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FIH Mobile Limited
富智康集團有限公司

(Incorporated in the Cayman Islands with limited liability)
(Stock Code: 2038)

CONTINUING CONNECTED TRANSACTION
ANNUAL CAPS REVISION

Financial adviser



云 锋 金 融

Yunfeng Financial Markets Limited

(A member of Yunfeng Financial Group)

The Group from time to time has been carrying out the Lease Expense Transaction with the Hon Hai Group pursuant to the Framework Lease Expense Agreement for a term up to 31 December 2019. The Lease Expense Transaction constitutes a non-exempt continuing connected transaction for the Company under the Listing Rules, and with reference to the Announcement, the Company fixed annual caps for the transaction for the three years ending 31 December 2019. The Company has envisaged that the annual caps of the Lease Expense Transaction for the two years ending 31 December 2018 and 2019 may not be sufficient and has therefore set the New Annual Caps.

Based on the maximum amount of the New Annual Caps, certain applicable percentage ratios are above 0.1% but all relevant percentage ratios are less than 5%. In accordance with Rule 14A.76(2) of the Listing Rules, the Lease Expense Transaction together with the New Annual Caps for the two years ending 31 December 2018 and 2019 are exempt from the circular (including independent financial advice) and the Independent Shareholders' approval requirements.

The Lease Expense Transaction is subject to the annual review requirements under Rules 14A.55 to 14A.59 of the Listing Rules.

INTRODUCTION

The Group is a vertically integrated manufacturing service provider for the handset industry worldwide. It provides a wide range of manufacturing services, including ancillary logistics and distribution services, to its customers in connection with the production and distribution of handsets.

The Hon Hai Group is the leading global manufacturing service provider in the 3C industries. Hon Hai is the ultimate controlling shareholder of the Company holding approximately 62.78% of the total number of issued shares of the Company as at the date of this announcement, and hence a connected person of the Company under the Listing Rules.

The Group from time to time has been carrying out the Lease Expense Transaction with the Hon Hai Group pursuant to the Framework Lease Expense Agreement for a term up to 31 December 2019 as more particularly described below. The Lease Expense Transaction constitutes a non-exempt continuing connected transaction for the Company under the Listing Rules, and with reference to the Announcement, the Company fixed annual caps for the transaction for the three years ending 31 December 2019. The Company has envisaged that the annual caps of the Lease Expense Transaction for the two years ending 31 December 2018 and 2019 may not be sufficient and has therefore set the New Annual Caps.

LEASE EXPENSE TRANSACTION

Pursuant to the Framework Lease Expense Agreement, the Hon Hai Group has agreed to lease premises owned by it and located worldwide to the Group from time to time as requested by the Group for a term up to 31 December 2019 upon and subject to the terms and conditions set out therein at a rental determined as follows:

The rental payable by the Group under the Lease Expense Transaction shall be determined on a fair and reasonable basis with reference to the average market rental of other similar local properties in the market. If the average market rental is not available, the rental payable under the Lease Expense Transaction shall be determined on a “cost plus” basis. If both the average market rental basis and the “cost plus” basis are not appropriate or applicable, the rental payable under the Lease Expense Transaction shall be agreed between the relevant parties based on reasonable commercial principles. Under the Lease Expense Transaction, the Group leases real properties from the Hon Hai Group mostly manufacturing premises for handset manufacturing. As the locations and the conditions of the properties vary, the Group is not able to fix the rentals but has instead agreed to the pricing terms set out above.

The relevant parties may enter into a separate specific lease agreement for the relevant premises leased by the Group under the Framework Lease Expense Agreement. The rentals for the Lease Expense Transaction are usually payable on a monthly basis.

PRICING DETAILS

The rental payable by the Group under the Lease Expense Transaction shall be determined on a fair and reasonable basis with reference to the average market rental of other similar local properties in the market. For the purpose of obtaining market rentals, in general, the Group refers to at least one recent lease transaction of the Group leasing a similar local property from an independent party within three months of the proposed transaction with the Hon Hai Group, and if the aforesaid is not available, at least one quotation from an independent party offering a similar local property for rent in the market.

If the average market rental is not available, the rental payable under the Lease Expense Transaction shall be determined on a “cost plus” basis. Cost plus is determined based on the relevant cost of the transaction plus a margin as agreed between the Group and the Hon Hai Group. In determining the margin, the Group takes into account the margin for lease of properties of similar nature in the market by way of referring to margins for the Group’s lease of properties of similar nature to independent parties. In general, the Company will select one independent transaction (most related to the subject property in nature) within three months of the proposed transaction with the Hon Hai Group to determine the market margin. The cost is usually determined on the basis of the depreciation charge and the related costs of the properties such as interests and insurance cost. Under the cost-plus pricing, the cost is based on the Hon Hai Group’s accounting records which are prepared based on International Financial Reporting Standards. The Group’s operation departments will assess the reasonableness of such cost taking into account the cost structure including the depreciation charge, interests and insurance costs. The Group’s accounting departments will check whether the cost is in accordance with the Hon Hai Group’s accounting records.

