



HARMONY ASSET LIMITED

亨亞有限公司*

(Incorporated in the Cayman Islands with limited liability)

(HKEX Stock Code: 428)

MANAGEMENT DISCUSSION AND ANALYSIS PREPARED IN ACCORDANCE WITH CANADIAN SECURITIES LAW

For the Quarter Ended: September 30, 2014

Date of Report: November 14, 2014

Nature of the Business

Harmony Asset Limited (“**Harmony**” or the “**Company**”) was incorporated in the Cayman Islands on September 28, 1993. The Company’s ordinary shares are listed on the Hong Kong Stock Exchange (the “**HKEX**”).

Harmony is an investment company that principally invests in securities listed on the HKEX with an emphasis on companies with undervalued and discounted shares. The Company also invests in private companies which have potential for earnings growth and capital appreciation. The Company takes an active role in building its investee companies and often retains a long-term strategic interest in the companies in which it invests. Harmony also takes on a consulting role and provides specialist advice to debt-stricken companies and medium-sized companies looking for financial and strategic partners for future growth.

This Management’s Discussion and Analysis (“**MD&A**”) includes the Financial Statements of Harmony and its wholly owned subsidiaries (together, the “**Group**”).

Reporting Currency

All monetary amounts contained in this MD&A are reported in Hong Kong dollars unless otherwise indicated.

Caution Regarding Forward-Looking Information

This MD&A contains forward-looking information, including forward-looking information regarding the global economy and financial markets, which reflects the Company’s current beliefs with respect to future events and is based on information currently available to the Company. Forward-looking information involves known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking information. When reviewing the Company’s forward-looking information, investors and others should not place undue reliance on this forward-looking information and should carefully consider uncertainties and potential events. Unless otherwise required by applicable securities laws, the Company disclaims any intention or obligation to

update the forward-looking information. The Company has an ongoing obligation to disclose material information as it becomes available.

OVERALL PERFORMANCE AND SIGNIFICANT EVENTS

Overall Performance

Financial highlights for the period ended September 30, 2014 with comparatives are set out below:

Operating Results (in HK\$)	Three months ended		Nine months ended	
	September 30 (unaudited)		September 30 (unaudited)	
	2014	2013	2014	2013
Turnover, other revenue and other gains and (losses)	(1,600,416)	(2,852,724)	(20,979,365)	(21,167,754)
Net loss before tax	(5,929,562)	(6,821,214)	(32,754,208)	(32,610,296)
Loss attributable to owners	(5,929,562)	(6,821,214)	(32,754,208)	(32,610,296)
Basic loss per ordinary share	(0.15)	(0.17)	(0.84)	(0.83)

- For the nine months ended September 30, 2014, the Group maintained its debt-free status.
- The Group principally invests in securities listed on recognised stock exchanges and unlisted securities, including equity securities and convertible bonds issued by corporate entities.
- For the nine months ended September 30, 2014, the Group recorded a turnover of HK\$3,114,586 as compared to HK\$4,586,731 in the same period last year, representing a decrease of approximately 32%. Such decrease was due to less dividend income received during the period.
- The Group incurred a net loss in turnover, other revenue and other gains and losses of HK\$24,099,194 for the nine months ended September 30, 2014 as compared to HK\$25,757,725 in the same period in the prior year. Such change has been discussed herein under the heading "Results of Operations".
- For the nine months ended September 30, 2014, the loss before income tax was HK\$32,754,208 as compared to HK\$32,610,296 in the same period in the prior year. The loss attributable to owners of the Company was HK\$32,754,208 as compared to HK\$32,610,296 in the same period in the prior year. The loss for the nine months ended September 30, 2014 was mainly due to a continuous decrease in the fair value of the Group's trading securities and derivative financial instruments.
- Looking back over the nine months ended September 30, 2014, the fluctuation in market value of certain publicly traded securities materially influenced the Company's performance. The Group intends to diversify its investment portfolio in order to mitigate the risk of uncertainty regarding price fluctuations of publicly traded securities.
- As at September 30, 2014, the Group had available funds of HK\$34,594,183 which were mainly placed with banks as time deposits. As at September 30, 2014, the Group's net current assets were HK\$109,294,749. The Group had no borrowing and also did not have any capital expenditure commitments. Management believes that the Group's net current assets are sufficient to meet the ongoing needs of its business.

Investments

As at September 30, 2014, the Group's unlisted investments (comprised of available-for-sale financial assets ("AFS") and loans and receivables) were HK\$121,771,268 as compared to HK\$114,229,014 as at December 31, 2013, representing a 6.6% increase. Such increase was mainly due to: (1) increase in fair value of AFS of HK\$4,560,500; (2) increase in value of AFS as a result of a further private equity investment in the amount of HK\$7,772,464; (3) decrease in value of AFS by disposal of a partial interest in a private equity investment in the amount of HK\$4,000,000; (4) increase in loans and receivables as a result of subscriptions for four convertible bonds in an aggregate amount of HK\$22,600,000; (5) redemption of convertible bonds of HK\$15,600,000; (6) accrual of interest of HK\$1,123,488 from convertible bonds held by the Group; (7) repayment of HK\$2,500,000 from an investee; and (8) impairment losses on loans and receivables of HK\$6,414,198.

