

# PROPOSED ACQUISITION OF A COMPLETE SET OF PRODUCTION LINE FOR PRODUCTION OF WOOD FREE PAPER PULP

## 1. Introduction

The Board of Directors of BHS Industries Berhad (“**BHS**” or the “**Company**”) wishes to announce that Nextgreen Pulp & Paper Sdn Bhd (1135982-K) (“**Nextgreen**” or the “**Buyer**”), a wholly-owned subsidiary of the Company, had on 3 June 2015 entered into a sale and purchase agreement (“**Agreement**”) with China-Shaanxi Zhisen Pulp & Paper Engineering Co Limited (“**China-Shaanxi**” or “**Seller**”) to acquire a complete set of production line with an annual production capacity of 10,000 metric tons of wood free paper pulp to be set up in Malaysia for a total purchase consideration of RM17,799,200 (Ringgit Malaysia Seventeen Million Seven Hundred Ninety Nine Thousand Two Hundred Only) (“**Agreement**”) (“**Total Purchase Consideration**”), subject to the terms and conditions as stated in the Agreement (“**Proposed Pulp Production Line Acquisition**”).

The production line shall comprise of a Feed Preparation & Pulp Making System (“**Contract Equipment**”) together with spare parts, tools, technical documents, manuals and related technical services and technical training for installation, commissioning, trial production run and operation and maintenance of such production line (“**Production Services**”). The Contract Equipment and Production Services shall collectively be referred to as the “**Pulp Production Line**”.

The Feed Preparation & Pulp Making System incorporates the PRC RBMP technology of using Empty Fruit Bunches, the by-product of crude palm oil mills manufacturing process, to manufacture paper pulp products.

## 2. Information on Nextgreen

Nextgreen was incorporated in Malaysia under the Companies Act, 1965 as a private limited company on 18 March 2015. The authorised share capital of Nextgreen is RM400,000 comprising 400,000 ordinary shares of RM1.00 each, of which 2 ordinary shares have been issued and fully paid-up. Nextgreen is principally engaged in processing, manufacturing, trading and selling of pulp and paper and its related products. Its registered office is at B-13A-28, Kompleks Rimbun Scott Gardens, 289 Jalan Kelang Lama, 58100 Kuala Lumpur

## 3. Information on China-Shaanxi

China-Shaanxi was incorporated in China under the law of the People Republic of China as a private limited company. The authorised and issued share capital of China-Shaanxi is Renminbi 3,600,000. China-Shaanxi is principally engaged in development and sale of paper making machinery and equipment and accessories. Its business address is at No. 97, (ChengYang Bastille), Western Part of XianYang Century Avenue, New Xixian District, Xi’an, 712046 People Republic of China.

#### 4. Salient terms of the Agreement

##### (i) Conditions precedent

- (a) The Proposed Pulp Production Line Acquisition is conditional upon the Buyer's holding company, BHS, obtaining the approval from the shareholders of BHS at the forthcoming extraordinary general meeting to be convened in relation to the Proposed Diversification (as defined in Section 8 of this announcement) 90 calendar days from the date of the signing of the Agreement.
- (b) If the approval has not been obtained within the stipulated 90 calendar days, the parties shall agree to extend for another 60 calendar days therefrom or any further period as mutually agreed by both parties.
- (c) In the event the Company fails to obtain the said approval as stated in 4(i)(a) above, the Agreement shall lapse and the Seller shall refund to the Buyer all monies it has received free of interest.
- (d) All related documents and parts of machinery relating to the Contract Equipment and Production Services shall be returned to the Seller except that if they contain the Technical Information (as defined under item 4(vi)(a) below, then the related documents and parts of machinery shall be returned to the Buyer and the Buyer shall reimburse the Seller the cost of those parts of machinery at a discounted rate to be negotiated between the parties.

