue increased by approximately 3% and the operating cash flows before working capital changes of the Group increased by approximately 7% arising therefrom. The Tariff Hikes are expected to have a positive impact on the Group's revenue and operating cash flows over the service concession period in the future.*

The initial amount of the water treatment service fee of a project is specified in the service concession agreement, which is negotiated between the Group and the relevant local government authorities. The Group's service concession agreements expressly provide for the circumstances under which the project companies may apply to adjust the water treatment service fee. Such circumstances include, but are not limited to, inflation, changes in loan benchmark interest rates or public utility charges, and changes in the relevant regulations on the quality standard of influent to be treated and the effluent after treatment. The Tariff Hikes become effective after they are approved by the relevant local government authorities. In general, the mechanism for effecting Tariff Hikes will be triggered when the increase in operating costs reaches certain amount or percentage. If the operating cost increases frequently within a short period of time, the Tariff Hikes will be effected within the prescribed period of time as specified in the agreement.

Question 2

Financial Statements and Audit Commit Commentary

The "Recoverability of trade receivables" is a key audit matter ("KAM") highlighted by the Independent Auditor in their Report on the Audit of the Financial Statements (page 78). Key audit matters are those matters that, in the professional judgement of the Independent Auditor, were of most significance in the audit of the financial statements of the current period.

As noted in the KAM, as at 31 December 2018, the group had trade receivables amounting to HK$721,281,000, net of expected credit losses ("ECL") allowance of HK$49,888,000.

In Note 22 (page 174 – Trade and other receivables), the ageing analysis of the trade receivables that are not impaired is as follows:

Group	**本集团**		
		As at 31 December 于十二月三十一日	
		2018 二零一八年 HK$'000 千港元	2017 二零一七年 HK$'000 千港元
Current	即期	**367,987**	222,142
Past due:	已逾期：		
- 1 to 30 days	– 1至30日	**21,844**	40,250
- 31 to 90 days	– 31至90日	**73,100**	32,578
- 91 to 180 days	– 91至180日	**133,978**	13,685
- 181 to 365 days	– 181至365日	**54,511**	25,391
- more than 1 year but within 2 years	– 超过一年但两年内	**38,851**	74,860
- over 2 years	– 两年以上	**31,010**	4,871
Amounts past due	逾期款项	**353,294**	191,635
		721,281	413,777

As at 31 December 2018, the outstanding amount of trade receivables past due but not impaired increased by 74% to HK$721 million. In particular, the amount past due by over 2 years jumped from HK$4.9 million to HK$31.0 million and the amount past due by 91 to 180 days is approximately 10 times higher at HK$134 million.

(i) Can management help shareholders understand the reasons for the increase in the total trade receivables past due but not impaired and, in particular, the amounts that are overdue by more than 2 years?

The Company's Response:

More than 95% of the trade receivables of the Group that have been overdue for more than 2 years, and for which impairment have not been provided for, can be attributed to the water treatment service fee receivables of a wastewater treatment project in Liaoning Province. Although the amount has been overdue for more than two years at the end of 2018 was relatively large, the relevant project company has continuously received payment of its service fees in recent years. Furthermore, the relevant local government does not have any disagreement on the amount outstanding. Throughout the years, the relevant project company has been actively discussing with the relevant local government regarding the matter and it has obtained a written letter from the relevant local government in November 2018, pursuant to which, the local government undertook to make repayment of all outstanding receivables in the next three years and, from 2018, to settle all the future water treatment service fees for any year within the same year. By the end of 2018, the local government had made full payment of the water treatment service fee for 2018 as promised, and according to the letter provided by the local government, the outstanding receivables overdue for more than 2 years will also be paid in 2019.

*Trade receivables that have been overdue for 91 days to 180 days have also increased as compared to last year. Such trade receivables are primarily attributed to (i) the water treatment service fee receivables of a waste water treatment project in Shandong Province (accounting for 33%), (ii) the receivables due from a customer arising from sales and installations of equipment under an engineering, procurement and construction ("**EPC**") project undertaken by Jiangsu Tongyong Environment Engineering Co., Ltd. ("**Jiangsu Tongyong**", which is a wholly-owned subsidiary of the Company that provides engineering and construction services) (accounting for 39%), and (iii) the project design service fee receivables of Xuzhou Municipal Design Institute Co., Ltd. ("**Xuzhou Design Institute**"), a company newly acquired by the Group in 2018 (accounting for 9%).*

The major reason for trade receivables of the above-mentioned waste water treatment project in Shandong Province being overdue was due to the delayed payment of water treatment service fees upon approval of tariff hike after the upgrading of the project was completed. As at 28 February 2019, the relevant local government has approved the payment of waste water treatment service fees of approximately HKD96.55 million.

