

HAFARY HOLDINGS LIMITED

(Company Registration No: 200918637C)

(Incorporated in the Republic of Singapore)

RESPONSE TO QUESTIONS RECEIVED ON THE ANNUAL REPORT

The Board of Directors (the "**Board**") of Hafary Holdings Limited (the "**Company**", and together with its subsidiaries, the "**Group**") wishes to provide the following response to the questions received in connection with the Company's Annual Report 2021 released via SGXNet on 23 March 2022 (the "**Annual Report 2021**").

The Company's responses to the collective questions received are as follows:-

A. QUESTIONS RELATING TO THE COMPANY'S OPERATIONS AND FINANCIAL MATTERS

Question 1

Would the board/management provide shareholders with greater clarity on the following operational and financial matters? Specifically:

- (i) General segment: Revenue from the segment increased by 53.4% to \$82.7 million. Does management expect this strong demand in the general segment to be sustainable? In addition, can management elaborate further on its digital strategy, including how it is leveraging social media? How successful is its Hafary app?
- (ii) Project segment: Revenue from the project segment reversed 4 years of decreases (from FY2017 to FY2020) and increased by 60% to \$43.3 million. The profit margin from the project and general segments was 4.5% (ORBIT/revenue) and 11.5% respectively. How can management improve the profitability of the project segment?
- (iii) Vietnam: Can management help shareholders understand the sentiments on the ground in Vietnam, especially with the spread of the Omicron variant? How affected was Viet Ceramics International Joint Stock Company ("VCI") and what is the pace of re-opening in Vietnam? Are there plans in the future to monetise the group's investment in VCI perhaps via a listing?
- (iv) Myanmar: What is the business and operating environment in Myanmar? Is Hafary Myanmar Co. Ltd, the joint venture company, self-sustaining? If not, how much more capital will the group be committing to it?
- (v) Please refer to page 21 of the Annual Report about "Financial review". Under "Impairment Losses" subtitle, it was stated that "The impairment losses increased by S\$4.1 million or 93.0% from S\$4.4 million during FY2020 to S\$8.5 million during FY2021. The impairment allowance for slow-moving inventories is based on the age of these inventories, the prevailing market demand of the inventory category and the deterioration of the products based on past experience." May I ask the Audit Committee what were these "slow-moving inventories" in FY2021?

Impairment of inventories: In the past years, the allowance for impairment of inventories have trended up: from \$472,000 (FY2016), \$1,499,000 (FY2017), \$1,259,000 (FY2018), \$1,012,000 (FY2019), \$4,068,000 (FY2020) to \$7,614,000 (FY2021). The assessment of impairment allowance on inventories is a key audit matter highlighted by the independent auditor in their report on the audit of the financial statements. Can the audit committee help shareholders understand if the impairment assessment method or criteria has changed? What caused the significant increase in inventory impairment in FY2020 and in FY2021? Was the under-recognition of impairment in prior years? What is the average age of the group's inventories?

Response:

- (i) As stated on page 20 of the Company's Annual Report 2021, the increase in revenue from the general segment was attributable to an active resale market, robust demand from home buyers who preferred the certainty of acquiring their properties in the resale market due to the construction delays relating to Build-To-Order properties, as a result of manpower shortages and supply chain disruptions.

With the reopening of Singapore's borders on 1 April 2022, management is cautiously optimistic that this could lead to stronger demand in the general segment as well as the construction sector. Nevertheless, Management continues to monitor developments closely.

The Company has leveraged on social media to promote its latest products, promotions and events to its existing and potential new customers. With the introduction of the Hafary app back in 2019, users have access to more than 5,000 quality products including tiles, stone, mosaic, wood and vinyl and are able to curate such products in a personalized project list, maintained on the Hafary app, for future reference and sharing with friends, family and other industry professionals. Management continues to promote the app to new and existing customers.

- (ii) Profitability of the project segment varies depending on the size of each project, the nature of each project as well as the market demand at the relevant point of time. Before entering into any supply contract with its customers, Management assesses the potential viability and profitability of a project, and, to the extent possible, ensures that pricing terms have been agreed with its suppliers, in order to minimize any unexpected increase in costs or disruptions to production.
- (iii) With the re-opening of Vietnam's border on 15 March 2022, Management expects economic activities to robust in Vietnam, and is cautiously optimistic that this may lead to a strong recovery of VCI Vietnam.

