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South Manganese Investment Limited

南方錳業投資有限公司

(incorporated in Bermuda with limited liability)
(Stock Code: 1091)

**(1) KEY FINDINGS OF INDEPENDENT INVESTIGATION;
AND
(2) CONTINUED SUSPENSION OF TRADING**

This announcement is made by South Manganese Investment Limited (the “**Company**”) pursuant to Rule 13.09(2) of the Rules (the “**Listing Rules**”) Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “**Stock Exchange**”) and the Inside Information Provisions (as defined in the Listing Rules) under Part XIVA of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong).

Reference is made to the announcements of the Company dated 29 March 2023, 31 March 2023, 2 May 2023, 28 May 2023, 29 June 2023, 28 July 2023, 2 August 2023 and 18 August 2023 (the “**Announcements**”) in relation to, among other things, (i) the delay in publication of the annual results and the annual report of the Company for the year ended 31 December 2022; (ii) the formation of an independent investigation committee (the “**Independent Investigation Committee**”); (iii) appointment of RSM Corporate Advisory (Hong Kong) Limited (currently known as “Acclime Corporate Advisory (Hong Kong) Limited”) as the independent forensic accountant (the “**Independent Forensic Accountant**”); (iv) the guidance for the resumption of trading issued to the Company by the Stock Exchange; (v) the quarterly update on the status of resumption; (vi) the appointment of independent internal control consultant; (vii) the resignation of PricewaterhouseCoopers (“**PwC**”) as the auditor of the Company with effect from 31 July 2023; (viii) the appointment of RSM Hong Kong as the new auditor

of the Company with effect from 18 August 2023; and (ix) the delay in publication of the interim results and the interim report of the Company for the six months ended 30 June 2023. Unless otherwise defined, capitalised terms used herein shall have the same meanings as those defined in the Announcements.

BACKGROUND

As disclosed in the Announcements, during the course of the audit process, the Board and the Audit Committee has received the Letter from PwC on 28 March 2023, regarding PwC's suggestions concerning the Manganese Ore Trading Business of the Group that, among others: (1) the Audit Committee is responsible for the formation of the Independent Investigation Committee; (2) the Independent Investigation Committee shall appoint an independent third-party investigative agency to assist the Independent Investigation on, among others, (a) the unusualness noted from the confirmations returned by the Supplier and the Customer (the "**Issue 1**"); (b) to provide further supporting documents to substantiate the trade with the Supplier and the Customer (the "**Issue 2**"); and (c) the commercial basis of the prepayment amounted to approximately RMB540 million as at 31 December 2022 made to the Supplier (the "**Issue 3**") (collectively the "**Audit Issues**").

PwC has concerns about the commercial substance of the Manganese Ore Trading Business and the authenticity of the relevant sale and purchase transactions, and requested the Company to provide explanation and additional information in the Letter as set out below, including but not limited to:

- (i) provide explanations for the above together with relevant supporting documents, especially the commercial rationale of paying significant amount of prepayment to the Supplier;
- (ii) conduct background investigations of the Supplier and the Customer, and explain whether there is any relationship between the Supplier and the Customer, and whether there is any relationship with the Group;
- (iii) provide complete walk-through documents of the Manganese Ore Trading Business, explain whether there is any genuine transfer of inventory ownership, explain the roles and responsibility of each counterparty in the entire trade chain, and the relationship among the involved parties (including whether they are held by the same party), the commercial rationale and substance of these transactions,

whether there are other relationships or arrangements not disclosed to PwC;

- (iv) comprehensively evaluate the reasonableness of the sales and purchase recognition of the Manganese Ore Trading Business; and
- (v) provide specific information on the funds flow to/ from the Supplier and the Customer with the Group.

Formation of the Independent Investigation Committee

In order to address and resolve the Audit Issues, the Independent Investigation Committee, comprising Mr. Zhang Yupeng, Mr. Yuan Mingliang and Mr. Lo Sze Hung, all independent non-executive Directors, was established on 31 March 2023. The duties and purposes of the Independent Investigation Committee is to commission and lead the Independent Investigation.

The Independent Forensic Accountant issued the report (the “**Independent Investigation Report**”) of the Independent Investigation on 15 September 2023.

SUMMARY OF THE KEY FINDINGS OF THE INDEPENDENT INVESTIGATION

The key findings of the Independent Investigation are summarized as follows:

Background of the Manganese Ore Trading Business

In late 2020, the Group entered into negotiation for business opportunities with a manganese ore mine owner (the “**Mine Owner**”) in Ghana and an agency agreement (the “**Agency Agreement**”) was eventually entered into in relation to the exclusive agency in South China except the Manganese Triangle (i.e. Huayuan County in Hunan, Xiushan Tujia and Miao Autonomous County in Chongqing and Songtao Miao Autonomous County in Guizhou) with agency period commenced from 1 January 2021 and ending on 31 December 2023. Under the Agency Agreement, the Group is required to purchase a minimum quantity of manganese ore from the Mine Owner for three years ending 31 December 2023.