As at September 30, 2014, accounts receivable and prepayments was HK\$9,689,636 as compared to HK\$30,910,631 as at December 31, 2013, representing a 69% decrease. Such decrease was primarily the result of (1) repayment of an outstanding balance of HK\$19,422,739 which was brought forward from last year, and (2) net decrease of HK\$104,028 from other receivables; (3) net increase of interest receivable of HK\$606,830; and (4) net decrease of deposits and prepayments of HK\$2,301,0589.

As at September 30, 2014, the Group held trading securities and convertible bonds designated as at fair value through profit or loss in an aggregate amount of HK\$37,397,924 as compared to HK\$54,235,622 as at December 31, 2013, representing a 31% decrease. The decrease was primarily due to: (1) purchases of securities during the nine months ended September 30, 2014 for an aggregate amount of HK\$12,112,289; (2) the disposal of certain securities which had an aggregate cost of HK\$13,097,684; and (3) net decrease in market value of the listed securities held by the Group in the aggregate amount of HK\$15,852,303.

Outlook

The second half of September 2014, saw S&P achieving new highs. Investors are concerned as to whether or not markets can continue to sustain such performance. The end of QE suggests some downside risk, but the lack of alternative may continuously to sustain current market trends. However, this liquidity driven market may change in a moments' notice due to global interest rate expectation.

RESULTS OF OPERATIONS

The Group's selected financial highlights for the three months and the nine months ended September 30, 2014 with comparatives are as follows:

Operating Results (all figures in HK\$)	Three months ended September 30 (unaudited)		Nine months ended September 30 (unaudited)	
	2014	2013	2014	2013
Turnover (total investment income)*	986,157	2,033,863	3,114,586	4,586,731
Interest income	794,534	532,403	2,845,649	1,572,843
Dividends received	191,623	1,501,460	268,937	3,013,888
Gain on disposal of listed investments	470,579	6,929,286	2,355,171	9,180,198

The reconciliation is set out in the results announcement and the Q3 report.

Net loss before tax	(5,929,562)	(6,821,214)	(32,754,208)	(32,610,296)
Loss attributable to equity holders	(5,929,562)	(6,821,214)	(32,754,208)	(32,610,296)

* Turnover comprises interest income (bank deposits, loans receivable, convertible notes) and dividends received (public and private companies).

Other income, other gains and (losses) (all figures in HK\$)	Three months ended September 30 (unaudited)		Nine months ended September 30 (unaudited)	
	2014	2013	2014	2013
Other income:				
Sundry Income	1	117	5,243	3,240
Total other income	1	117	5,243	3,240
Other gains and (losses):				
Exchange (loss) gain, net	21,750	76,626	102,218	(190,423)
Fair value changes on financial assets at fair value through profit or loss				
- trading securities	(3,078,903)	(7,715,849)	(15,852,303)	(26,211,625)
- derivative financial instruments			(6,538,155)	(4,528,489)
Net realized gain on disposals of financial assets at fair value through profit or loss				
- trading securities	470,579	6,929,286	2,355,171	9,180,198
- derivative financial instruments				
Recovery of impairment loss on accounts receivable				
Recovery of impairment loss on loans and receivables		760,000		884,381
Net realized gain on disposals of AFS			2,248,073	3,702,105
Impairment loss on loans and receivables		(8,593,872)	(6,414,198)	(8,593,872)
Impairment loss on AFS				
- equity investments				
- deposits on investments written off				
Total other gains and (losses)	(2,586,574)	(4,886,704)	(24,099,194)	(25,757,725)
Total	(2,586,573)	(4,886,587)	(24,093,951)	(25,754,485)

For the three months ended September 30, 2014 versus the three months ended September 30, 2013

For the three months ended September 30, 2014, the Group received interest income in the aggregate amount of HK\$794,534 (2013: HK\$532,403). The interest income comprised HK\$31,645 (2013: HK\$5,611) earned from bank deposits and HK\$762,889 (2013: HK\$526,792) earned from loans receivable and convertible bonds. Dividend income generated from only listed securities was HK\$191,623 (2013: HK\$1,460 from listed securities and HK\$1,500,000 from an unlisted security). Turnover was HK\$986,157 as compared to HK\$2,033,863 in the same period last year, representing a 52% decrease.

In the three months ended September 30, 2014, the Group disposed of certain of its publicly traded securities to record a net realised gain of HK\$470,579 (2013: HK\$6,929,286). Given the impact of the consistently unfavourable performance of certain publicly traded securities during the period, the Group recorded an unrealised loss on trading securities for the third quarter of 2014 of HK\$3,078,903 (2013: unrealised loss of HK\$7,715,849).

For the three months ended September 30, 2014, no recovery of impairment losses on loans and receivables was recognised (2013: HK\$760,000). No provision for impairment loss on loans and receivables were made (2013: HK\$8,593,872). No gain on disposal of unlisted investments was recorded (2013: HK\$3,657,105). Net exchange gain was HK\$21,750 (2013: HK\$76,626).