The above-mentioned trade receivables of Jiangsu Tongyong arose from sales and installations of equipment, and such trade receivables are expected to be recovered in full amount in 2019.

Xuzhou Design Institute was acquired by the Group in 2018. Although a number of trade receivables were overdue as at the date of completion of the acquisition, the Group has included some protective clauses in the sales and purchase agreement to ensure that the Group will not suffer losses in connection therewith.

(ii) What is the process by management to evaluate the collectability of these long outstanding receivables?

<u>*The Company's Response:*</u>

For long outstanding trade receivables, the Management primarily assesses the recoverability of the trade receivables of a customer based on such customer's financial condition, credit standing, settlement track record and the past experiences with the customer.

Since the Group's customers are local government departments in different provinces of the PRC, the settlement of trade receivables mainly depends on the budget, credit standing, fiscal policy, development plan and the related priorities of the local government departments. Based on the Group's past experiences, although sometimes there might be delay in payments by local government departments, none of the projects has experienced issues with non-payment. Payments from local government departments have been made constantly and there has been no dispute on the balances or any default in payments. As such, the Management considers the credit risk faced by the Group to be low and there is minimum and manageable risk regarding the recoverability of long-aged trade receivables.

(iii) Can management help shareholders understand its efforts in collecting these long outstanding trade receivables? Given that most of the debtors are local government authorities in the PRC tied down to a long contract, how can management improve its working capital management to free up capital to support its future growth?

<u>The Company's Response:</u>

*Since the listing of the Company on the Singapore Exchange Securities Trading Limited ("**SGX-ST**") through the reverse takeover of HanKore Environment Tech Group Limited in December 2014 and the acquisition of Dalian Dongda Water Co. Ltd. in November 2015, the Management has been focusing on managing trade receivables, especially the recovery of the long-aged trade receivables. Through providing safe, stable and quality standard-conforming services and proactively cooperating with the local government departments in their upgrading plans, the Group receives recognition from, and establishes a good working relationship with, the local government departments. This facilitates the collection of the trade receivables. In particular, as for the acquired projects which experienced non-payment from local government departments or had trade receivables overdue for more than two years at the time of acquisition, the trade receivables situation has drastically improved. Since 2016, the trade receivables collection rate has increased year by year. In particular, in 2017, the trade receivables collection rate exceeded 100%, indicating that the Group not only received in full the water treatment service fees for that year, but it also recovered some of the outstanding receivables from prior years. As such, trade receivables balance as at end of that year was reduced to HK$414 million.*

The Management maintains extensive and close communication with the local government departments to ensure that the payment of the outstanding receivables from past years and for the current year is included in the budget of the local government department, so as to recover the outstanding trade receivables. For example, trade receivables of a wastewater treatment project in Liaoning Province had been overdue for more than 2 years when the project was acquired in November 2015. After three years of unremitting efforts of the Management, the Group received a letter from the local government department in November 2018 under which the local government undertook to pay the outstanding amount in full in three years from 2019 to 2021 in the proportion of 30%, 30% and 40% respectively.

In view of the fact that the Group's customers are mainly local government departments in the PRC and the term of the contracts are long, the Group short-lists and partners with credible business partners based on the risk assessment of each potential investment project. The Management takes into consideration of the financial capabilities and credit standing of the relevant local government during the assessment stage to avoid the occurrence of credit risk problems at a later stage of the investment. During the operation stage of a project, the Management maintains close communication and co-operation with local government departments and strengthens the efforts in collecting trade receivables, in order to free up more funds to support the development and growth of the Group.

(iv) Has the audit committee (AC) evaluated if the group's credit risk has increased as the group scaled up its operations? Has the AC considered making further improvement to its credit risk framework?

<u>The Company's Response:</u>

In relation to the credit risk faced during its operations, the Group adopts a series of credit risk management measures to prevent and reduce such risk. The Audit Committee and the Board, together with the Management are deeply involved in the formulation and implementation of such measures.

Currently, most customers of the Group are the local government authorities of PRC and most of the Group's revenue comes from the service fees collected from the PRC's local governments in respect of its provision of the water treatment or water environment management services. Pursuant to the service agreements relating to the water treatment projects or water environment management projects, the local governments shall pay the service fees to the Group either one month or on a regular basis after the Group's provision of such services. In practice, due to the local governments' finance budgets or settlement cycles, local governments pay the service fees to the Group at different timings and cycles. For example, while the local governments for some of the Group's projects adopt a half-yearly or an irregular settlement cycles, they generally ensure that all the service fees payable for the year are fully paid within the same year. As such, the Group's receivable balance demonstrates certain fluctuations. Besides that, some of the acquired projects, due to the historical factors which existed before the Group's acquisition, record substantial amount of receivables, and this would usually take a few years to improve and resolve after the Group completes the acquisition.

