
THIS CIRCULAR IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION

If you are in any doubt as to any aspect of this circular or as to the action to be taken, you should consult a licensed securities dealer, bank manager, solicitor, professional accountant or other professional adviser.

If you have sold or transferred all your shares in Harbin Power Equipment Company Limited (the "Company"), you should at once hand this circular to the purchaser or transferee or to the bank, stockbroker or other agent through whom the sale or transfer was effected for transmission to the purchaser or transferee.

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哈尔滨动力设备股份有限公司

HARBIN POWER EQUIPMENT COMPANY LIMITED

(A joint stock limited company incorporated in the People's Republic of China with limited liability)

(Stock Code: 1133)

CONTINUING CONNECTED TRANSACTIONS IN RESPECT OF THE DEPOSITORY SERVICES UNDER THE FINANCIAL SERVICES FRAMEWORK AGREEMENT

**Independent financial adviser to the Independent Board Committee
and the Independent Shareholders**



招商證券(香港)有限公司

CHINA MERCHANTS SECURITIES (HK) CO., LTD.

A letter of recommendation from the Independent Board Committee is set out on page 17 of this circular and a letter of recommendation from China Merchants Securities (HK) Co., Limited, the independent financial adviser to the Independent Board Committee and the Independent Shareholders is set out on pages 18 to 32 of this circular.

A notice convening the extraordinary general meeting (the "EGM") of Harbin Power Equipment Company Limited to be held at 17th Floor Meeting Room, Block B, 39 Sandadongli Road, Xiangfang District, Harbin, Heilongjiang Province, the People's Republic of China on Wednesday, 6 July 2011 at 9:00 a.m. is set out on pages 38 to 39 of this circular.

A form of proxy for use at the EGM is enclosed with this circular. If you do not intend to attend the EGM, you are requested to complete the form of proxy in accordance with the instructions printed thereon and return it to registered office of the Company at Block B, 39 Sandadongli Road, Xiangfang District, Harbin, Heilongjiang Province, the People's Republic of China as soon as possible and in any event not less than twenty-four (24) hours before the time appointed for holding the EGM. Completion and return of the form of proxy will not preclude you from attending and voting in person at the EGM or any adjournment of it, if you so wish.

18 May 2011

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DEFINITIONS

In this circular, unless the context otherwise requires, the following expressions have the following meanings:

“associate(s)”	has the meaning ascribed to it under the Listing Rules;
“Board”	the board of Directors;
“CBRC”	中國銀行業監督管理委員會 (China Banking Regulatory Commission);
“Company”	Harbin Power Equipment Company Limited, a company incorporated in the PRC with limited liability, the H Shares of which are listed on the Stock Exchange;
“connected person(s)”	has the meaning ascribed to it under the Listing Rules;
“controlling shareholder”	has the meaning ascribed to it under the Listing Rules;
“Depository Services”	the provision of the depository services to be provide by the Finance Company in accepting deposits placed by the Group pursuant to the Financial Services Framework Agreement;
“Directors”	the directors of the Company;
“Domestic Share(s)”	domestic invested share(s) of RMB1.00 each in the share capital of the Company;
“EGM”	the extraordinary general meeting of the Company to be convened to consider, and if thought fit, approve the Depository Services to be provided by the Finance Company pursuant to the Financial Services Framework Agreement;
“Existing Financial Service Framework Agreement”	the financial service framework agreement dated 14 December 2010 entered into between the Company and the Finance Company which is the subject of the Company’s announcement dated 14 December 2010;
“Finance Company”	哈爾濱電氣集團財務有限責任公司 (HE Finance Company Limited*) a limited company incorporated in the PRC;