For the three months ended September 30, 2014, the Group recorded a net loss in turnover, other revenue and other gains and losses of HK\$1,600,416 as compared to a net loss of HK\$2,852,724 in the same period last year. The loss incurred was due to consistently unfavourable performance of certain trading securities in the third quarter of 2014.

For the three months ended September 30, 2014, employee benefits expenses were HK\$911,853 (2013: HK\$851,165). Other operating expenses were HK\$3,305,719 (2013: HK\$2,944,529). The net increase in other operating expenses was mainly due to a provision of impairment loss of HK\$1,100,738 on other receivable.

The loss before income tax for the three months ended September 30, 2014 was HK\$5,929,562 as compared to a loss of HK\$6,821,214 in the same period in the prior year. The loss attributable to equity holders was HK\$5,929,562 as compared to a loss of HK\$6,821,214 in the same period in the prior year. The loss for the three months ended September 30, 2014 was mainly due to a decrease in the fair value of the Group's trading securities and derivative financial instruments.

For the nine months ended September 30, 2014 versus the nine months ended September 30, 2013

For the nine months ended September 30, 2014, the Group received interest income in the aggregate amount of HK\$2,845,649 as compared to HK\$1,572,843 in the same period last year, representing an 81% increase. The interest income comprised HK\$58,471 (2013: HK\$21,365) earned from bank deposits and HK\$2,787,178 (2013: HK\$1,551,478) earned from loans receivable and convertible bonds. Dividend income generated from only listed securities amounted to HK\$268,937 (2013: HK\$13,888 from listed securities and HK\$3,000,000 from an unlisted security). Turnover was HK\$3,114,586 as compared to HK\$4,586,731 in the same period last year, representing a 32% decrease.

For the nine months ended September 30, 2014, the Group disposed of certain of its publicly traded securities to obtain a net realised gain of HK\$2,355,171 (2013: HK\$9,180,198). With the impact of the consistently unfavourable performance of certain trading securities in the third quarter of 2014, the Group recorded a significant unrealised loss of HK\$15,852,303 (2013: loss of HK\$26,211,625).

No recovery of impairment losses on loans and receivables was recognised (2013: HK\$884,381). Provision for impairment loss on certain loans and receivables was HK\$6,414,198 (2013: HK\$8,593,872). Net gain on disposal of unlisted investments was HK\$2,248,073 (2013: HK\$3,702,105). Net exchange gain was HK\$102,218 (2013: loss of HK\$190,423).

The Group recorded a net loss in turnover, other revenue and other gains and losses of HK\$24,099,194 for the nine months ended September 30, 2014 as compared to a net loss of HK\$25,757,725 in the same

period in the prior year. The loss incurred was due to unfavourable performance of certain trading securities continuously in the third quarter of 2014.

For the nine months ended September 30, 2014, employee benefits expenses were HK\$2,514,866 (2013: HK\$2,678,249). Other operating expenses were HK\$8,925,811 (2012: HK\$8,245,118). The net increase in other operating expenses was mainly due to a provision of impairment loss of HK\$1,100,738 on other receivable.

For the nine months ended September 30, 2014, the loss before income tax was HK\$32,754,208 as compared to a loss of HK\$32,610,296 in the same period in the prior year. The loss attributable to owners of the Company was HK\$32,754,208 as compared to a loss of HK\$32,610,296 in the same period in the prior year. The loss for the nine months ended September 30, 2014 was mainly due to a consistent decrease in the fair value of the Group's trading securities and derivative financial instruments.

SUMMARY OF QUARTERLY RESULTS

The following table sets out a summary of the Group's quarterly results for the eight most recently completed quarters. This information has been derived from the financial statements of the Company, which have been prepared in accordance with International Financial Reporting Standards ("IFRS").

	September 30, 2014	June 30, 2014	March 31, 2014	December 31, 2013
Net investment gains (loss)	(5,929,562)	(21,002,759)	(5,821,887)	(6,351,554)
Net income (loss) for the period	(5,929,562)	(21,002,759)	(5,821,887)	(6,351,554)
Earnings (loss) per ordinary share – basic	(0.15)	(0.54)	(0.15)	(0.16)
Earnings (loss) per ordinary share – diluted	(0.15)	(0.54)	(0.15)	(0.16)

	September 30, 2013	June 30, 2013	March 31, 2013	December 31, 2012
Net investment gains (loss)	(6,821,214)	(15,189,948)	(10,599,134)	22,731,039
Net income (loss) for the period	(6,821,214)	(15,189,948)	(10,599,134)	22,731,039
Earnings (loss) per ordinary share – basic	(0.17)	(0.39)	(0.27)	0.58
Earnings (loss) per ordinary share – diluted	(0.17)	(0.39)	(0.27)	0.58

Significant variations arise in the quarterly results due to interest income, dividend income, realized and unrealized gains/losses on investments recognised in the income statement. The values at which publicly traded investments are carried are subject to fluctuations in the public markets from quarter to quarter. The private investments are re-valued when management adjusts its estimates of the fair value of the investments, which is completed on a quarterly or monthly basis. Management is not aware of any significant seasonal and cyclical factors that would contribute to the quarter-to-quarter variations of the Group's performance.