At this stage, Management has no plans to monetize the Group's investment in VCI via a listing in the foreseeable future.

- (iv) COVID-19 and the political situation in Myanmar continue to hamper the business activities of Hafary Myanmar Co. Ltd.

At this stage, the Company is unlikely to increase its capital contribution to Hafary Myanmar Co. Ltd.

- (v) The “slow-moving” inventories refer to inventories that have minimal or no movement and have not had any considerable subsequent sales or orders.

Management assess the allowance for impairment of inventories on an ongoing basis. This assessment requires a degree of estimation and judgement. The level of the loss allowance is assessed by taking into account the recent sales experience, the ageing of inventories, other factors that affect inventory obsolescence and subsequent events (including the impact of the COVID-19 pandemic). Of these inventories, substantial impairment allowance has been made for slow-moving inventories. The impairment allowance for slow-moving inventories is based on the age of these inventories, the prevailing market demand of the inventory category, deteriorating ageing profile of inventories and the deterioration of the sale of the products based on past experience.

Management continuously assesses the Group's inventory impairment policy, to ensure the impairment policy is reflecting the current economic conditions, and has, in prior FYs, applied the same methodology in determining the value of the allowance for the impairment for inventories.

The Audit Committee (“**AC**”) has reviewed the methodologies used by Management in assessing the value of the allowance for the impairment for inventories, and is of the opinion that the methodologies used to determine the value of the impairment are reasonable.

The AC noted that the external auditor has carried out a review of the methodologies used by Management in determining the value of the impairment. The external auditor has assessed the Management’s judgement and assumptions applied to comply with the Group’s inventory allowance policy by analysing the historical data trend as well as performing analytical procedures on the inventory aging profile.

The significant increase in inventory impairment in FY2020 and FY2021 was mainly contributed by inventories that have minimal or no movement and have not had any considerable subsequent sales or orders. Following the impairment assessment, such inventory impairment was recognised in FY2021 and FY2020 respectively.

Please refer to the page 24 of the Company’s Annual Report 2021 for the average age of the Group’s inventories as at 31 December 2021.

Question 2

Please refer to page 21 of the Annual Report about “Financial review”. Under “Cost of Sales” subtitle, it was stated that “The gross profit margin had improved from 45.4% in FY2020 to 46.5% in FY2021.” Nevertheless, has the Group been facing cost inflationary pressures, especially from materials, recently?

Response:

The Group expects to face increasing inflationary pressures moving forward, in line with global trends. Nevertheless, the Group is committed to maximizing shareholder value and believes that it has the necessary experience and expertise to continue to do so.

Question 3

Has the Group been affected by supply chain disruptions, particularly from shipping?

Response:

As the Group sources its raw materials from various countries, some of the Group's operations have been affected by such global supply change disruptions. The Group continues to monitor the situation and will make the appropriate announcements in the event such disruptions are material.

Question 4

Please refer to page 93 of the Annual Report about “Geographical information”. Why revenue from the top overseas country (Cambodia) declined by 75.2% from \$5.337m in 2020 to \$1.322m in 2021?

Response:

Revenue derived from Cambodia pertains to the Group's delivery of its products to building projects in Cambodia. More of such projects completed in FY2020, as compared with FY2021. As such, revenue from Cambodia declined in FY2021 as compared with FY2020.

Question 5

Please refer to page 96 of the Annual Report about “Impairment losses”. May I ask the Audit Committee what was the nature of this “Allowance for impairment of other receivables” of \$350K in 2021?

Response:

As disclosed in page 110 of the Annual Report, the allowance for impairment of \$350,000 is on the non-trade receivable from the Group's joint venture in Myanmar. Management is of the view that such amounts may not be recovered from the Myanmar joint venture in the foreseeable future and as such has made the necessary allowance for impairment.

Question 6

Please refer to page 25 of the Annual Report about “Financial review” about “Leasehold properties held by the Group”. What will happen to the warehouse at “54/56 Sungei Kadut Loop Singapore 729477”, as well as the marble processing facility at “18C Sungei Kadut Street 4” when their land tenures expire in 3 years’ time (2025) respectively?