##### (ii) Total Purchase Consideration and payment currency

- (a) The Total Purchase Consideration shall be based on Cost, Insurance & Freight / Kuantan Port at a fixed sum of RM17,799,200 (Ringgit Malaysia Seventeen Million Seven Hundred Ninety Nine Thousand Two Hundred Only). The price includes complete special used equipment, water treatment equipment, project design, transportation, installation, testing and commissioning.
- (b) The currency used under this Agreement shall be Ringgit Malaysia (RM) as payment currency.

##### (iii) Payment terms and conditions

The Total Purchase Consideration shall be paid as follows:

- (a) A sum of RM5,161,020 (Ringgit Malaysia Five Million One Hundred Sixty One Thousand Twenty Only) ("**Deposit**"), represents twenty-eight point ninety-nine percent (28.99%), shall be paid by the Buyer to the Seller, the receipt of which the Seller acknowledge as part payment of the Total Purchase Consideration upon the execution of the Agreement;
- (b) The Buyer shall pay the sum of RM10,930,800 (Ringgit Malaysia Ten Million Nine Hundred Thirty Thousand Eight Hundred) only ("**Balance Total Purchase Considerations**"), represents sixty-one point forty-one percent (61.41%), progressively in accordance with the Milestone Achievement as per schedule of payments of the Agreement; and
- (c) A sum of RM1,707,380 (Ringgit Malaysia One Million Seven Hundred Seven Thousand Three Hundred Eighty Only) shall be held as retention sum ("**Retention Sum**"), represents nine point six percent (9.60%).

The first part of the retention sum equivalent to fifty percent (50%) of the Retention Sum plus any variation order shall be released within 90 calendar days upon issuance of Certificate of Practical Completion ("**CPC**") of contract works.

The second part of the retention sum shall be held by the Buyer until the latest of the following has been fulfilled:

- (a) The end of defects liability period which is 12 months from the date of CPC under the Agreement;
- (b) All defects, defaults, damages, losses and expenses have been made good or settled; and Certificate of Making Good Defects (“**CMGD**”) is being issued; and
- (c) Submission of all documents deemed necessary by the Buyer for the preparation of final accounts.

The Seller shall give the Buyer a written notice of 14 calendar days before any milestone which are to be achieved. The Buyer shall give the Seller not less than 48 hours’ notice of intention to witness the achievement of such milestone. The milestone certificate shall be issued by the Buyer after the successful achievement of milestone within 14 calendar days from the date of inspection. Payments to the Seller shall be made as valued by the Buyer not later than 14 calendar days from the date of such valuation by the Buyer.

**(iv) Seller’s representations**

The Seller declares, warrants, covenants and represents that:

- (a) The final product of the Pulp Production Line is the wood free pulp;
- (b) The quality of the final product wood free pulps shall comply with the quality standard as per the Production Quality and Industrial Standard set forth in Annexure 8 of the Agreement;
- (c) The annual production capacity of the final product is guaranteed at ten thousand metric tons (10,000 metric tons); and
- (d) The Seller agrees and acknowledges that the Buyer is entering into this Agreement agreeing to purchase the Pulp Production Line in reliance upon the declarations, representations, warranties and covenants.

**(v) Scope of work to be supplied under the Agreement**

The scope of work to be supplied by the Seller to the Buyer shall consist of:

- (a) Design, manufacture, supply, delivery and installation, commissioning, and trial production run of Pulp Production Line (including licensed computer software program for automation control system) per Annexure 1 of the Agreement;
- (b) Supply and delivery of spare parts including start-up spare parts per Annexure 2 of the Agreement;
- (c) Supply and delivery of tools and accessories necessary for operation per Annexure 3 of the Agreement;
- (d) Supply and delivery of design drawings including as built, isometric and schematic drawing related to engineering and construction of the factory at which the Pulp Production Line will be installed including layout, conceptual design, workshop and warehouse, pipeline of water, electricity and gas as well as technical documents;
- (e) Assist the Buyer in the survey information & geographical plan required for construction of the factory regarding geology, hydrology, meteorology;
- (f) Provision of quality supervision of construction of the factory;
- (g) Provision of supervision of installation, commissioning and trial run of the Pulp Production Line in the Buyer’s factory;
- (h) Provision of technical training to the Buyer’s technical personnel at the Buyer’s factory site; and
- (i) Provision of maintenance and operation service for 1 year at the Buyer’s factory site after the Pulp Production Line is fully accepted by the Buyer.