DEFINITIONS

“Finance Service Framework Agreement”	the finance service framework agreement dated 13 April 2011 entered into between the Company and the Finance Company in respect of the Financial Services;
“Financial Services”	the Depository Service, the Loan Services, the Settlement Services and Other Financial Services;
“Group”	the Company and its subsidiaries;
“H Share(s)”	overseas listed foreign invested shares of RMB1.00 each in the capital of the Company which are listed on the Stock Exchange;
“Harbin Electric”	哈爾濱電氣集團公司 (Harbin Electric Corporation*), a state-owned enterprise and the controlling shareholder of the Company;
“Harbin Electric Group”	Harbin Electric and its subsidiaries, including the Group;
“Hong Kong”	the Hong Kong Special Administrative Region of the PRC;
“IFA”	China Merchants Securities (HK) Co., Limited, a corporation licensed under the SFO to conduct Type 1 (dealing in securities), Type 2 (dealing in futures contracts), Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities under the SFO, being the independent financial adviser appointed by the Company to advise the Independent Board Committee and the Independent Shareholders in respect of the terms of the Depository Services under the Financial Services Framework Agreement and the annual caps in respect thereof;
“Independent Board Committee”	a board committee comprising of the independent non-executive Directors of the Company constituted to make recommendations to the Independent Shareholders in respect of the Depository Services and the annual caps in respect thereof;
“Independent Shareholders”	the Shareholders other than Harbin Electric and its associates;

DEFINITIONS

“Independent Third Party”	a person who, to the best of the Directors’ knowledge, information and belief having made all reasonable enquiries, is a third party independent of the Company and its connected persons (as defined under the Listing Rules);
“Latest Practicable Date”	16 May 2011, being the latest practicable date prior to the printing of this circular for the purpose of ascertaining certain information contained herein;
“Listing Rules”	the Rules Governing the Listing of Securities on the Main Board of the Stock Exchange;
“Loan Services”	the loan services to be provided by the Finance Company to the Group pursuant to the Financial Services Framework Agreement, including provision of guarantees; provision of bill acceptance and bill discount services; and other loan services as may be approved by the CBRC (including but not limited to provision of loans and finance leasing services);
“Other Financial Services”	other financial services to be provide by the Finance Company to the Group pursuant to the Financial Services Framework Agreement, including provision of finance services and financing consultancy services, credit verification and related consultancy and agency services; payment and receipt of transaction proceeds; provision of approved insurance agency services; inter-bank borrowing and lending services; and other business as may be approved by the CBRC;
“PBOC”	People’s Bank of China (中國人民銀行);
“PRC”	the People’s Republic of China, and for the purpose of this circular, excluding Hong Kong, Macau and Taiwan;
“SAIC”	the State Administration for Industry and Commerce;
“Settlement Services”	the provision of intra-group transfer and settlement services and liquidation planning services to be provide by the Finance Company to the Group pursuant to the Financial Services Framework Agreement;

DEFINITIONS

“SFO”	the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong);
“Shares”	H Share(s) and Domestic Share(s);
“Shareholder(s)”	holder(s) of Share(s);
“Stock Exchange”	The Stock Exchange of Hong Kong Limited;
“subsidiary”	has the meaning ascribed to it under the Listing Rules;
“HK\$”	Hong Kong Dollars, the lawful currency of Hong Kong;
“RMB”	Renminbi, the lawful currency of the PRC; and
“%”	per cent.

* For identification purposes only

LETTER FROM THE BOARD



哈尔滨动力设备股份有限公司

HARBIN POWER EQUIPMENT COMPANY LIMITED

(A joint stock limited company incorporated in the People's Republic of China with limited liability)

(Stock Code: 1133)

Executive Directors:

Mr. Gong Jing-kun
Mr. Zou Lei
Mr. Duan Hong-yi
Mr. Wu Wei-zhang
Mr. Shang Zhong-fu

Registered Office and headquarters:

Block 3 Nangang District
High-Technology Production Base
Harbin, Heilongjiang
PRC

Independent Non-Executive Directors:

Mr. Sun Chang-ji
Mr. Jia Cheng-bing
Ms. Li He-jun
Mr. Yu Bo
Mr. Liu Deng-qing

Principal Place of Business in Hong Kong:

20th Floor
Alexandra House
18 Chater Road
Central
Hong Kong

18 May 2011

To the Shareholders

Dear Sir or Madam,

CONTINUING CONNECTED TRANSACTIONS IN RESPECT OF THE DEPOSITORY SERVICES UNDER THE FINANCIAL SERVICES FRAMEWORK AGREEMENT

INTRODUCTION

On 13 April 2011, the Company entered into the Financial Services Framework Agreement with the Finance Company, pursuant to which the Finance Company will provide the Financial Services (including the Depository Services, Loan Services, Settlement Services and Other Finance Services) to the Group. Pursuant to the Financial Services Framework Agreement, of the Finance Company will provide the Financial Services to the Group. The Group is not under any obligation to obtain any or all of the Financial Services from the Finance Company and may obtain such Financial Services based on its business needs.