CASH FLOW

The Group's selected cash flow information for the three months and the nine months ended September 30, 2014 and 2013 are as follows:

(Unaudited)	Three months ended		Nine months ended	
	September 30, 2014	September 30, 2013	September 30, 2014	September 30, 2013

Net cash (used in) from operating activities	2,723,615	(9,739,103)	13,516,563	(2,662,763)
Net cash (used in) from investing activities	10,253,102	13,260,056	(9,801,252)	(12,994,842)
Net cash used in financing activities	—	—	—	—
Net (decrease) increase in cash and cash equivalents	12,976,717	3,520,953	3,715,311	(15,657,605)
Cash and cash equivalents at July 1 and January 1	21,617,466	14,917,854	30,878,872	34,096,412
Cash and cash equivalents at September 30	34,594,183	18,438,807	34,594,183	18,438,807
Analysis of the balance of cash and cash equivalents:				
Bank balances and cash	34,594,183	18,438,807	34,594,183	18,438,807

For the three months ended September 30, 2014 versus the three months ended September 30, 2013

In the normal course of business for Harmony, significant fluctuations in cash flows can occur. Generally, this category includes such items as share transactions, accounts receivable, operating loans to investees and listing expenses. For the three months ended September 30, 2014, net cash flow of HK\$2,723,615 from operations included:

- HK\$6.61 million in loss before working capital changes (a non-cash item);
- HK\$8.91 million decrease in financial assets at fair value through profit or loss;
- HK\$0.46 million decrease in accounts receivable and prepayments; and
- HK\$0.04 million decrease in accounts payable and accruals.

In contrast, for the three months ended September 30, 2013, net cash flow of HK\$9,739,103 used in operations included:

- HK\$3.21 million in gain before working capital changes (a non-cash item);
- (HK\$1.31) million increase in financial assets at fair value through profit or loss;
- (HK\$11.26) million increase in accounts receivable and prepayments; and
- (HK\$0.38) million decrease in accounts payable and accruals.

For the three months ended September 30, 2014, net cash from investing activities was HK\$10,253,102 as compared to HK\$13,260,056 in the same period in the prior year. There were no cash dividends received from the Group's private investments (2013: HK\$1,500,000). Interest received from bank deposits, loans and receivables and convertible bonds was HK\$491,852 (2013: HK\$339,666).

During the three months ended September 30, 2014, no investment was made by the Group except payment of a deposit of HK\$1,938,750 for the subscription of a listed security. Redemption of a convertible bond occurred in an aggregate amount of HK\$11,700,000 (2013: HK\$3,000,000).

For the nine months ended September 30, 2014 versus the nine months ended September 30, 2013

For the nine months ended September 30, 2014, net cash flow of HK\$12,722,029 from operations included:

- HK\$11.79 million in loss before working capital changes (a non-cash item);

- HK\$4.07 million decrease in financial assets at fair value through profit or loss;
- HK\$21.72 million decrease in accounts receivable and prepayments;
- HK\$1.28 million decrease in accounts payable and accruals.

In contrast, for the nine months ended September 30, 2013, net cash flow of HK\$5,323,890 used in operations included:

- (HK\$1.92) million in loss before working capital changes (a non-cash item);
- HK\$2.57 million decrease in financial assets at fair value through profit or loss;
- (HK\$3.78) million increase in accounts receivable and prepayments;
- (HK\$1.14) million decrease in accounts payable and accruals.
- HK\$1.06 million decrease in amount due to a related company.

For the nine months ended September 30, 2014, net cash used in investing activities was HK\$9,006,718 as compared to HK\$12,994,842 in the same period in the prior year. There were no cash dividends received from the Group's private investments (2013: HK\$3,000,000). Interest received from bank deposits, loans and receivables and convertible bonds was HK\$1,221,175 (2013: HK\$1,623,668).

During the nine months ended September 30, 2014, the Group increased its equity interest in an unlisted investment in the amount of HK\$7,772,464 (2013: HK\$19,127,965). Subscriptions of convertible bonds were completed for an aggregate amount of HK\$22,600,000 (2013: HK\$13,284,999). Cash of HK\$15,600,000 was received from the redemption of convertible bonds (2013: HK\$5,000,000). No cash was advanced to investee companies (2013: HK\$165,000). Payment of HK\$1,938,750 was made for an investment deposit (2013: HK\$600,000). Repayment of HK\$2,500,000 was received from an investee (2013: HK\$2,345,349). Cash proceeds of HK\$4,000,000 were received from the disposal of a partial interest in an unlisted investment (2013: HK\$7,614,105). Cash of HK\$16,679 was used in the purchase of fixed assets (2013: nil).

LIQUIDITY

Debt, contractual obligations and contingent liabilities

As at the date of this MD&A, the Group had no debt outstanding and no contingent liabilities.

The Group had available funds of HK\$34,594,183, which were mainly placed with banks as time deposits. Cash and bank balances held by the Group are mainly denominated in Hong Kong dollars.

For the nine months ended September 30, 2014, the Group had no borrowing (2013: nil). The gearing ratio for the Group was 0% (2013: 0%). The gearing ratio represents the ratio of the Group's borrowings to the net asset value of the Group.