**(vi) Intellectual properties rights**

- (a) Intellectual property rights in all specifications, drawings, technical descriptions and other technical information of the Seller in whatever format or medium (collectively referred to as "**Technical Information**") and in any equipment, both as supplied by the Seller or to the Seller in connection with the Agreement exclusively and permanently belong to Green Patent Technologies Sdn Bhd ("**Technology Provider**") which has been licensed absolutely to System Publishing House Sdn Bhd ("**SPH**"), a subsidiary of the Company, by way of a Master Licence Agreement dated 10 November 2014;
- (b) All techniques and technologies employed in the Contract Equipment belong to the intellectual property rights of SPH and/ or the Technology Provider. The Buyer, however, shall have the rights to sell the entire factory and Contract Equipment together with other related facilities to any third party without obtaining the consent of the Seller, SPH and/ or Technology Provider.

**5. Purchase Consideration**

The Total Purchase Consideration as set out in item 4(ii) above was arrived at on a willing buyer-willing seller basis, after taking into account the negotiations and offers with other existing suppliers of similar equipment and machinery.

**6. Source of funds**

The Company would use its internally generated fund to pay the deposit of RM5,161,020 (Ringgit Malaysia Five Million One Hundred Sixty One Thousand Twenty Only) and any of the progress payments should become due from the Balance Total Purchase Consideration of RM10,930,800 (Ringgit Malaysia Ten Million Nine Hundred Thirty Thousand Eight Hundred) as set out in item 4(iii)(b) above; the remaining is intended to be financed by the proceeds to be raised from the Company's proposed rights issue with warrants which was announced on 29 April 2015.

**7. Liabilities to be assumed**

There are no liabilities, including contingent liabilities and guarantees to be assumed by the Buyer and/ or the Company arising from the Proposed Pulp Production Line Acquisition.

**8. Rationale for the Proposed Pulp Production Line Acquisition**

The proposed diversification which was announced on 29 April 2015 involving the existing core businesses of BHS and its subsidiaries ("**BHS Group**" or "**Group**") to include the utilisation and sub-licensing of paper pulp making technology, manufacturing of renewable paper pulp products generated from Empty Fruit Bunches ("**EFB**") using the Pre-conditioning Refiner Chemical Recycled Bleached Mechanised Pulp Technology and other related activities ("**Proposed Diversification**"). It would supplement the existing core businesses of BHS Group, whereby the wood free pulp and paper products produced from the plant to be set up, can be utilised as the raw material for the printing and publishing businesses of BHS Group, thus reducing the reliance on suppliers for the supply of paper and ensuring the long term security and undisrupted supply of paper at a lower price.

In addition, the new business would provide a platform to the Company to market the technology to palm oil mills which would generate streams of income from provision of technology, licence fees, royalties and services.

## **9. Financial Effects of the Proposed Pulp Production Line Acquisition**

The Proposed Pulp Production Line Acquisition will not have any effect on the issued and paid-up share capital of BHS and the substantial shareholders' shareholding of BHS.

There would be no financial effects on earnings, earning per share, net assets per share and gearing of the Company for the financial year ending 30 June 2015.

## **10. Estimated timeframe for completion**

It is expected that the Proposed Pulp Production Line Acquisition will be completed when the Production Line is completely and fully installed, commissioned, trial production run and acceptance by the Buyer which is expected to be completed by the second half of calendar year 2016.

## **11. Prospects and Risks in relation to the Proposed Pulp Production Line Acquisition**

### **11.1 Prospects**

#### **11.1.1 Government's Plan and Initiatives**

As stated in the Industrial Master Plan (IMP3) ("**IMP 3 Initiative**"), the investment in the oil palm industry is projected to register an average annual growth of 8.2% during the period from 2006 to 2020. Between 2011 and 2015, the investment in the oil palm industry is expected to reach RM8.6 billion.