Specifically, the Group focuses on economically more developed regions as its key expansion regions for the new projects, such as: Yangtze River Delta, Bohai Economic Rim, and Guangdong-Hong Kong-Macao Greater Bay Area. Most of the Group's existing projects are also located in the coastal economically developed regions, such as Shandong Province, Jiangsu Province, Dalian City and inland economically developed regions, such as Beijing Municipality, Shaanxi Province, Henan Province, Hubei Province. The local governments of such regions usually possess stronger financial capability, contractual spirit and environmental protection awareness. In negotiating the terms and conditions of the projects, the Group ensures that the terms regarding the service fee payment and adjustment mechanism are clearly set out in the project agreements. When the Board or the Management considers the projects, the financial capability and creditworthiness of the counterparty to the project agreements is also one of the key consideration factors. In respect of the acquisition projects, during the due diligence, commercial negotiation and investment decision-making process, the Group also monitors and puts a lot of consideration into the economic development situation of the regions where the projects are located and the financial capability and creditworthiness of the local governments or the project customers. In relation to the acquisition projects with larger receivables amount or higher credit risk, the Group usually prevents and reduces the impact of the credit risks on the Group through arrangements such as contingent payment, receivables recovery guarantee or performance guarantee.

*In relation to the operating projects, the Management, at least once a month, summarises and analyses the Group's receivables based on locations and types of projects and ageing of debts. For the projects which have a larger amount and a longer ageing period of receivables, the Management, apart from implementing good operation management of the projects, actively communicates with the relevant local governments to obtain a concrete repayment plan or explores innovative methods to solve the receivables problem. The Audit Committee and the Board, at least once a quarter, receive a report from the Management on the Group's receivables, and they will then discuss in details and formulate targeted measures towards improvement of the situations. The internal auditors of the Group carry out audits on the receivables management of the Group and the credit risk of the customers; communicate such audit results and the proposed rectification actions to the relevant project companies; record the details in their audit reports; and report to the Audit Committee every quarter. In addition, the external auditor of the Group (the "**Independent Auditor**") also includes the recovery of trade receivables as a key audit matter and has disclosed the relevant audit procedure in the Independent Auditor's Report.*

The Audit Committee periodically evaluates the credit risk faced by the Group and is of the view that the credit risk currently faced by the Group is within control and the existing credit risk management system remains effective in the material aspect of preventing and reducing the credit risk. Following the expansion of the Group's business scale and business area, the Audit Committee will continue working with the Management as well as the internal auditors and the external auditors to evaluate and further improve and enhance the credit risk management system, as and when appropriate.

<u>Question 3</u>

Corporate Governance

In the Corporate governance report, it was disclosed that Mr. Lim Yu Neng Paul and Ms. Cheng Fong Yee were first appointed to the board on 31 July 2007. Mr. Lim and Ms. Cheng have each served on the board for over 11 years.

In addition, in August 2018, the Monetary Authority of Singapore issued a revised Code of Corporate Governance ("2018 CG Code"). As a consequence of the revised 2018 CG Code, the Singapore Exchange has made amendments to its Listing Rules which came into effect on 1 January 2019, except for the rules on the 9-year tenure for independent directors and the requirement for independent directors to comprise one-third of the board which come into effect on 1 January 2022. Under the revised Listing Rules, the term of an independent director will be limited to nine years after which the long tenured directors will be subject to a two-tier vote by shareholders.

(i) Has the company evaluated the impact of the 2018 CG Code and the amendments to the Listing Rules on the board?

<u>The Company's Response:</u>

*The Board currently comprises seven Directors, including a Non-Executive Chairman, two Executive Directors and four Independent Directors; and the Chairman of the Board (the "**Chairman**") and the Chief Executive Officer are not related to each other. The Board has established five sub-committees ("**Board Committees**"), namely, the Audit Committee, Nominating Committee, Remuneration Committee, Strategy Committee and Management Committee. These Board Committees function within written terms of reference and operating procedures, which are reviewed on a regular basis. Each of these Board Committees reports its activities regularly to the Board. All the members of the Audit Committee, Nominating Committee and Remuneration Committee are Non-Executive Directors, and the chairman and majority of the members of each such committees are Independent Directors. Apart from that, in respect of the Board's conduct of affairs, Board performance, remuneration policy and disclosure of remuneration, risk management and internal controls, shareholder rights and communication, and engagement with shareholders, the Company has been complying with the principles under the Code of Corporate Governance 2012 (the "**2012 Code**") and following the best practices recommended by the 2012 Code. In the event that the Company's practices deviate from any guidelines of the 2012 Code, the Company provides the relevant explanation for such deviation in its annual reports.*