Management believes that the Group's current cash position is sufficient to meet the ongoing needs of its business. However, the Group may choose to access capital markets and/or bank financing for funding of future expansion and other opportunities.

CAPITAL RESOURCES

As at the date of this MD&A, the Group has unutilized banking facilities of HK\$10,000,000 and requires no significant funding for investment and capital expenditure commitments. The interest rate charged on the banking facilities is 3% per annum over the applicable Hong Kong Interbank Offered Rate.

As of the date of this MD&A, except for the commitment of operating leases, the Group does not have any capital expenditure commitments and management is not aware of any expected fluctuations in the Group's capital resources. As at September 30, 2014, the Group had future contractual obligations including aggregate minimum lease payments under non-cancellable operating leases in respect of land and buildings as follows:

	Group	
	As at September 30, 2014	As at December 31, 2013
	HK\$	HK\$
Within one year	1,954,800	1,954,800
In the second to fifth years inclusive	2,097,338	3,563,438
Total	4,052,138	5,518,238

FINANCIAL INSTRUMENTS

The Group has minor exposure to fluctuations in foreign exchange rates. This exposure is managed by careful attention to trends in money markets rather than relying on any financial instruments to hedge such exposure.

Financial assets and financial liabilities are recognised on the statement of financial position when a Group entity becomes a party to the contractual provisions of the financial instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

The Group's financial assets are classified into one of three categories, comprising financial assets at fair value through profit or loss, loans and receivables, and available-for-sale financial assets. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Financial liabilities and equity instruments issued by a Group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

An equity instrument is any contract that evidences a residual interest in the assets of a Group entity after deducting all of its liabilities.

The Group's financial instruments as at September 30, 2014 and December 31, 2013 are categorised as follows:

	Group	
	September 30 2014 (unaudited)	December 31 2013
	HK\$	HK\$
Available-for-sale financial assets	<u>79,483,267</u>	<u>71,150,303</u>
Loans and receivables		
Loans and receivables	42,288,001	43,078,711
Accounts receivable	9,120,742	28,069,296
Bank balances and cash	34,594,183	30,878,872
	<u>86,002,926</u>	<u>102,026,879</u>
Financial assets at fair value through profit or loss		
Trading securities	37,397,924	54,235,622
Derivative financial instruments	7,845,677	14,383,832
	<u>45,243,601</u>	<u>68,619,454</u>
Total financial assets	<u>210,729,794</u>	<u>241,796,636</u>
Other financial liabilities		
Accounts payable and accruals	6,252,957	7,529,196
Total financial liabilities	<u>6,252,957</u>	<u>7,529,196</u>

As at and for the period ended September 30, 2014, the significant changes in financial assets and liabilities as compared to the statement of financial position as at December 31, 2013 consisted primarily of:

- (1) The change in the Group's AFS and loans and receivables was primarily due to: (1) increase in fair value of AFS of HK\$4,560,500; (2) increase in value of AFS as a result of a further investment in a private equity in the amount of HK\$7,772,464; (3) decrease in value of AFS due to the disposal of a partial interest in a private equity investment in the amount of HK\$4,000,000; (4) increase in loans and receivables as a results of subscriptions for four convertible bonds in an aggregate amount of HK\$22,600,000; (5) redemption of convertible bonds of HK\$15,600,000; (6) accrual of interest of HK\$1,123,488 from convertible bonds held by the Group; (7) repayment of HK\$2,500,000 from an investee; and (8) impairment losses on loans and receivables of HK\$6,414,198.
- (2) The change in the Group's accounts receivable and prepayments was primarily the result of (1) repayment of an outstanding balance of HK\$19,422,739 which was brought forward from last year, and (2) net decrease of HK\$104,028 from other receivables; (3) net increase of interest receivable of HK\$606,830; and (4) net decrease of deposits and prepayments of HK\$2,301,0589.
- (3) During the nine months ended September 30, 2013, the Group had the following major trading transactions: (1) purchases of securities during the nine months ended September 30, 2014 for an aggregate amount of HK\$12,112,289; (2) the disposal of certain securities which had an aggregate cost of HK\$13,097,684; and (3) net decrease in market value of the listed securities held by the Group in the aggregate amount of HK\$15,852,303.

Further detailed information with respect to the financial instruments and significant assumptions made by the Group in estimation of fair value with respect to its financial instruments have been disclosed in notes (4)(d) and 27(b) of the audited financial statements of the Group for the year ended December 31, 2013.

OFF-BALANCE SHEET ARRANGEMENTS

As of the date of this MD&A, there are no off-balance sheet arrangements.

TRANSACTIONS WITH RELATED PARTIES

The Company has entered into an investment management agreement with Harmony Asset Management Limited ("**HAML**"), a company which is wholly-owned by a director of the Company, Dr. Chow Pok Yu Augustine. Under the investment management agreement entered into between the Company and HAML on April 8, 2010 (the "**Original Investment Management Agreement**"). HAML agreed to provide investment management services to the Group for three years until May 31, 2013.