LETTER FROM THE BOARD

The purpose of this circular is (i) to provide you with further information in relation to the transactions contemplated under the Financial Services Framework Agreement; (ii) to set out the opinions and recommendations of the Independent Board Committee and the IFA; and (iii) to give you notice of the EGM at which the resolutions set out therein will be proposed. The EGM will be held on Wednesday, 6 July 2011 for the purposes of, among others, obtaining the approval from the Independent Shareholders for the Depository Services and the annual caps in respect thereof by way of poll. Each of Harbin Electric and its associates, which holds an aggregate of 701,235,000 Shares as at the Latest Practicable Date, will abstain from voting on the relevant resolutions to be proposed at the EGM.

FINANCIAL SERVICES FRAMEWORK AGREEMENT

On 13 April 2011, the Company and the Finance Company entered into the Financial Services Framework Agreement, the principal terms of which are set out below:

- Date: 13 April 2011
- Parties: (i) the Company; and
(ii) the Finance Company
- Term: The Financial Services Framework Agreement shall be for a term of 3 years from the Independent Shareholders having approved the Financial Services Framework Agreement and the financial services provided pursuant to the Financial Services Framework Agreement.
- Subject to the compliance with applicable laws and regulations (including the Listing Rules), the term of the agreement will upon expiry automatically be renewed for a further term of 3 years unless terminated by either party before the expiry of each term.
- Services: Pursuant to the Financial Services Framework Agreement, the Finance Company agreed to provide the Financial Services to the Group. The Finance Company undertakes under the Financial Services Framework Agreement that the terms of any Financial Services to be provided by the Finance Company to the Group will be no less favourable than those offered by independent third parties to the Group and the benchmark rates determined by PBOC (if applicable). The Group is not under any obligation to obtain any of the Financial Services from the Finance Company and may obtain such Financial Services based on its business needs.

LETTER FROM THE BOARD

Depository Services

The Group may from time to time deposit money with the Finance Company pursuant to the Financial Services Framework Agreement. The Finance Company shall accept deposit from the Group at an interest rate not less than the interest rate as may be offered by any independent third party to the Group for the same type of deposits. The Finance Company has further provided an irrevocable undertaking to the Company that the interest rate for the deposits placed by the Group under the Financial Services Framework Agreement will be equal to the benchmark rates determined by the PBOC from time to time and will not be downward adjusted.

Moneys deposited by the Company and its subsidiaries with the Finance Company may only be deployed for services or products provided by PBOC or one or more other commercial banks in the ordinary course of their business.

Loan Services

The Group may from time to time request the Finance Company to provide Loan Services to them pursuant to the Financial Services Framework Agreement. The Finance Company shall provide such loan services to the Group at a fee or an interest rate not higher than the fee or the interest rate as may be offered by any third party to the Group for the same type of services. The annual credit that may be extended by the Finance Company to the Company and its subsidiaries should in principal not be less than the maximum amount of deposits made by them for each of the three years ending 31 December 2013.

The Group will not be required to provide any security for the loans provided by the Finance Company provided that the amount of the loans does not exceed the annual credit.

LETTER FROM THE BOARD

In the event that any member of the Group is required to provide any security for the Loan Services, the Company would propose to seek Independent Shareholders' approval on the cap for the Loan Services and comply with the requirements under Chapter 14A of the Listing Rules.

Settlement Services

The Group may from time to time request the Finance Company to provide Settlement Services to them pursuant to the Financial Framework Agreement free of charge.

Other Financial Services

The Group may from time to time request the Finance Company to provide Other Financial Services to them pursuant to the Financial Framework Agreement. The fees charged by the Finance Company for the provision of such Other Financial Services will not be more than rate charged any third party on any member of the Group for the same type of services.