*The Company notes that the Code of Corporate Governance 2018 ("**2018 Code**") and the amendments to the SGX-ST Listing Manual updated some of the requirements and practices relating to corporate governance. After review and evaluation, the Company is of the view that such updates do not have any impact on the Board as the Company has complied with the updated requirements or practices under the 2018 Code in material aspects such as in* *relation to the composition and conduct of affairs of the Board and Board Committees. As for the two-tier vote in respect of re-election of the Independent Directors with more than 9 years in service, the Company will ensure that such requirement to be complied with within the prescribed period.*

(ii) Is the company considered a foreign issuer on the SGX and thus required to have at least two independent directors who are Singapore residents on a continuing basis?

The Company's Response:

The Company was incorporated in Bermuda pursuant to the Bermuda Companies Act 1981 and is considered as a "foreign issuer" listed on SGX-ST. As such, the Company is required at all times to have at least two Independent Directors, who are residents in Singapore.

(iii) With the appointment of independent directors Mr. Zhai Haitao and Ms. Hao Gang in 2015 and 2018 respectively, what are the company's other near term plans to refresh the membership of the board to comply with the new 2018 Code in good time?

The Company's Response:

As mentioned above, the Company's current composition of the Board and Board Committees have complied with the principles and guidelines under the 2018 Code.

The Board currently has two members (namely Mr. Lim Yu Neng Paul and Ms. Cheng Fong Yee) who have served the Board for over 9 years. They were both appointed as the Company's Independent Directors in July 2007. Since then, the Company experienced changes in controlling shareholders and the Management teams twice. The current controlling shareholder only gained control of the Company in December 2014 and the current remaining Board members as well as all the senior management personnel and executive officers joined the Company following that change. Thus, although Mr. Lim Yu Neng Paul and Ms. Cheng Fong Yee served the Board for over nine years from the date of their appointment, both the Nominating Committee and the Board held the view that they remain independent in character, judgment and conduct and that they have no relationship with the Company, its controlling shareholders or its officers that could jeopardize their independence. The Nominating Committee and the Board will continue undertaking a rigorous review of the independence of the Independent Directors who have served the Board for more than nine years, and will ensure that the Company complies with the 2018 Code and the revised SGX-ST Listing Manual relating to the two-tier vote for the appointment of the relevant Independent Directors.

The Nominating Committee of the Company, at least once a year, reviews the composition of the Board, including the education and working background, expertise, experience and contributions of each Board member towards the Company to ensure that the Board is sufficiently independent and diverse, and is able to provide constructive advice on the Company's development from various perspectives. After forming an opinion on the composition of the Board, the Nominating Committee makes recommendation to the Board for their deliberation and decision. In the event that there is any change to the composition of the Board or the relevant Board Committee, the Company will release an announcement immediately.

(iv) What is the search and nomination process for new directors, especially independent directors? Is the board leveraging on professional search firms to cast the net wider to possibly increase the quality and diversity of its candidate pool?

The Company's Response:

When the Board or the Nominating Committee is of the view that there is a need for a new Board member, the Board (with the assistance of the Nominating Committee) will determine the professional background, qualifications and experience required on such new Board member. The Company will then identify a suitable candidate accordingly and submit his / her resume to the Chairman and the chairman of the Nominating Committee for their consideration and at the same time, the Company's relevant personnel will approach the candidate and confirm his / her preliminary interest in such appointment. The Chairman will then have a formal or informal meeting with the candidate. After that, the Nominating Committee will conduct an interview with the candidate and have an internal discussion. If the candidate is suitable, the Nominating Committee will make a recommendation to the Board for consideration. The Board will then consider the candidacy of such candidate, and once the appointment is approved by the Board and the candidate signs the relevant statutory documents, his / her appointment as a Director becomes effective. Before his / her appointment as a new Director comes into effect, the Company will arrange for external lawyers to conduct a training for him / her to educate him / her on the roles and responsibilities of a director of a company listed on SGX-ST, and designate a personnel of the Company to assist him / her to familiarise him / her with the Company's business and industry.

The Board has not engaged a professional search firm to look for suitable candidate for the Director role. However, in the future, the Company will consider leveraging on professional search firms to cast a wider net to look for a suitable candidate for the Director role.

By Order of the Board
CHINA EVERBRIGHT WATER LIMITED

An Xuesong
Executive Director and Chief Executive Officer

Date: 12 April 2019