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## SAN MIGUEL BREWERY HONG KONG LTD.

香港生力啤酒廠有限公司

*(Incorporated in Hong Kong with limited liability)*

(Stock Code: 236)

### CONTINUING CONNECTED TRANSACTIONS

The Group has been carrying out certain continuing connected transactions with the San Miguel Group including, among other things, (i) purchase by the Group from the San Miguel Group of (a) packaging materials for the production of the Group and (b) alcoholic and non-alcoholic beverage products for the Group's wholesale and retail distribution; and (ii) sales of packaged beer and non-alcoholic beverage products by the Group to the San Miguel Group. Such transactions constitute continuing connected transactions for the Company in its ordinary and usual course of business. As set out in the announcements of the Company dated 6 December 2007 and 11 May 2009 and the circulars of the Company dated 20 December 2007 and 29 May 2009, the Company entered into the 2007 Agreement on 6 December 2007 and the 2009 Agreement on 11 May 2009 setting out the terms of the continuing connected transactions between the Group and the San Miguel Group as described in items (i) and (ii) above. Both the 2007 Agreement and 2009 Agreement will expire on 31 December 2010. Accordingly, the Company and SMC entered into the New Agreement dated 15 October 2010 with a view to renewing the agreement to carry out the Continuing Connected Transactions from 1 January 2011 to 31 December 2013 on substantially the same terms as those under the 2007 Agreement and 2009 Agreement.

As at the date of this announcement, the San Miguel Group controls approximately 65.78% of the issued share capital of the Company. SMC and its associates are therefore connected persons of the Company for the purposes of the Listing Rules. The Continuing Connected Transactions under the New Agreement constitute non-exempt continuing connected transactions under the Listing Rules and are subject to the annual review requirements under Rules 14A.37 to 14A.39, the reporting requirements under Rules 14A.45 to 14A.47, and the approval of the Independent Shareholders requirements under Rule 14A.48 of the Listing Rules.

An independent board committee comprising Dr. The Hon. Sir. David K.P. Li, Mr. Ng Wai Sun and Mr. Carmelo L. Santiago has been established to advise the Independent Shareholders in respect of the terms of the New Agreement, the Continuing Connected Transactions and the Caps. KBC Bank has been appointed as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders on whether the terms of the New Agreement, the Continuing Connected Transactions and the Caps are on normal commercial terms, in the ordinary and usual course of business, fair and reasonable and in the interests of the Company and its Shareholders as a whole.

A circular containing the particulars of the New Agreement, the Continuing Connected Transactions, the Caps, the advice from the Independent Board Committee to the Independent Shareholders, the advice from KBC Bank to the Independent Board Committee and the Independent Shareholders and a notice convening the EGM to approve the terms of the New Agreement, the Continuing Connected Transactions and the Caps will be despatched to the Shareholders on or before 8 November 2010.

## **BACKGROUND**

The principal business activities of the Group are the production and distribution of bottled, canned and draught beers and other beverage products. SMC is the ultimate controlling shareholder of the Company. SMC is one of the Philippines' most diversified conglomerates with operations in beverages, food, packaging, energy, power, mining, telecommunications and infrastructure.

The Group has been carrying out certain continuing connected transactions with the San Miguel Group including, among other things, (i) purchase by the Group from the San Miguel Group of (a) packaging materials for the production of the Group and (b) alcoholic and non-alcoholic beverage products for the Group's wholesale and retail distribution; and (ii) sales of packaged beer and non-alcoholic beverage products by the Group to the San Miguel Group. Such transactions constitute continuing connected transactions for the Company in its ordinary and usual course of business. As set out in the announcements of the Company dated 6 December 2007 and 11 May 2009 and the circulars of the Company dated 20 December 2007 and 29 May 2009, the Company entered into the 2007 Agreement on 6 December 2007 and the 2009 Agreement on 11 May 2009 setting out the terms of the continuing connected transactions between the Group and the San Miguel Group as described in items (i) and (ii) above. Both the 2007 Agreement and 2009 Agreement will expire on 31 December 2010. Accordingly, the Company and SMC entered into the New Agreement dated 15 October 2010 with a view to renewing the agreements to carry out the Continuing Connected Transactions from 1 January 2011 to 31 December 2013 on substantially the same terms as those under the 2007 Agreement and 2009 Agreement.