The Group is entitled, to the extent permitted under the laws, to set-off any amount owing by the Group to the Finance Company and/or Harbin Electric and its subsidiaries (other than the Group) against the deposit (including the accrued interest) placed by the Group with the Finance Company. On the other hand, the Finance Company does not have the right to set-off any amount owing by the Group to it against any deposit (including the accrued interest) placed by the Group with the Finance Company. The Company has been advised by its PRC legal advisers that there is no existing legal restrictions to the set-off arrangement under PRC laws.

Proposed annual caps for the Depository Services

The table below sets out the maximum cap for the value of Depository Services to be received by the Group (in respect of which Independent Shareholders' approval is proposed to be sought at the EGM) from the Finance Company for the years 2011, 2012 and 2013:

	year ending 31 December		
	2011	2012	2013
	RMB'000	RMB'000	RMB'000
Receipt of Depository Services			
– Daily maximum outstanding balance of deposit (including accrued interest and handling fees)	7,000,000	7,000,000	7,000,000

LETTER FROM THE BOARD

As disclosed in the Company's announcement dated 14 December 2010, the Company entered into the Existing Financial Services Framework Agreement with the Finance Company, pursuant to which the annual caps for the daily maximum outstanding balance of deposit (including accrued interest and handling fees) for each of the years ending 31 December 2012 is RMB760 million. The Financial Services Framework Agreement provides that Existing Financial Services Framework Agreement will be terminated upon the Financial Services Framework Agreement becoming effective. As at 31 December 2010, the Group has cash deposits in the Finance Company in the amount of RMB759.1 million.

As at 31 December 2008, 31 December 2009 and 31 December 2010, the Group had cash deposits in commercial banks (excluding the Finance Company) in the amount of approximately RMB10.8 billion, RMB14.7 billion and RMB12 billion, including unpledged cash deposits of approximately RMB10.3 billion, RMB14.2 billion and RMB11.7 billion. The annual caps for 2011, 2012 and 2013 have been set by reference to approximately 58% of the average unpledged cash of the Group over the last three years ending 31 December 2010. Given that the Group may not be able to enjoy the benefits of utilizing the Financial Services provided by the Finance Company if the annual caps are set too low and that it may not be in the interests of the Company and its Shareholders as a whole if the annual caps are set too high, the executive Directors are of the view that determining the annual caps in between the range of 50% to 100% of the Groups' average unpledged cash deposits over the last three years ended 31 December 2010 is fair and reasonable and is in the interests of the Company and its Shareholders as a whole. Shareholders should note that (i) if the full extent of the annual caps are utilized then deposits of a majority of the unpledged cash of the Group may be concentrated in the Finance Company instead of one or more commercial banks in the PRC; and (ii) if there occurs any circumstance that may affect the deposits placed by the Group with the Finance Company or any breach by the Finance Company or Harbin Electric, the Company may incur substantive costs and time in protecting its interests or enforcing its rights under the Financial Services Framework Agreement or the undertakings given by Harbin Electric, each of which may materially and adversely affect the Company's financial position. However, in view of the Depository Services being subject to annual review by the independent non-executive Directors and auditors of the Company as required under the Listing Rules and the regulatory requirements to be which the Finance Company is subject and the risk management measures provided under the Financial Services Framework Agreement as detailed below, the Directors are of the view that appropriate measures are in place to govern the conduct of the Depository Services and safeguard the interests of the Independent Shareholders.

LETTER FROM THE BOARD

Set out below is a summary of the Group's consolidated unpledged bank deposits, cash and cash equivalents, interest-bearing bank borrowings as extracted from the relevant annual reports and interim reports of the Company:

	As at 31 December		As at 30 June	
	2010	2009	2010	2009
	RMB'000	RMB'000	RMB'000	RMB'000
	(Audited)	(Audited)	(Unaudited)	(Unaudited)
Unpledged bank deposits	1,090,000	3,553,595	2,620,000	4,470,428
Cash and cash equivalents	11,425,774	10,612,136	9,785,289	7,292,224
Interest-bearing bank borrowings	2,056,914	3,995,678	3,747,230	4,380,026

In arriving at the above proposed annual caps set out in the above table, in addition to the above reasons, the following factors have also been considered:

- (i) the amount of unpledged deposit the Group has placed with independent commercial banks as at 31 December 2008, 31 December 2009 and 31 December 2010;
- (ii) the utilization of the Depository Services when considered in the context of the Loan Services and the Settlement Services that are available to the Group can greatly facilitate deployment of surplus funds within the Group which can have a material impact as the business of the Group grows and its cash resources increase; and
- (iii) the possible favourable interest rate to be obtained by the Group from the Finance Company compared with interest rate that could otherwise be obtained by placing deposits with independent commercial banks.