If both the average market rental basis and the “cost plus” basis are not appropriate or applicable, the rental payable under the Lease Expense Transaction shall be agreed between the relevant parties based on reasonable commercial principles. In consideration of its properties utilisation management, the Hon Hai Group may agree to prices lower than costs and market rentals. In such cases, the Company would lease the properties from the Hon Hai Group at such lower prices as agreed by the Hon Hai Group. The Company shall review and ensure such prices are lower than costs and market rentals. This pricing term has not been applied since 2015 but remains to be relevant to cater to such circumstances in the future.

REASONS FOR THE LEASE EXPENSE TRANSACTION

A part of the Group’s operations in the PRC is located in the Hon Hai Group’s industrial parks in the PRC in view of the benefits of locating close to the members of the Hon Hai Group which possess leading capabilities and expertise amid the convergence trend within the 3C industries, and the physical proximity can lead to additional savings and efficiency to the Group if the Group’s customers select these members of the Hon Hai Group as suppliers of materials and components for the manufacture of handsets as approved by the customers of the Group.

HISTORICAL VALUES AND ANNUAL CAPS

With reference to the Announcement, the Company fixed annual caps for the Lease Expense Transaction for the three years ending 31 December 2017, 2018 and 2019. In view of the forthcoming renewal of certain specific lease agreements at terms in accordance with the Framework Lease Expense Agreement and taking into account the prevailing market rentals and the Group’s additional requirement of manufacturing facilities as estimated based on the Group’s business and production plan, the Company has envisaged that the annual caps for the Lease Expense Transaction for the two years ending 31 December 2018 and 2019 may not be sufficient and has therefore set the New Annual Caps. The table below sets out (a) the historical actual amounts of the Lease Expense Transaction for the two years ended 31 December 2016 and 2017; (b) the annual caps for the Lease Expense Transaction for the three years ending 31 December 2019 as fixed under the Announcement; and (c) the New Annual Caps.

	Actual transaction amounts		Annual caps fixed under			New Annual Caps	
	for the year ended		the Announcement			for the year ending	
	31 December	31 December	for the year ending			31 December	31 December
(in US\$ '000)	2016	2017	2017	2018	2019	2018	2019
	(audited)	(audited)					
Lease Expense Transaction	<u>3,396</u>	<u>3,413</u>	<u>5,000</u>	<u>5,000</u>	<u>5,000</u>	<u>8,059</u>	<u>10,097</u>

The New Annual Caps are determined with reference to projections of the Company which in turn are prepared by the Company mainly with reference to the following major factors:

- the existing specific lease agreements entered into under the Framework Lease Expense Agreement;
- the renewal of certain specific lease agreements at terms in accordance with the Framework Lease Expense Agreement and taking into account prevailing market rentals;
- the Group's additional requirement of manufacturing facilities as estimated based on the Group's business and production plan; and
- an additional buffer of 5%, to cater for any increase in the transaction which is unexpected but not substantial.

The Directors (including the independent non-executive Directors) consider that the New Annual Caps are fair and reasonable, the entering into of the Lease Expense Transaction is in the Group's ordinary and usual course of business, and the terms of the Lease Expense Transaction are fair and reasonable, on normal commercial terms and in the interests of the Company and its Shareholders as a whole. In view of their relationship with Hon Hai, Mr. WANG Chien Ho and Mr. HUANG Chin Hsien (both being executive Directors) have abstained from voting on the Board resolutions in relation to the Lease Expense Transaction and the New Annual Caps.

INTERNAL CONTROL

The Group has adopted the following internal control procedures over the continuing connected transactions of the Company including the Lease Expense Transaction:

- Before entering into a transaction under the continuing connected transactions of the Company, the purchase departments and/or the operation departments (as the case may be) of the Group will review and check whether the pricing is fair and reasonable adhering to the pricing terms and details. In addition to reviewing the pricing before entering into a transaction under the continuing connected transactions of the Company where the pricing terms under the relevant agreements are applied for the first time or the pricing terms are different from those used previously, the accounting departments of the relevant member companies of the Group will review the aforesaid works carried out by the purchase departments and/or the operation departments (as the case may be) on a quarterly basis.