During the negotiation process between the Mine Owner and the Group and with a view to commence the trading business pending finalisation of the terms of the Agency

Agreement, the Mine Owner introduced the Supplier, which was then an existing customer and the authorized distributor and sales partner in the PRC of the Mine Owner, to the Group for business opportunities. The Mine Owner recognized that the purchase from the Supplier would be counted for the purpose of fulfilling the minimum purchase quantity of the Group under the Agency Agreement. The Supplier also referred the Customer, which was then an existing customer of the Supplier, to the Group for business opportunities in 2021.

The Group conducted the Manganese Ore Trading Business by two ways: (i) the Group directly imported Ghana manganese ore from the Mine Owner to the PRC and then sold to downstream domestic traders or manufacturers; and (ii) the Group dealt with the upstream and downstream traders by way of domestic commodities trading. Under the model of domestic commodities trading, the transactions among the Supplier, the Group and the Customer are carried out based on the certificate of weight, certificate of quality issued by the authoritative body, and the delivery orders issued by the Supplier to the Group and issued by the Group to the Customer.

During the year ended 31 December 2022, the Manganese Ore Trading Business was solely conducted by way of domestic commodities trading among the Supplier, the Group and the Customer.

Issue 1

The unusualness noted from the confirmations returned by the Supplier and the Customer

For the registered addresses of the Supplier and the Customer, both the Supplier and the Customer use virtual office as their registered address which are driven by the tax incentives offered by the local governmental authorities of the local district where the said virtual offices are located. The use of virtual office as registered address, and the registered address not being the office address of the Supplier and the Customer are permitted under the local policy and is not an isolated case.

While the office addresses of the Supplier and the Customer are located in close proximity, there are clear signage erected outside their respective office addresses and with office equipment and staff working inside their respective office addresses. Given the proximity of their respective office addresses and the staff of the Supplier and the Customer would assist each other in daily logistic work, such as receiving and sending

of delivery parcels, the unusualness noted by PwC, e.g. the confirmations returned by the Supplier and the Customer from same address, are due to the inattention of the administrative staff of the Supplier and the Customer.

In response to PwC's concerns on (i) not being able to obtain effective responses from the contact persons of the confirmations of the Supplier and the Customer and (ii) being unable to reach the relevant staff of the Supplier at the office number obtained from public source, the Independent Forensic Accountant conducted interviews with the responsible staff of both the Supplier and the Customer, redialed the office numbers of the Supplier and Customer and obtained replies from the relevant staff to some extent and verified the content of the confirmations returned.

Regarding the Issue 1, the Independent Forensic Accountant is able to obtain explanation from the relevant parties to a certain extent and does not identify any material unusualness.

Issue 2

To provide further supporting documents to substantiate the trade with the Supplier and the Customer

During the year ended 31 December 2022, the transactions among the Supplier, the Group and the Customer in relation to the Manganese Ore Trading Business were solely conducted by way of domestic commodities trading.

Unlike bulk cargo trading, the most important features of the domestic commodities trading of the Group in relation to the Manganese Ore Trading Business are the transfer of the ownership of the Ghana manganese ore, the settlement, the issue of the value added tax invoice for settlement, and the making and receipt of the payment, rather than taking physical delivery for settlement. The Independent Forensic Accountant noted from the published announcement of another listed company whose business covers domestic commodities trading in the PRC, that such listed company also has a similar trading arrangement. Based on the public disclosure of the said listed company, the settlement procedure is also based on the certificate of weight and certificate of quality issued by authoritative body, while the completion of transfer of cargo rights amongst the upstream trader, the company and the downstream trader is also based on the delivery instructions issued by each party. The Independent Forensic Accountant noted the similarities of the business model and nature between the domestic commodities

trading of the Group in relation to the Manganese Ore Trading Business and that of the said public listed company.