As the Group is not under any obligations to place deposits in the Finance Company, the Directors are of the view that, through the Financial Services Framework Agreement, the Group can benefit from the flexibility in the allocation of its unrestricted cash should the terms be attractive to the Company, and the annual caps are fair and reasonable.

In order to safeguard the interests of the Shareholders, the Financial Services Framework Agreement provides for the following risk management measures:

- (i) to ensure security of the deposits made by the Group in the Finance Company, the Finance Company is required to make sure the safe operation of the deposit management information systems which have passed all safety tests in relation to online bank interfaces of commercial banks, used direct dedicated line when connecting to commercial banks and reached safety standards of the PRC commercial banks and complied with the specifications under the CA safety certification;

LETTER FROM THE BOARD

- (ii) the Finance Company shall be operated in strict compliance with the risk monitoring indicators required by the CBRC and the major risk monitoring indicators such as the gearing ratio and liquidity ratio of the Finance Company shall adhere to the requirements of the CBRC and other applicable laws and regulations;
- (iii) a copy of each internal control report to be submitted by the Finance Company to the CBRC shall also be provided to the Company;
- (iv) if there occurs any circumstance that may affect the deposits placed by the Group with the Finance Company or any significant hidden danger which may undermine the safety of such deposits, the Finance Company shall inform the Group of the same within 2 working days from the date of such occurrence and adopt measures to prevent any loss or to minimize loss. On receipt of such notice, the Group is entitled to forthwith withdraw the deposit (together with interests accrued thereon). If the deposit (together with interests accrued thereon) could not be withdrawn, the deposit may be set-off against loans from the Finance Company;
- (v) the Finance Company will by 10 a.m. on each working day provide the Company with a daily report on the status of the Group's deposits with the Finance Company to allow the Company to monitor and ensure that the average daily deposit balance with the Finance Company would not exceed the upper limit;
- (vi) the Finance Company will on the fifth working day of each month provide a monthly financial report of the previous month to the Company for review and the Finance Company will provide to the Company a copy of each regulatory report submitted to the CBRC within three working days after submission;
- (vii) Harbin Electric has given a guarantee to the CBRC that it will make further capital contributions in the event that the Finance Company has difficulty in fulfilling its payment obligations to ensure normal operation of the Finance Company;
- (viii) the Company may unilaterally terminate the Finance Service Framework Agreement if the Company and/or its subsidiaries may face material risk or loss as a result of the Finance Company's breach or possible breach of PRC laws and regulations, or the Finance Company's non-performance or breach of any provision of the Finance Service Framework Agreement, or the occurrence or possible occurrence of material operation problem or payment difficulty on the part of the Finance Company;

LETTER FROM THE BOARD

- (ix) Harbin Electric has irrevocably and unconditionally provided a separate letter of undertaking to the Company that, where the Finance Company fails to pay any amounts when due or perform any of its obligations under the Financial Services Framework Agreement:
- (a) Harbin Electric will immediately pay such amounts and perform such obligations on demand of the Company as if Harbin Electric is the primary obligor;
 - (b) to the extent permitted under the laws, in the event that the amount owing by the Group to Harbin Electric and any of its members (other than the Group) does not exceed the capital and accrued interest of the deposits placed by the Group with the Finance Company in accordance with the Financial Services Framework Agreement, the Company is entitled to set off such amount owing by the Group to Harbin Electric and any of its members (other than the Group) against the deposits placed by the Group. Harbin Electric shall sign and procure any of its member (other than the Group) to execute any document to effect such agreement in relation to such set-off; and
 - (c) Harbin Electric will, on demand of the Group, promptly indemnify the Group for any losses suffered as a result of the non-performance of the Finance Company of its obligations under the Financial Services Framework Agreement, or invalidity or illegality of such obligations (which have caused any expenses, loss or liability incurred by the Group).