On April 11, 2013, the Company entered into a new investment management agreement with HAML (the "**New Investment Management Agreement**") as detailed in the circular of the Company dated May 10, 2013 whereby HAML agreed to provide investment management services for three additional years until May 31, 2016. In accordance with the Original Investment Management Agreement and the New Investment Management Agreement, HAML is entitled to a monthly management fee calculated at 1.5% per annum on the net asset value of the Group of the preceding month and an incentive fee is calculated at 10% of the audited net profit in a financial year (before accrual of the incentive fee) subject to an annual cap of HK\$5,690,073 and HK\$4,827,726 for management fees and incentive fee respectively for the year ending to December 31, 2014.

On April 24, 2013, the Company and HAML entered into a supplemental agreement (the "**Supplemental Agreement**") to amend the calculation method of the incentive fee under the New Investment Management Agreement. After entering into the Supplemental Agreement, the incentive fee payable by the Company to HAML under the New Investment Management Agreement (as amended by the Supplemental Agreement) in respect of each financial year shall be 10% of the audited net profit of the Group in the financial year and for the purpose of the calculating the audited net profit of the financial year (i) any audited net loss of the Group in any financial year commencing January 1, 2013 shall be carried forward and set off against the audited net profit of the Group in subsequent financial years, and (ii) the audited net profit of the financial year shall be calculated before accrual of any incentive fee that will be payable. The New Investment Management Agreement and the Supplemental Agreement were approved by the independent shareholders of the Company on the extraordinary meeting of the Company which was held on May 31, 2013.

For the nine months ended September 30, 2014, the management fees paid to HAML are as follows:

	2014 HK\$	2013 HK\$
Management fees	<u>2,564,488</u>	<u>2,984,868</u>

PROPOSED TRANSACTIONS

The Company is not a party to any proposed asset or business acquisition or disposition or any proposed transaction that may have an effect on the financial condition, results of operations, or cash flows of the Company.

OUTSTANDING SHARE DATA

The authorized share capital of the Company is HK\$100,000,000 divided into 100,000,000 Ordinary Shares with a nominal value of HK\$1.00 per Ordinary Share.

As at November 14, 2014, the number of ordinary shares of the Company outstanding is as follows:

<u>Ordinary Shares</u>	<u>Number</u>
Outstanding	39,058,614
Total diluted ordinary shares.....	39,058,614

PRINCIPAL ACCOUNTING POLICIES AND CRITICAL ACCOUNTING ESTIMATES:

1. Basis of preparation

This MD&A should be read in conjunction with the unaudited financial statements for the interim period ended September 30, 2014 and the audited financial statements of the Company for the financial year ended December 31, 2013 and December 31, 2012 (collectively, the "**Financial**

Statements”), which were prepared in accordance with IFRS issued by the International Accounting Standards Board, the disclosure requirements of the Hong Kong Companies Ordinance and the Rules Governing the Listing of Securities on the HKEX. The Financial Statements are available under the Company's profile on the System for Electronic Document Analysis and Retrieval (SEDAR) at www.sedar.com.

The Financial Statements have been prepared under the historical cost basis, except that, as disclosed in the accounting policies shown in the Financial Statements, available-for-sale financial assets and financial assets at fair value through profit or loss are stated at fair value.

This MD&A includes the Financial Statements of Harmony and its wholly owned subsidiaries. All significant inter-company balances and transactions have been eliminated on consolidation.

2. Significant accounting polices

A summary of significant accounting policies are set out in the note 4 to the audited financial statements of the Company for the year ended December 31, 2013.

3. Use of estimates

The preparation of the consolidated financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results may differ from those estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revision to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The Group adopts two principal methodologies to determine the fair value of its financial assets carried at fair value:

(a) *Market price:*

The Group adopts the market price of financial assets through profit and loss for the calculation of their fair value. The surplus or deficit of the fair value will be recognized as unrealized gain or loss respectively through profit and loss.

(b) *Net asset value or discounted cash flows:*

The calculation of fair value of unlisted available-for-sale financial assets is principally based on the net asset value or discounted cash flows of those assets. The net change in fair value of available-for-sale financial assets is recognized in the fair value reserve account.

CHANGES IN ACCOUNTING POLICY

Adoption of new or revised IFRSs during the year ended December 31, 2013 is detailed in note 2 to the audited Financial Statements for such period. The adoption of new or revised IFRSs has no significant

impact on the Group's financial statements. The Group is in the process of making an assessment of the potential impact of new or revised IFRSs that have been issued but are not yet effective for the year ended December 31, 2013 and the directors of the Company have to date concluded that the application of these new or revised IFRSs will have no material impact on the Group's financial statements except for IFRS9, which is explained in note 2 to the audited Financial Statements.

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

The Canadian Securities Administrators have published National Instrument 52-109 - *Certification of Disclosure in Issuers' Annual and Interim Filings* ("**National Instrument 52-109**") which requires public companies in Canada to submit annual and interim certificates relating to the design and effectiveness of the disclosure controls and procedures that are in use at the company. Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported on a timely basis to senior management, including the Company's Chairman and Chief Executive Officer and Chief Financial Officer, to enable this information to be reviewed and discussed so that appropriate decisions can be made regarding the timely public disclosure of the information.