Under the 2007 Agreement, the continuing connected transactions between the Group and the San Miguel Group comprise (i) purchase of packaging materials (comprising, but not limited to, cans, bottles, crown seals and crates) by the Group from the San Miguel Group and (ii) purchase of alcoholic and non-alcoholic beverage products by the Group from the San Miguel Group.

Under the 2009 Agreement, the continuing connected transactions between the Group and the San Miguel Group comprise sales of packaged beer and non-alcoholic beverage products by the Group to the San Miguel Group. Both the 2007 Agreement and 2009 Agreement shall expire on 31 December 2010.

## **THE NEW AGREEMENT**

### **Date**

15 October 2010

### **Parties**

The Company and SMC

### **Continuing Connected Transactions and the Caps**

Under the New Agreement, the Group will enter into the following Continuing Connected Transactions with the San Miguel Group: (i) purchase by the Group from the San Miguel Group of packaging materials (including, but not limited to, cans, bottles, crown seals and crates) and packaged beer; and (ii) sales of packaged beer and non-alcoholic beverage products by the Group to the San Miguel Group.

## **Term**

Subject to the Independent Shareholders' approval on the Continuing Connected Transactions, the New Agreement and the proposed Caps, the New Agreement shall have a term ending on 31 December 2013 and its terms shall apply to the Continuing Connected Transactions for the period commencing on 1 January 2011 to 31 December 2013. In the event that the New Agreement, Continuing Connected Transactions and the Caps are not approved by the Independent Shareholders, the Company has the right to terminate the New Agreement.

## **Pricing**

The Company confirms that the pricing policy of the Company in respect of the Continuing Connected Transactions is on an arm's length basis and is consistent with the Group's historical pricing policy in respect of the past transactions between the Group and the San Miguel Group, which are described below:

### *(a) Purchase of packaging materials from the San Miguel Group*

In respect of the purchase of packaging materials (comprising, but not limited to, cans, bottles, crown seals and crates) by the Group from the San Miguel Group, the basis of the prices payable by and the credit terms offered to the Group have historically been negotiated and shall continue to be negotiated between the Group and the San Miguel Group on an annual basis with reference to the prices and credit terms available from suppliers which are independent third parties and are able to meet the Group's stringent quality requirements and delivery schedules and if no such comparable reference prices/credit terms are available, the prices/credit terms shall be determined by arm's length negotiations between the Group and the San Miguel Group based upon reasonable commercial principles.

### *(b) Purchase of packaged beer from the San Miguel Group*

In respect of the purchase of packaged beer by the Group from the San Miguel Group, the prices payable by and the credit terms offered to the Group have been and shall continue to be determined by reference to the prices paid by and the credit terms offered to the Group in respect of similar products sourced by the Group from suppliers which are independent third parties and if no such comparable reference prices/credit terms are available, the prices/credit terms shall be determined by arm's length negotiations between the Group and the San Miguel Group based upon reasonable commercial principles.

### *(c) Sales of packaged beer and non-alcoholic beverage products to the San Miguel Group*

In respect of the sales of packaged beer and non-alcoholic beverage products by the Group to the San Miguel Group, the prices receivable by the Group have been and shall continue to be determined in the ordinary and usual course of business based on the Group's production cost plus profit margins. Such profit margins are determined with reference to profit margins which are no less favourable to the Group than those imposed by the Group on independent third party customers in respect of the sales of similar packaged beer and non-alcoholic beverage products, and if no such comparable profit margins are available, the profit margins shall be determined by arm's length negotiations between the Group and the San Miguel Group based upon reasonable commercial principles.

The credit terms offered by the Group for the sales of packaged beer and non-alcoholic beverage products to the San Miguel Group have been and shall continue to be determined by reference to the credit terms offered by the Group to its independent third party customers, and if no such comparable credit terms are available, the credit terms shall be determined by arm's length negotiations between the Group and the San Miguel Group based on reasonable commercial principles.