Regarding a portion of the Ghana manganese ore under a shipment allegedly sold to a third party by the Supplier in August and September 2022 which were included in the purchase recorded by the Group from the Supplier and the sales to the Customer recognised by the Group in December 2022, the quantity involved (i) is approximately 611.2 wet metric tons of Ghana manganese ore; (ii) only formed a small part of the Ghana manganese ore involved in this batch of transaction among the Supplier, the Group and the Customer of approximately 204,724.7 wet metric tons of Ghana manganese ore; and (iii) formed part of the excess quantity of Ghana manganese ore as stated in the certificate of weight issued by the arriving port when comparing to the certificate of weight issued by the departing port. Since the unit price of the whole batch of Ghana manganese ore was yet to be finalised between the Group and the Supplier when such batch of Ghana manganese ore arrived the dock in August 2022, the Group had not yet decided whether to take up the whole batch of Ghana manganese ore by then. The Supplier then sold part of the said excess quantity of Ghana manganese ore to the third party in August and September 2022. In or around December 2022, when the Group decided to take up the whole batch of Ghana manganese ore, the Supplier topped up the discrepancy due to the sale to the third party. Both the Supplier and the freight forwarding agent in the dock confirmed that the Supplier had restored the quantity of the Ghana manganese ore from another batch of Ghana manganese ore before transfer the ownership thereof. There were no claims or litigation made against the Group by the Customer and/or other parties in relation to the same and the Independent Forensic Accountant also does not identify any material abnormalities.

The background and relationship of the Supplier and the Customer

Save that the supervisor of the Customer (who does not participate in the management of the Customer and is an acquaintance of the beneficial owner of the Supplier and the Customer) is also the supervisor of a company, of which the former legal representative and executive director of the Supplier is the ultimate beneficial owner, legal representative and executive director, the Independent Forensic Accountant does not identify other relationship between the Supplier and the Customer.

Based on the public searches made by the Independent Forensic Accountant on the Supplier and Customer, the ultimate beneficial owners of the Supplier and the Customer as well as the key persons of the aforesaid parties, each of the Supplier and the Customer

is third party independent of and not connected with the Group.

Issue 3

Prepayment made to the Supplier

A framework sales agreement for each year (but no individual sales agreement for each transaction) was entered into between the Group and the Supplier, with provisions regarding the amount of Ghana manganese ore to be purchased, the provisional price and the prepayment requirements. When the Supplier transfers the ownership of Ghana manganese ore to the Group, the Group would proceed to settlement, issue value added tax invoice, deduct purchase price from the prepayment. The prepayment would be made by the Group from time to time which had no direct correlation to the progress of the transfer the ownership of Ghana manganese ore to the Group.

The prepayment amount incurred in the domestic commodities trading in relation to the Manganese Ore Trading Business is mainly due to the contractual requirement under the framework sales agreements entered into with the Supplier. For instance, the Group entered into framework sales agreement (the “**2022 Framework Sales Agreement**”) with the Supplier in relation to the sale and purchase of 1,000,000 ($\pm 10\%$) wet metric tons Ghana manganese ore at the contract sum of approximately RMB1,140,700,000 on 27 October 2021. Pursuant to the terms of the 2022 Framework Sales Agreement, the Group was required to make prepayment in the sum of RMB1,083,665,000 (equivalent to 95% of the contract sum) to the Supplier from time to time. Part of such prepayment was satisfied by carrying forward the prepayment made pursuant to the framework sales agreement in prior year.

Prepayment to the Supplier from 31 December 2022 to 28 March 2023

The Group made prepayment of approximately RMB58 million to the Supplier from 31 December 2022 to 28 March 2023 in view of the quantity of the Ghana manganese ore to be purchased by the Group from the Supplier. Though the framework sales agreement for the year 2023 was not entered into at that time, the Group has already reached consensus with the Supplier on the purchase quantity of 1,000,000 wet metric tons Ghana manganese ore in order to comply with the Agency Agreement. The framework sales agreement for 2023 was subsequently entered into between the Group and the Supplier.

Having considered the prepayment of approximately RMB58 million paid by the Group to the Supplier from 31 December 2022 to 28 March 2023 before the entering into of the framework sales agreement for 2023, the Independent Forensic Accountant recommends the management of the Group to strengthen the procedure in relation to the Manganese Ore Trading Business, including but not limited to determining the pricing with the supplier and the customer, approval of sales agreement, making of prepayment.

The account receivable from the Customer

Individual sales agreement for each transaction (but no framework sales agreement for each year) was entered into between the Group and the Customer, and prepayment would be made based on the quantity and purchase price of the Ghana manganese ore under each transaction.

Despite the general requirement for prepayment before issuing delivery order to the Customer, the Group recorded an account receivable from the Customer of approximately RMB77 million as at 31 December 2022. Given the then upcoming Chinese New Year and the negative impact brought by COVID-19 across the PRC, the Customer was having a cash flow pressure and asked the Group to grant credit terms to the Customer only for this transaction. Having considered the previous good trading record of the Customer and the Customer being a major customer of the Group in relation to the Manganese Ore Trading Business, the Group granted credit terms to the Customer. The Customer subsequently settled the account payable in full by 13 March 2023.