Between 2006 and 2020, the gross export value of oil palm industry is projected to grow at an average annual rate of 7.6% and reaches RM78.8 billion in 2020

The application of oil palm biomass in the pulp and paper industry is one of the target areas that will be promoted during the implementation of IMP3. In addition, research, development and commercialisation of oil palm products are also encouraged. Under the IMP3, institutional support and infrastructure will be strengthened to assist the growth of the oil palm industry

Hence this policy would augur well for BHS who would have the technology to use EFB for the production of wood free pulp and paper as initiatives and supports would be given by the Government to promote the target areas of growth of the IMP3.

*(Source: Reports issued by Ministry of International Trade and Industry)*

### **11.2 Risks involved**

#### **11.2.1 Competition**

Under the IMP3 initiative, it is expected that the Government would encourage greater participation in research and development and commercialisation in the pulp and paper industry in the near future. It is possible that other institutional and commercial entities may develop their own technologies in converting EFB to other commercially viable products or advancing the pulp and paper technology to higher quality and efficiency levels. It is natural that any breakthrough in technologies will lead to eventual competition for newer technologies and raw materials.

*(Source: Reports issued by Ministry of International Trade and Industry)*

### **11.2.2 Dependency on supply of EFB raw materials**

This technology relies on constant supply of EFB raw material to justify its return of investment. It is imperative that a long term contract for the supply of raw material is secured. It is cost saving for the sources of raw material EFB supply be located in close proximity to the manufacturing site where the technology is used.

### **11.2.3 Performance of the Local and Global Economies**

Any prolonged and/or widespread downturn such as those of the recent global financial turmoil can affect the global and Malaysian economies. This slowdown in the global and local economies can reduce consumption in general, thus it will affect the demand for Wood Free Pulp and Paper for the printing activities. However, as evidenced in the past the Malaysian Government's continued prompt policy flexibility in implementing pro-growth measures to sustain the economy to mitigate such downturn. In addition, Malaysian government monitor their currency policies closely in order to react promptly to any changes in the global economy.

For example, since 21 July 2005, the ringgit was allowed to operate on a managed float rate, which is determined by economic fundamentals. Bank Negara Malaysia will monitor the exchange rate against the trade weighted index of Malaysia trading partners. Bank Negara Malaysia's primary policy objective of promoting the stability of the exchange rate will provide some mitigation against volatile movements of foreign currency hence soften the impact on the local economy.

*(Source: Reports issued by Bank Negara Malaysia)*

## **12. Approvals required**

The Proposed Pulp Production Line Acquisition does not require the approval of BHS's shareholders or the approval of any relevant authorities, but is subject to the approval from the shareholders of BHS at the forthcoming extraordinary general meeting to be convened in relation to the Proposed Diversification of BHS.

## **13. Highest percentage ratio**

The highest percentage ratio applicable to the Proposed Pulp Production Line Acquisition pursuant to Chapter 10 of the Main Market Listing Requirements of Bursa Malaysia Securities Berhad is 24.1%.

## **14. Interest of Directors and major shareholders and persons connected to them**

None of the Directors and major shareholders of BHS and persons connected to them has any interest, either directly or indirectly in the Proposed Pulp Production Line Acquisition.

## **15. Directors' Statement**

The Board of Directors of BHS having considered all aspects of the execution of the Agreement is of the opinion that the Proposed Pulp Production Line Acquisition is in the best interest of the Company.

**16. Document Available for Inspections**

A copy of the Agreement is available for inspection at the registered office of BHS at No. 802, 8<sup>th</sup> Floor, Block C, Kelana Square, Jalan SS 7/26, 47301 Petaling Jaya, Selangor during normal office hours from Mondays to Fridays (except public holidays) for a period of 3 months from the date of this announcement.

This announcement is dated 3 June 2015.