There is no provision in the New Agreement requiring the Group to exclusively source packaging materials and packaged beer from the San Miguel Group nor sell the packaged beer and non-alcoholic beverage products to the San Miguel Group.

The Directors (excluding the independent non-executive Directors who will express their view after receiving advice from KBC Bank) consider that the Continuing Connected Transactions are entered into in the ordinary course of business of the Group and the terms of the New Agreement are on normal commercial terms, fair and reasonable and are in the interests of the Company and the Shareholders as a whole.

## **REASONS FOR THE CONTINUING CONNECTED TRANSACTIONS**

The Group sources various packaging materials including cans, bottles, crown seals and crates for use in the packaging and distribution of its beer products. The San Miguel Group has established itself as a competitively priced and dependable supplier to the Group which meet the Group's stringent quality requirements and delivery schedules.

The Group purchases packaged beer from San Miguel Brewery, Inc., a company owned as to 51% by SMC to complement the range of products sold by the Group. The Group believes that this will enhance the product range and earnings potential of the Group.

San Miguel Brewery, Inc. is a company listed on The Philippine Stock Exchange, Inc. and is principally engaged in the manufacture and sale of fermented and malt-based beverages, particularly beer of all kinds and classes. San Miguel Brewery, Inc. runs the domestic brewery business of the San Miguel Group in the Philippines.

The packaged beer and non-alcoholic beverage products sold by the Group to the San Miguel Group are produced at the Group's plants located at (i) Shunde District, Foshan City, Guangdong Province, the PRC and (ii) Yuen Long, Hong Kong. The Group sells such packaged beer overseas to widen its income source. However, the Group does not have an international sales force outside Hong Kong and Macau. The Group is able to reach customers in export markets through the San Miguel Group which markets and sells products to customers through its international sales channels. Accordingly, the Group may sell its products, through the San Miguel Group, to certain export markets where the Group will also avoid taking exchange rate risk and counterparty risk with the ultimate customers in the relevant export markets. The Company expects such arrangement will help broaden market shares of the Company's products overseas.

## HISTORICAL VALUES AND ANNUAL CAPS

Set out below is a summary of (i) the amounts of the continuing connected transactions between the Group and the San Miguel Group for the two years ended 31 December 2009 and the nine months ended 30 September 2010, (ii) the relevant cap amounts under the 2007 Agreement and the 2009 Agreement and (iii) the proposed Caps under the New Agreement for the three years ending 31 December 2013:

| HK\$'000  | Year ended<br>31 December 2008 |               | Year ended<br>31 December 2009 |               | Actual<br>amount from<br>1 January<br>2010 to<br>30 September<br>2010 | Year ending<br>31 December<br>2010 | Caps for the three years ending<br>31 December 2013 pursuant to the New Agreement               |        |         |         |
|---|--------------------------------|---------------|--------------------------------|---------------|---|------------------------------------|---|--------|---------|---------|
|   | Actual<br>amount<br>(audited)  | Cap<br>amount | Actual<br>amount<br>(audited)  | Cap<br>amount |   | Cap<br>amount                      | 2011  | 2012   | 2013    |         |
| Purchase of packaging materials by the Group from the San Miguel Group                                      | 20,906                         | 42,100        | 27,973                         | 52,000        | 29,836  | 60,000                             | Purchase of packaging materials by the Group from the San Miguel Group                          | 47,000 | 54,000  | 61,000  |
| Purchase of alcoholic and non-alcoholic beverage products by the Group from the San Miguel Group            | 3,906                          | 7,500         | 3,874                          | 8,200         | 3,403   | 9,200                              | Purchase of packaged beer by the Group from the San Miguel Group                                | 4,900  | 5,300   | 5,700   |
| Sales of packaged beer and non-alcoholic beverage products by the Group to the San Miguel Group<br>(Note 1) | N/A                            | N/A           | 27,372                         | 105,954       | 35,151  | 183,583                            | Sales of packaged beer and non-alcoholic beverage products by the Group to the San Miguel Group | 97,000 | 103,000 | 108,000 |