As of September 30, 2014, management has evaluated the effectiveness of the design and the operating effectiveness of the disclosure controls and procedures as defined by National Instrument 52-109. This evaluation was performed under the supervision of and with the participation of the Company's Chairman and Chief Executive Officer and Chief Financial Officer. Based on this evaluation, the Company's Chairman and Chief Executive Officer and Chief Financial Officer concluded that the design and operation of the disclosure controls and procedures in use at the Company were effective as of September 30, 2014.

INTERNAL CONTROL OVER FINANCIAL REPORTING

National Instrument 52-109 also requires public companies in Canada to submit an interim certificate relating to the design and operating effectiveness of internal control over financial reporting ("**ICFR**"). ICFR is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian generally accepted accounting principles. Management is responsible for establishing and maintaining ICFR and management, including the Company's Chairman and Chief Executive Officer and Chief Financial Officer, has evaluated the design and tested the effectiveness of the ICFR at September 30, 2014. Based on this evaluation, management, with the participation of the Company's Chairman and Chief Executive Officer and Chief Financial Officer, has concluded that the design and operating effectiveness of ICFR was effective as of September 30, 2014. The Company has continued to use the basic framework for international control and risk management internal control framework issued by the Hong Kong Institute of Certified Public Accountants to design its ICFR. Due to its inherent limitations, internal control over financial reporting may not prevent or detect misstatements on a timely basis as such systems can only be designed to provide reasonable as opposed to absolute assurance. Also, projections of any evaluation of the effectiveness of ICFR to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

National Instrument 52-109 also requires public companies in Canada to disclose in their MD&A any change in ICFR during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, internal control over financial reporting. There were no changes in ICFR during the

quarter ended September 30, 2014 that materially affected or are reasonably likely to materially affect the Company's ICFR.

Risk Factors

The following are certain risk factors inherent in the Company's businesses and an investment in the ordinary shares of the Company. The following information is a summary only of certain risk factors and is qualified in its entirety by reference to, and must be read in conjunction with, the detailed information appearing in the Company's Annual Information Form for the financial year ended December 31, 2013 (the "AIF"). These risks and uncertainties are not the only ones facing the Company. Additional risks and uncertainties not currently known to the Company, or that the Company currently considers immaterial, may also impair the business of the Company. If any such risks actually occur, the business, financial condition, liquidity and results of operations of the Company could be materially adversely affected.

1. Risks of doing business in the People's Republic of China

Some of the Group's investments have operations located in the People's Republic of China ("PRC"). The PRC's economy and legal system differ from those of most developed countries in many respects, including the level of development and transparency. The Group will be affected by any political or economic instability in the PRC. Changes in investment policies or shifts in political attitude in the PRC may adversely affect the Group's businesses. Operations will also be adversely affected in varying degrees by government regulations including but not limited to restrictions on production, price controls, income taxes, and expropriation of property. The introduction of new policies, legislation or amendments to existing policies or legislation by various levels of government in the PRC or the interpretation of those laws in the PRC or elsewhere could impact adversely on the assets, operations and financial performance of the Group.

2. Risk of Limited Number of Investments

The Company intends to participate in a limited number of investments and, as a consequence, the aggregate return of the Company may be substantially adversely affected by the unfavourable performance of even a single investment. In addition, as the Company's investments are concentrated in certain sectors, the Company's performance will be disproportionately subject to adverse developments in those sectors.

3. Marketability of the Company's Investments

The Company often makes direct investments in publicly-traded securities. The value of these investments may be affected by factors such as investor demand, resale restrictions, general market trends and regulatory restrictions. Fluctuation in the market value of such investments may occur for a number of reasons beyond the control of the board of directors of the Company, and there is no assurance that an adequate market will exist for investments made by the Company. Many of the investments made by the Company may be relatively illiquid and may decline in price if a significant number of such investments are offered for sale by the Company or other investors.

The Company also invests in securities of privately held companies. Investments in privately held companies cannot be resold without a prospectus, an available exemption or an appropriate ruling under relevant securities legislation and there may not be any market for such securities. These limitations may impair the Company's ability to react quickly to market conditions or negotiate

the most favourable terms for exiting such investments. Investments in privately held companies may offer relatively high potential returns, but will also be subject to a relatively high degree of risk. There can be no assurance that a public market will develop for any of the Company's private company investments or that the Company will otherwise be able to realize a return on such investments.

The value attributed to securities of privately held companies will be the cost or net asset value thereof, subject to adjustment in limited circumstances, and therefore may not reflect the amount for which they can actually be sold. Because valuations, and in particular valuations of investments for which market quotations are not readily available, are inherently uncertain, may fluctuate within short periods of time and may be based on estimates, determinations of fair value may differ materially from the values that would have resulted if a ready market had existed for the investments.

4. *(a) Due Diligence*

The due diligence process that the Company undertakes in connection with investments may not reveal all facts that may be relevant in connection with an investment. Before making investments, the Company conducts due diligence that it deems reasonable and appropriate based on the facts and circumstances applicable to each investment. When conducting due diligence, the Company may be required to evaluate important and complex business, financial, tax, accounting, environmental and legal issues. Outside consultants, legal advisors, accountants and investment banks may be involved in the due diligence process in varying degrees depending on the type of investment. Nevertheless, when conducting due diligence and making an assessment regarding an investment, the Company relies on the resources available to us, including information provided by the target of the investment and, in some circumstances, third-party investigations. The due diligence investigation that is carried out with respect to any investment opportunity may not reveal or highlight all relevant facts that may be necessary or helpful in evaluating such investment opportunity. Moreover, such an investigation will not necessarily result in the investment being successful.