Comparisons between the Supplier and the other suppliers of the Group

During the year ended 31 December 2022, the Supplier is the Group's sole supplier of the Ghana Manganese ore. The Group is not informed as to the supplier samples adopted by PwC in making comparison to the prepayment amount and aging of the Supplier and is of the view that other suppliers of the Group for bulk cargo trading are not suitable comparables.

Further, manganese carbonate ore is a high-grade manganese ore with relatively simple processing procedure, and is the best raw material for electrolytic manganese. Given that the Ghana manganese ore is the only manganese carbonate ore in the world with scarce supply, the Ghana manganese ore mine owners have a very strong bargaining

power in pricing. Moreover, as the PRC is one of the major manufacturers of electrolytic manganese which imports approximately 30 million tons manganese ore per year and has a high degree of dependency on import of approximately 80%, industry experts confirm that the level of prepayment paid by the Group to the Supplier is consistent with the industry norm in the PRC.

In fact, the Agency Agreement also requires the same level of prepayment and the high prepayment level for Ghana manganese ore is extended from the mine owners to the downstream companies.

Pattern of the transactions among the Group, the Supplier and the Customer

After the issuance of delivery order by the Supplier, the Group would proceed to settlement, issue value added tax invoice and deduct the settlement sum from the prepayment amount. As the Group and the Supplier only entered into framework sales agreement for a year but did not enter into separate contract regarding shipment of the Ghana manganese ore, the progress in making prepayment to the Supplier had no direct correlation with the transfer of ownership of the Ghana manganese ore from the Supplier.

Further, once a substantial amount of prepayment was made to the Supplier, having considered the risk exposure and cash management of the Group, the Group would only make further prepayment to the Supplier after securing the order from the Customer and obtaining prepayment from the Customer.

Communication with the Supplier about the details of prepayment, including payment amount and timing

Given PwC's concern on relying on verbal communication with the Supplier on the details of prepayment (including payment amount and timing and the lack of written documents recording the same), since March 2023, the Group reviewed and adopted remedial actions such that the communication between the Group and the Supplier and between the Group and the Customer (including whether to take up the Ghana manganese ore and the details of the delivery) is carried out by way of email.

Other findings by the Independent Forensic Accountant

The Independent Forensic Accountant noted that as at 31 May 2023, all the prepayment

made by the Group to the Supplier and amount receivable from the Customer has been settled, and the Group has not suffered any loss.

Further, the Independent Forensic Accountant also notes that the Manganese Ore Trading Business has complied with relevant internal approval processes and possesses complete records and traceable approvals. Also, the Manganese Ore Trading Business is profitable even taking into account the finance cost of the Group.

OPINION OF THE INDEPENDENT INVESTIGATION COMMITTEE

The Independent Investigation Committee has reviewed and considered the Independent Investigation Report. Having examined the Letter from PwC, the Independent Investigation Committee is of the view that the Independent Forensic Accountant has investigated into the Audit Issues to the extent that is practicable and the content and findings of the Independent Investigation are reasonable and acceptable. The Independent Forensic Accountant had performed appropriate procedures in respect of the Independent Investigation. The Independent Investigation Committee considers that the Audit Issues in respect of the Manganese Ore Trading Business have been adequately addressed. The Independent Investigation Committee suggests the Group to strengthen the procedure in relation to the Manganese Ore Trading Business, including but not limited to determining the pricing with the supplier and the customer, approval of sales agreement, making of prepayment in order to control the inherent risks.

OPINION OF THE BOARD

The Board has reviewed the content and the findings of the Independent Investigation Report. The Board concurs with the Independent Investigation Committee that and is of the view that the Independent Forensic Accountant has investigated into the Audit Issues raised by PwC and adequately addressed the concerns raised by PwC, and the findings of the Independent Investigation in the Independent Investigation Reports are reasonable and acceptable. The Board accepts the Independent Investigation Committee's suggestions to strengthen the procedure in relation to the Manganese Ore Trading Business in order to control the inherent risks.

CONTINUED SUSPENSION OF TRADING

At the request of the Company, trading in the shares of the Company on the Stock Exchange has been suspended with effect from 9:00 a.m. on 30 March 2023. Trading

in the shares of the Company will remain suspended until further notice

Shareholders and potential investors of the Company are advised to exercise caution when dealing in the securities of the Company.

By order of the Board
SOUTH MANGANESE INVESTMENT LIMITED
Li Weijian
Chairman and Chief Executive Officer

Hong Kong, 20 September 2023

As at the date of this announcement, the executive Directors are Mr. Li Weijian, Mr. Zhang He, Mr. Xu Xiang and Mr. Li Junji; the non-executive Directors are Ms. Cui Ling and Mr. Pan Shenghai; and the independent non-executive Directors are Mr. Zhang Yupeng, Mr. Yuan Mingliang and Mr. Lo Sze Hung.