*Note 1:* an agreement dated 11 March 2005 was entered into between the Company and SMC in relation to, inter alia, the continuing connected transactions regarding the sales of packaged beer by the Group to the San Miguel Group and which expired on 31 December 2007. The packaged beer sold by the Group to the San Miguel Group was produced at the Company's Hong Kong plant. The brewing operations of the Company's plant in Hong Kong ceased in 2007 and the sales of packaged beer by the Group to the San Miguel Group was discontinued. Accordingly, no such continuing connected transaction was recorded in 2008. Subsequently, brewing operations of the Company's Hong Kong plant have been resumed since April 2009 and the Company planned to produce non-alcoholic beverage products in the said plant as well. Accordingly, sales of packaged beer by the Group to the San Miguel Group have been resumed in 2009 and sales of non-alcoholic beverage products was included in the continuing connected transactions. The 2009 Agreement was entered into to set out the cap amounts for the two years ending 31 December 2010 in relation to the sales of packaged beer and non-alcoholic beverage products by the Group to the San Miguel Group.

In respect of the Caps in relation to the purchase of packaging materials and packaged beer by the Group from the San Miguel Group, the proposed Caps were determined by reference to a number of factors including, among other things, the historical sales amount of beer products, the marketing plan of the Group's products, the expected growth in demand for the Group's products (after taking into account the possible exchange rate fluctuations and the possible inflation) and the consequential increase in the need for the relevant packaging materials to meet the Group's production requirements.



In respect of the Caps in relation to the sales of packaged beer and non-alcoholic beverage products by the Group to the San Miguel Group, the proposed Caps were determined by reference to a number of factors including, among other things, the historical product lines, the expected demand for the Group's products and the Company's expectations on the demand for the Group's packaged beer and non-alcoholic beverage products for export markets after having discussed with the San Miguel Group, the expected costs of production and distribution, the expected selling margin, the possible exchange rates fluctuations and the possible inflation.

Buffer of 10% has been built in when the Caps were determined with a view to taking into account possible further market demand.

## **GENERAL**

As at the date of this announcement, the San Miguel Group controls approximately 65.78% of the issued share capital of the Company. Accordingly, SMC and its associates are connected persons of the Company for the purposes of the Listing Rules. The Continuing Connected Transactions under the New Agreement constitute non-exempt continuing connected transactions under the Listing Rules and are subject to the annual review requirements under Rules 14A.37 to 14A.39, the reporting requirements under Rules 14A.45 to 14A.47, and the approval of the Independent Shareholders requirements under Rule 14A.48 of the Listing Rules.

An EGM will be convened to seek Independent Shareholders' approval for the terms of the New Agreement, the Continuing Connected Transactions and the Caps. In view of the interest of the San Miguel Group in the Continuing Connected Transactions, SMC and its associates (as defined in the Listing Rules), which control approximately 65.78% of the issued share capital of the Company, will abstain from voting at the EGM. The votes to be taken at the EGM will be taken by poll, the results of which will be announced after the EGM. The Independent Board Committee comprising Dr. The Hon. Sir. David K.P. Li, Mr. Ng Wai Sun and Mr. Carmelo L. Santiago has been established to advise the Independent Shareholders in respect of the terms of the New Agreement, the Continuing Connected Transactions and the Caps. KBC Bank has been appointed as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders on whether the terms of the New Agreement, the Continuing Connected Transactions, and the Caps are on normal commercial terms, in the ordinary and usual course of business, fair and reasonable and in the interests of the Company and its Shareholders as a whole.

A circular containing the particulars of the New Agreement, the Continuing Connected Transactions, the Caps, the advice from the Independent Board Committee to the Independent Shareholders, the advice from KBC Bank to the Independent Board Committee and the Independent Shareholders and a notice convening the EGM to approve the terms of the New Agreement, the Continuing Connected Transactions and the Caps will be despatched to the Shareholders on or before 8 November 2010.