Response:

The lease for our existing warehouses located at 54/56 Sungei Kadut Loop and 18C Sungei Kadut Street 4 (“the sites”) will expire on 15 January 2025 and 15 September 2025 respectively.

JTC is unable to extend the lease term for the sites and the sites will have to be returned to JTC when the lease expires.

Question 7

Please refer to page 124 of the Annual Report about “Capital commitments”. How will the “capital commitments” trend be like over the next 2-3 years? How will they be funded?

Response:

As part of the Company’s ordinary course of business and in line with the Group’s business expansion plan, capital expenditure is budgeted for investment on long term assets which will be supported by both internal and external sources of finance.

B. QUESTIONS RELATING TO WFH AND THE GROUP’S ACQUISITION OF 35.0% OF WFH

Question 8

Please refer to page 106 of the Annual Report about “Investments in subsidiaries”. Why has World Furnishing Hub Pte Ltd (“WFH”) been in a net liabilities position for both 2020 and 2021? Is there any going concern issue?

Response:

The net liabilities position for both 2020 and 2021 is mainly due to WFH incurring losses prior to 2020 as the rental occupancy rate was insufficient to cover total expenses.

With reference to page 105 and 106 of the Annual Report 2021, WFH had been generating positive cash inflow from its operating activities and was profitable for FY2020 and FY2021. There are no going concern issues.

Question 9

Please refer to page 132 of the Annual Report about “Events after the end of the reporting year”. It was stated that “On 17 January 2022, the wholly-owned subsidiary of the company, Hafary Pte Ltd (“HPL”) acquired an additional shareholdings of 30% in WFH for a consideration of \$3.020,000. WFH became 81% owned subsidiary of HPL on 17 January 2022.” This effectively values WFH (on a 100%-basis) at \$10.07m, despite having a net liabilities position of -\$3.828m as at 31 Dec 2021. Can the Board share the basis of the valuation of WFH shares with respect to its net liabilities position?

Question 10

The Group has been increasing its stake in World Furnishing Hub Pte. Ltd. (“WFH”). Prior to the increased stake, the company owns 46% of WFH but consolidates WFH as a subsidiary as it has management control of WFH.

Following two acquisitions in December 2021 and January 2022, the company now owns 81% of WFH.

As at 31 December 2021, the carrying amount of the 49% non-controlling interests in WFH was \$(1.88) million. WFH remains in a net liabilities position of \$(3.83) million as at 31 December 2021. In fact, WFH had current assets of \$292,000 and current liabilities of \$(8.97) million.

- (i) Can the board/management elaborate further on the financial position of WFH? In particular, does WFH have the necessary working capital to continue as a going concern?
- (ii) What is the current/committed occupancy rate at the World Furnishing Hub?
- (iii) Given that WFH has been in a net liabilities position, how did the board value the sale shares? Was a valuation of the sale shares carried out prior to the acquisitions?

For the first acquisition from Sitra Agencies Pte Ltd (“Sitra”), the company paid the seller \$3.7 million for a 10% stake in WFH (the “Sitra Shares”).

In the second acquisition from Mr Ching Chiat Kwong (“Mr Ching”), the company acquired the seller’s 25% interest in WFH for a consideration of \$1.17 million along with the assignment of \$1.1 million in shareholder’s loan (the “Ching Shares”).

- (iv) Can the board/audit committee clarify if there has been a decrease in the valuation of the sale shares after the first acquisition?
- (v) What is the total amount invested in WFH for the 81% stake?
- (vi) What is the strategic value of underlying asset at 18 Sungei Kadut Street 2 – World Furnishing Hub?

Response to Question 9 and 10:

- (i) As disclosed in page 105 of the Annual Report 2021, WFH was profitable for FY2020 and FY2021. WFH's current liabilities mainly consist of outstanding amounts owing to WFH's shareholders and rental deposits.
- (ii) The occupancy rate of WFH is approximately 99% as at the date of this announcement.
- (iii) Please refer to the Company's announcements dated 24 March 2021 and 29 December 2021, which set out the factors taken into account at arriving at the consideration paid by the Group for the Sitra's and Mr Ching's shares in WFH respectively.

The Company wishes to reiterate that the Company's acquisition of the Sitra Shares and the Company's acquisition of the Ching Shares were separate and distinct transactions, with the Company dealing separately with Sitra (in respect of the Sitra Shares) and with Ching (in respect of the Ching Shares) and different points in time.