- The accounting department of the Company is primarily responsible to review and monitor the continuing connected transactions ensuring that the annual caps of the relevant continuing connected transactions are not exceeded and the continuing connected transactions have been conducted in accordance with the pricing policies or mechanisms under the framework agreements relating to such continuing connected transactions. The accounting department of the Company will consult with the Group's internal audit function in respect of continuing connected transaction compliance issues and annually report to the chief financial officer of the Company, who (in his own capacity and on behalf of the Group's management designated for the purposes of the Group's enterprise risk management and internal controls) will report to the audit committee of the Company and also provide a confirmation to the audit committee that the continuing connected transactions of the Company which are subject to the annual review and disclosure requirements under the Listing Rules have been entered into (a) in the ordinary and usual course of business of the Group; (b) on normal commercial terms or better; and (c) in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the Shareholders as a whole; and that the Group's internal control procedures applicable to continuing connected transactions are adequate and effective to ensure that such transactions were so conducted. The audit committee will consider this accordingly.
- The Company's external auditors will review the continuing connected transactions (which are subject to the annual review and disclosure requirements under the Listing Rules) annually to check and confirm (among others) whether the pricing terms have been adhered to and whether the relevant caps have been exceeded.
- The independent non-executive Directors will review the continuing connected transactions of the Company (which are subject to the annual review and disclosure requirements under the Listing Rules) annually to check and confirm whether such continuing connected transactions are conducted in the ordinary and usual course of business of the Group, on normal commercial terms or better, in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the Shareholders as a whole, and whether the internal control procedures put in place by the Company are adequate and effective to ensure that such continuing connected transactions were conducted in accordance with the pricing policies set out in such relevant agreements.

LISTING RULES REQUIREMENTS

Based on the maximum amount of the New Annual Caps, certain applicable percentage ratios are above 0.1% but all relevant percentage ratios are less than 5%. In accordance with Rule 14A.76(2) of the Listing Rules, the Lease Expense Transaction together with the New Annual Caps are exempt from the circular (including independent financial advice) and the Independent Shareholders' approval requirements.

The Lease Expense Transaction is subject to the annual review requirements under Rules 14A.55 to 14A.59 of the Listing Rules.

DEFINITIONS

“Announcement”	the announcement of the Company dated 11 August 2016
“associate(s)”	having the meaning as defined in the Listing Rules
“Board”	the board of Directors
“Company”	FIH Mobile Limited, a limited liability company incorporated in the Cayman Islands, the shares of which are listed on the Stock Exchange
“Director(s)”	the director(s) of the Company
“Framework Lease Expense Agreement”	the framework lease agreement entered into between 深圳富泰宏精密工業有限公司 (Shenzhen Futaihong Precision Industrial Co., Ltd. for identification purposes only) (a wholly-owned subsidiary of the Company), which was subsequently replaced by the Company as the party thereto, and Hon Hai dated 18 January 2005 (as amended by the respective supplemental agreements dated 12 January 2006, 20 September 2006, 24 October 2007, 19 November 2010, 17 October 2013 and 11 August 2016)
“Group”	the Company and/or its subsidiaries (as the case may be)
“Hon Hai”	鴻海精密工業股份有限公司 (Hon Hai Precision Industry Co. Ltd. for identification purposes only), the ultimate controlling shareholder of the Company
“Hon Hai Group”	Hon Hai, its subsidiaries and/or associates (as the case may be)
“Independent Shareholders”	Shareholders other than Hon Hai and its associates
“Lease Expense Transaction”	the lease of premises by the Group from the Hon Hai Group contemplated under the Framework Lease Expense Agreement
“Listing Rules”	the Rules Governing the Listing of Securities on the Stock Exchange, as amended and/or supplemented from time to time
“New Annual Caps”	the new annual caps for the Lease Expense Transaction for the two years ending 31 December 2019
“percentage ratios”	the percentage ratios calculated based on the requirements under Rule 14.07 of the Listing Rules
“PRC”	the People’s Republic of China

“Shareholders”	the holders of the Shares
“Share(s)”	the ordinary share(s) of US\$0.04 each of the Company
“Stock Exchange”	The Stock Exchange of Hong Kong Limited
“subsidiary(ies)”	having the meaning ascribed to it under the Companies Ordinance (Chapter 622 of the Laws of Hong Kong)
“US\$”	United States dollars, the lawful currency of the United States of America
“3C”	computer, communication and consumer electronics

By Order of the Board
CHIH Yu Yang
Acting Chairman

Hong Kong, 8 March 2018

As at the date of this announcement, the Board of the Company comprises four executive directors, namely Mr. CHIH Yu Yang, Mr. WANG Chien Ho, Mr. HUANG Chin Hsien and Mr. YU Mingjen; one non-executive director, namely Dr. LUO Zhongsheng; and three independent non-executive directors, namely Mr. LAU Siu Ki, Dr. Daniel Joseph MEHAN and Mr. TAO Yun Chih.