*As at the date of this announcement, the Board of the Company comprises the executive director, Mr. Peter K. Y. Tam, the non-executive directors, Mr. Ramon S. Ang (Chairman), Mr. Carlos Antonio M. Berba (Deputy Chairman), Mr. Cheung Yuen Tak, Mr. Thelmo Luis O. Cunanan Jr., General Benjamin P. Defensor, Jr., Mr. Motoyasu Ishihara, Mr. Taro Matsunaga and Mr. Keisuke Nishimura; and the independent non-executive directors, Dr. The Hon. Sir. David K. P. Li, Mr. Ng Wai Sun and Mr. Carmelo L. Santiago.*

## DEFINITIONS

Unless the context requires otherwise, the use of capitalised terms in this announcement shall have the following meanings:

|                                     |  |
|-------------------------------------|--|
| “2007 Agreement”                    | the agreement dated 6 December 2007 entered into between the Company and SMC in respect of (i) purchase of packaging materials by the Group from the San Miguel Group and (ii) purchase of alcoholic and non-alcoholic beverage products by the Group from the San Miguel Group  |
| “2009 Agreement”                    | the agreement dated 11 May 2009 entered into between the Company and SMC in respect of the sales of packaged beer and non-alcoholic beverage products by the Group to the San Miguel Group   |
| “associate(s)”                      | has the meaning ascribed to it under the Listing Rules   |
| “Board”                             | the board of Directors   |
| “Cap(s)”                            | the maximum annual aggregate value for each of the Continuing Connected Transactions under the New Agreement for the three years ending 31 December 2013   |
| “Company”                           | San Miguel Brewery Hong Kong Limited, a company incorporated in Hong Kong with limited liability, whose shares are listed in the Stock Exchange  |
| “Continuing Connected Transactions” | the following transactions between the Group and the San Miguel Group pursuant to the New Agreement: (i) purchase by the Group from the San Miguel Group of packaging materials and packaged beer; and (ii) sales by the Group to the San Miguel Group of packaged beer and non-alcoholic beverages products (provided that, in respect of the sales of packaged beer by the Group to the San Miguel Group, the sales or distribution of packaged beer shall not be carried out in the Philippines, unless such sales or distribution is carried out through San Miguel Brewery, Inc.) |
| “Directors”                         | the directors of the Company   |
| “EGM”                               | the extraordinary general meeting to be convened by the Company to consider, and if thought fit, approve the New Agreement, the Continuing Connected Transactions and the Caps   |
| “Group”                             | the Company and its subsidiaries   |
| “Hong Kong”                         | the Hong Kong Special Administrative Region of the People’s Republic of China  |

|                               |  |
|-------------------------------|--|
| “Independent Board Committee” | an independent committee of the Board, comprising Dr. The Hon. Sir. David K.P. Li, Mr. Ng Wai Sun and Mr. Carmelo L. Santiago, all of them being independent non-executive Directors, which has been established by the Board to advise the Independent Shareholders in respect of the New Agreement, the Continuing Connected Transactions and the Caps |
| “Independent Shareholder(s)”  | the shareholder(s) of the Company, other than SMC and its associates   |
| “KBC Bank”                    | KBC Bank N.V., acting through its Hong Kong Branch, a licensed bank under the Banking Ordinance and a registered institution registered for Type 6 (advising on corporate finance) regulated activity under the Securities and Futures Ordinance   |
| “Listing Rules”               | the Rules Governing the Listing of Securities on the Stock Exchange  |
| “New Agreement”               | the agreement dated 15 October 2010 entered into between the Company and SMC in respect of the Continuing Connected Transactions   |
| “PRC”                         | the People’s Republic of China which, for the purpose of this announcement, excludes Hong Kong, Macau and Taiwan   |
| “Share(s)”                    | ordinary share(s) of HK\$0.5 each in the share capital of the Company  |
| “Shareholders”                | the shareholders of the Company  |
| “SMC”                         | San Miguel Corporation, the ultimate controlling shareholder of the Company  |
| “San Miguel Group”            | SMC and its associates, excluding the Group, for the purpose of this announcement  |
| “Stock Exchange”              | The Stock Exchange of Hong Kong Limited  |
| “HK\$”                        | Hong Kong dollars, the lawful currency of Hong Kong  |

By Order of the Board  
**John K.L. Cheung**  
*Company Secretary*

Hong Kong, 18 October 2010