(b) Lack of formal purchase agreements and/or shareholder/subscription agreements

The Company does not have formal purchase agreements and/or shareholder/subscription agreements in place for some of its investments in privately held companies. As at September 30, 2014, the total carrying value of all the Group's investments was approximately HK\$11.5 million, which is approximately 5.4% of the net asset value of the Group. It is not entirely abnormal for the Company to make investments in privately held companies in the absence of formal purchase agreements and/or shareholder/subscription agreements. As mentioned in the preceding paragraph, due diligence process was undertaken by the Company in connection with its investments through internal resources or by hiring external consultancy and/or professional advisors and most of the investments in privately held companies made by the Company took the form of share equities. Under the laws of the jurisdictions of these privately held companies, the certificates specifying the shares held by the Company are prima facie evidence of the title of the Company to those share equities and the Board considers the risk of the Company having title to its investments challenged due to lack of formal purchase agreements and/or shareholder/subscription agreements is low.

5. *Reliance upon the Directors and Management*

Shareholders must rely upon the expertise and discretion of the board of directors and management of the Company in selecting and investing in securities, the composition of the portfolio of such securities owned or acquired by the Company and in determining whether to dispose of any securities held by the Company. The success of the Company will be dependent upon the board of directors and management of the Company successfully identifying and managing the Company's investments. Accordingly, the Company's continued success will depend upon the continued services of these individuals who are not obligated to remain employed with the Company. The loss of the services of any of these individuals could have a material adverse effect on the Company's revenues, net income and cash flows and could harm the Company's ability to maintain or grow its existing assets and raise additional funds in the future.

6. *Currency and Foreign Exchange Rate Risks*

A substantial proportion of the Company's investments are made in Hong Kong dollars and the Company may also invest in securities denominated or quoted in other foreign currencies. Therefore, changes in currency exchange rates as well as associated transaction costs could adversely affect the value of the ordinary shares during any period. In addition, the Company could also make investments in jurisdictions which may place restrictions on the repatriation of funds. The Company does not enter into hedging or derivative arrangements to manage its foreign exchange risk.

7. *Liquidity Risk*

Should the Company be unable to dispose of any portion of the Company's portfolio, the Company may experience delays in receiving the proceeds of disposition of any security within the portfolio until such time as the Company is able to dispose of such securities. Further, should the Company wish to acquire particular securities for the Company's portfolio, the Company may be unable to acquire the desired quantity of such securities at a price acceptable to the Company should the market for such security prove illiquid.

Further, investments in small capitalization companies or privately held companies tend to be less liquid than other types of investments. Due to the Company's investment in particular small or unlisted companies that can be affected by political and economic events, the securities within the Company's portfolio may be difficult to value or sell. As a result, these securities may trade at values significantly lower than their true value. This may result in the Company's difficulty in converting these securities into cash in a timely and cost effective manner.

8. *Interest Rate Risk*

Due to the Company's investment strategy and portfolio composition, the value of the securities within the Company's portfolio may fluctuate with changes in interest rates. These changes mean that the market price for the securities held in the Company's portfolio will be affected by prevailing interest rates.

9. *Speculative Nature of Ordinary Shares*

The investment in the ordinary shares of the Company is speculative in nature and suitable only for investors able to sustain a total loss of their investment. Shareholders should not rely upon

realizing any significant returns from the ordinary shares of the Company and should be aware that the value of the ordinary shares and the income from them could, in common with other shares and bonds, fluctuate. There is no assurance that the investment objectives of the Company will actually be achieved.

10. Trading Price of Shares relative to Net Asset Value

The Company is neither a mutual fund nor an investment fund and due to the nature of the Company's business and investment strategy and the composition of its investment portfolio, the market price of the ordinary shares, at any time, may vary significantly from its net asset value per share. This risk is separate and distinct from the risk that the market price of the ordinary shares of the Company may decrease.

FINANCIAL RISK MANAGEMENT

The Company has implemented policies to manage its exposure to certain financial risks. Refer to Note 27 of the notes to the audited financial statements of the Company for the year ended December 31, 2013 for a discussion regarding the Company's financial risk management.

ADDITIONAL INFORMATION

Additional information relating to Harmony may be found on SEDAR at www.sedar.com, the HKEX website at www.hkex.com.hk or the Company's website at www.harmonyasset.com.hk. Additional financial information is provided in the Company's AIF and Annual Report for the financial year ended December 31, 2013. The Annual Report includes the audited consolidated financial statements as at December 31, 2013, the notes thereto and the report of the Company's auditors thereon. Copies of these documents, together with copies of this MD&A and copies of any documents or the pertinent pages of any documents incorporated by reference in this MD&A, are available upon request to the Company, provided that the Company may require payment of a reasonable charge if the request is made by a person who is not a security holder of the Company.