In relation to the consideration paid for the Sitra Shares, as disclosed in the Company's announcement dated 24 March 2021, the Company had in 2013 granted Sitra a put option in respect of its shares in WFH at the market value of the property at the date of exercise. It was against this context that Company had agreed with Sitra on the consideration payable for its shares in WFH.

As disclosed in the Company's announcement dated 24 March 2021, the parties had relied on the market value of the unencumbered remaining leasehold interest in the Property that was conducted by Knight Frank Pte Ltd as at 18 November 2020, among other factors, in arriving at the consideration.

- (iv) The consideration paid by the Company for the shares in WFH represents the outcome of arm's length negotiations between the Company and each of Sitra and Mr Ching.
- (v) The total amount invested in WFH for the 81% stake is \$5,381,000.
- (vi) WFH is within JTC Corporation's green masterplan to transform and revamp Sungei Kadut into one-of-a-kind eco-district.

Management recognizes the performance and continuing potential of WFH and is of the view that the Company will benefit from better operational productivity and cost efficiencies. The acquisitions would allow the Company to consolidate a higher percentage of WFH's financial results and performance in the future, and may improve the Company's profitability and enhance shareholders' value in the long term.

C. QUESTIONS RELATING TO THE REMUNERATION OF DIRECTORS AND EXECUTIVE OFFICERS

Question 11

Please refer to page 54 of the Annual Report about “Corporate governance statement”. Despite still being a Covid year, the remuneration of Executive Director Mr Low Kok Ann has increased from “S\$250,000 to S\$499,999” in 2020 to “S\$750,000 to S\$999,999” in 2021. Can the Remuneration Committee share what remuneration factor(s) specifically led to the increase? How much is attributable to each of these remuneration factor(s)?

Response:

As disclosed in the Corporate Governance Statement on page 51 of the Annual Report 2021, The Executive Director and CEO does not receive Director’s fees and is paid based on his Service Agreement with the Company. In setting the remuneration packages of the Executive Director and CEO, the Company takes into account the performance of the Group and that of the Executive Director and CEO which is aligned with long term interest of the Group. There is no change in the formula computation of his remuneration package between FY2020 and FY2021. The amount of variable bonus payment (i.e. performance bonus) for a particular financial period is dependent on the amount of the Group’s profit before income tax achieved as set out below:

Profit before income tax (“PBT”)	Performance bonus
Up to S\$3 million	1.5% of PBT
Above S\$3 million and up to S\$5 million	S\$45,000 plus 3.0% of PBT in excess of S\$3 million
Above S\$5 million	S\$105,000 plus 4.5% of PBT in excess of S\$5 million

The Group registered a net PBT of S\$15,133,000, a jump of 141.7% in FY2021 as compared to net PBT of S\$6,260,000 in FY2020, hence, the increase in the CEO’s remuneration is in-line with the increase in net profit generated.

Question 12

Please refer to page 54 of the Annual Report about “Corporate governance statement”. Despite still being a Covid year, the remuneration of Project Director Mr Goh Keng Boon Frank and Public Project Director Mr Tay Eng Kiat Jackson have each increased from “Below S\$250,000” in 2020 to “S\$250,000 to S\$499,999” in 2021. Can the Remuneration Committee share what remuneration factor(s) specifically led to the increase? How much is attributable to each of these remuneration factor(s)?

Response:

As disclosed in the Corporate Governance Statement on page 52 of the Annual Report 2021, the remuneration package for key management personnel is linked to the performance of the Company and the individual.

The Group registered a net PBT of S\$15,133,000, a jump of 141.7% in FY2021 as compared to net PBT of S\$6,260,000 in FY2020, hence, the increase in the key management's remuneration is also in-line with the increase in net profit generated.

D. QUESTIONS RELATING TO BOARD RENEWAL

Question 13

At the annual general meeting scheduled to be held on 7 April 2022, Mr Terrance Tan Kong Hwa will be retiring pursuant to article 104 of the company's constitution and will be seeking his re-election as an independent director.

The profile of the directors can be found on pages 12 to 15 of the annual report. Additional information on directors seeking re-election can be found on pages 135 to 153,

Mr Terrance Tan Kong Hwa was first appointed to the board 10 November 2009.

On 30 November 2021, Mr Tan Boon Gin, chief executive of Singapore Exchange Regulation, gave guidance that companies are expected to use the two-tier rule sparingly to promote renewal and succession planning¹.

- (i) Can the nominating committee (NC) help shareholders understand if the proposed nomination of Mr Terrance Tan Kong Hwa will delay the progressive renewal of the board?

As disclosed in the Notice of meeting for the AGM (dated 31 March 2021), the authority conferred by the passing of resolution 15 on the continued appointment of Mr Terrance Tan Kong Hwa as independent director of the company for the purposes of Rule 210(5)(d)(iii) (B) of the Listing Manual of the SGX-ST will continue in force until the retirement or resignation of Mr Terrance Tan Kong Hwa as director.

- (ii) Will the company confirm that Mr Terrance Tan Kong Hwa is not seeking a two-tier vote by shareholders for his continued appointment as independent director?
- (iii) Given that no such two-tier vote is sought for Mr Terrance Tan Kong Hwa at the AGM to be held on 7 April 2022, if re-elected, would the director be deemed non-independent?

In addition, as the independent chairman of the board, Mr Ong Beng Chye has been on the board for more than 12 years since his appointment in November 2009.

- (iv) Would Mr Ong Beng Chye be holding himself to higher governance standards and lead by example, especially in setting the tone with regard to the tenure of independent directors?
- (v) Would the NC provide shareholders with greater clarity on the near-term plans to facilitate the progressive renewal of the board in view of the guidance from SGX RegCo?
- (vi) Can the NC explain how the sourcing of candidates "through an extensive network of contacts" would support the company's diversity policy?

¹ <https://www.businesstimes.com.sg/companies-markets/answer-my-question-before-i-vote-sgx-regco-sets-new-timelines-for-companies-to>

Response:

The proposed nomination of Mr Terrance Tan Kong Hwa will not delay the progressive renewal of the Board. The Company notes (a) the appointment of Mr Foo Yong How, and the retirement of Mr Chow Wen Kwan, each as Independent Directors, in 2020; (b) the appointment of Mr Yong Teak Jan @ Yong Teck Jan as a Non-Independent Non-Executive Director in 2018; and (c) the appointment of two Non-Executive Directors, namely Datuk Edward Lee Ming Foo and Ms Cheah Yee Leng, in 2015, each of whom were appointed to address the evolving needs of the Company and who has and continues to contribute their respective functional skill sets and domain expertise to support the Company's strategy and business.

The NC continues to assess board diversity on an ongoing basis and will, in the event suitable candidates are available, make the appropriate changes to promote renewal and succession planning of the Board. This is a continuous process. On the other hand, the Board recognises that Independent Directors may over time develop significant insights in the Group's business and operations and can continue to provide noteworthy and valuable contribution objectively to the Board as a whole.

The Company also notes that Mr Terrance Tan Kong Hwa was subject to the two-tier voting procedure at the Company's last AGM on 14 April 2021 and his re-election as Director at the current AGM is pursuant to Regulation 104 of the Company's Constitution. As such, the authority conferred on Mr Tan's continued appointment as Independent Director shall cease in the event the resolution on Mr Tan's re-election as Director is not approved by the shareholders at the upcoming AGM, in which case his retirement as Director will take place after the conclusion of the upcoming AGM.

The Board is of the view that the independence of the independent directors must be based on the substance of their professionalism and integrity, and should not merely based on the number of years of service. With the concurrence of the NC, the Board is of the view that Mr Ong Beng Chye has demonstrated strong independent character and judgment over the years in discharging his duties and responsibilities as an Independent Director of the Company, and has no reason to believe that he would not be able to continue to do so moving forward.

The NC assesses suitable candidates based on the strength of his or her caliber, experience, grasp of corporate strategy and potential to contribute to the Company and its businesses. Each Director brings valuable insights from different perspectives, such as strategic planning, management, finance, accounting and legal, vital to the strategic interests of the Company. Given that each member of the Board has considerable experience, and, by extension, an extensive network of contacts, the NC leverages on such contacts in considering suitable candidates to promote board diversity. If the NC decides that the candidate is suitable, the NC then recommends its choice to the Board. Meetings with such candidates may be arranged to facilitate open discussion.

By Order of the Board

Low Kok Ann
Executive Director and CEO
3 April 2022