For the avoidance of doubt, the guarantee given by Harbin Electric is a joint liability guarantee. The guarantee period shall be two years from the due date of the performance period of each principal indebtedness. Harbin Electric also agrees that if the Company and the Finance Company changes the performance period of any principal indebtedness, the guarantee period will commenced from the amended performance period. The Company has been advised by its PRC legal advisors that the guarantee is enforceable against Harbin Electric under PRC laws. In assessing Harbin Electric's capacity as guarantor, the Board has considered that Harbin Electric is a state-owned enterprise established in the PRC directly supervised by the State Council of the PRC (中國國務院國有資產監管理委員會) and that Harbin Electric Group is one of the largest power plant equipment manufacturers in the PRC.

LETTER FROM THE BOARD

Reasons for, and benefits of, the Financial Services Framework Agreement

The Group is principally engaged in the business of manufacturing power plant equipment, its principal activities include manufacturing of (i) thermal power equipment; (ii) hydro power equipment; and (iii) nuclear power main equipment; turn-key construction of power station projects and other engineering projects; contract supply of complete sets of thermal and hydro power equipment; import and export of power equipment; technology transfer, technical consultation and services; and environmental protection engineering services.

Harbin Electric, together with its subsidiaries, was the oldest large-scale power plant equipment manufacturer in the PRC. Harbin Electric holds, as at the Latest Practicable Date, 50.93% of the issued share capital of the Company.

The Finance Company was duly established in the PRC as a non-banking financial institution in 2010. The principal business of the Finance Company includes the provision of, among others, deposit services, loan services, settlement services and other financial services. The Finance Company is regulated by the People's Bank of China (中國人民銀行) and the CBRC and provides its services in accordance with the rules and operational requirements of these regulatory authorities. The registered capital of Finance Company is RMB300 million. As at the Latest Practicable Date, Harbin Electric, the Company, 哈爾濱電機廠有限責任公司 (Harbin Generators Company Limited*) (a non-wholly owned subsidiary of the Company), 哈爾濱鍋爐廠有限責任公司 (Harbin Boiler Company Limited*) (a non-wholly owned subsidiary of the Company), 哈爾濱汽輪機廠有限責任公司 (Harbin Turbine Company Limited*) (a non-wholly owned subsidiary of the Company) and 佳木斯電機股份有限公司 (Jiamusi Electric Machine Company Limited*) (an indirect non-wholly-owned subsidiary of Harbin Electric) is interested in 51%, 21%, 8%, 8%, 8% and 4% of the equity interest of the Finance Company, respectively.

Reference is made to the Company's circular dated 19 April 2010 in respect of the financial services framework agreement dated 9 April 2010 entered into between the Company and Harbin Electric ("Previous Financial Services Framework Agreement"). The resolution to approve the transactions contemplated under the Previous Financial Services Framework Agreement was not passed by Independent Shareholders at the extraordinary general meeting held on 3 June 2010. As the Finance Company had not then been established, the Company entered into the Previous Financial Services Framework Agreement with Harbin Electric instead of the Finance Company and therefore provisions in the Previous Financial Services Framework Agreement which sought to impose certain obligations on the Finance Company might not be enforceable against the Finance Company in accordance with the PRC laws. However, this no longer presents an issue as the Finance Company has now been established and is a contracting party to the Financial Services Framework Agreement.

Having considered the reasons set out below, the Directors (including the independent non-executive Directors whose views are set out in the Letter from the Independent Board Committee) are of the view that the Financial Services Framework Agreement was entered into in the ordinary and usual course of business of the Group on normal commercial terms and the terms of which (including the proposed maximum daily

LETTER FROM THE BOARD

amount to be deposited with the Finance Company) are fair and reasonable and in the interests of the Company and the Shareholders as a whole:

- (i) the Finance Company is a non-bank financial institution approved and regulated by People's Bank of China (中國人民銀行) and CBRC and is engaged in providing various financial services in compliance with the rules and other operational requirements set by these regulatory authorities. The Finance Company will be required under 企業集團財務公司管理辦法 (Measures for the Administration of the Finance Companies of Enterprise Groups promulgated by the CBRC on 27 July 2004 (as amended on 28 December 2006)) to satisfy the following operation conditions in respect of assets and liabilities ratios:
 - (a) the capital adequacy ratio is not less than 10%;
 - (b) the balance of borrowings shall not exceed the total capital;
 - (c) the total amount of outstanding guarantees provided shall not exceed the total capital;
 - (d) the short-term securities investment to total capital ratio is not more than 40%;
 - (e) the long-term investment to total capital ratio is not more than 30%; and
 - (f) the self-owned fixed assets to total capital ratio is not more than 20%;
- (ii) the Finance Company will establish its system of internal control and risk management and implement the corporate governance guidelines in accordance with the requirements of the CBRC and are required under the Financial Services Framework Agreement to comply with the risk management measures outlined above;
- (iii) the Finance Company has provided an irrevocable undertaking to the Company that the interest rate for the deposits placed by the Group under the Financial Services Framework Agreement will be equal to the benchmark rates determined by the PBOC (which serves as an upper limit for deposit rates for all financial institutions in the PRC) from time to time and will not be downward adjusted. There is no assurance that the same rate of interest will be available to the Group from other commercial banks;
- (iv) given that the terms of the services available to the Group will be no less favourable than those offered by other PRC commercial banks, the Group can benefit from the lower cost of funding and other financial service charges and thereby enhancing the profitability of the Group. Pursuant to the Existing Financial Services Framework Agreement, the Finance Company has been providing to the Group free settlement services, guarantee services at a rate equal to or lower than those of other commercial banks and bill discount services at a rate substantially lower than those of other commercial banks;

LETTER FROM THE BOARD

- (v) the Finance Company will only provide financial services to members of the Harbin Electric Group and will therefore be exposed to a lower level of potential risk than other PRC commercial banks dealing with customers of various credit ratings. Based on the information published by the China National Association of Finance Companies (中國財務公司協會) and China Banking Regulatory Commission (中國銀行業監督管理委員會), corporate group finance companies industry as a whole had a lower bad loan ratio than commercial banks for the years 2007-2009. The risk of deposits with the Finance Company is further reduced by the undertaking given by Harbin Electric and the Group's right to set-off any amount owing by the Group to the Finance Company and/or Harbin Electric and its subsidiaries (other than the Group) against the deposits placed with the Finance Company;
- (vi) the arrangements with Finance Company under the Financial Services Framework Agreement provides the Group with an alternative but do not preclude the Group from using the services of other PRC commercial banks. The Group still maintains its own discretion in choosing other PRC commercial banks as its financial services provider as it thinks fit and appropriate for the benefit of the Group;
- (vii) the Company and its subsidiaries through its 45% equity interest in the Finance Company will be able to share the profits of the Finance Company; and
- (viii) increasing the maximum daily amount of the depository services between the Group and the Finance Company would provide an additional financial option for the Group and expand the operating scale of the Finance Company, and the Group may in turn enhance cost savings by obtaining more Financial Services on terms no less favourable than those offered by other commercial banks and enjoy more profits sharing through its shareholdings in the Finance Company.

Listing Rules Implications

Harbin Electric is the controlling shareholder of the Company. As the Finance Company is a subsidiary and therefore an associate of Harbin Electric and a connected person of the Company, the transactions contemplated under the Financial Services Framework Agreement constitute continuing connected transactions of the Company under the Listing Rules. As one or more of the applicable percentage ratios calculated in accordance with the Listing Rules in respect of the maximum daily amount of the Depository Services exceed 5% and the annual caps exceeds HK\$10,000,000, the Depository Services under the Financial Services Framework Agreement is subject to the reporting, announcement and Independent Shareholders' approval requirements under Chapter 14A of the Listing Rules.

LETTER FROM THE BOARD

As the Loan Services to be provided by the Finance Company to the Group for the benefit of the Group on normal commercial terms (or better to the Group) where no security over the assets of the Group, the Loan Services pursuant to the Financial Services Framework Agreement are exempt from the reporting, announcement and Independent Shareholders' approval requirements under Chapter 14A of the Listing Rules. There are no annual caps in respect of the Loan Services specified under the Financial Services Framework Agreement.

As it is expected that each of the applicable percentage ratios calculated in accordance with the Listing Rules in respect of the annual service charges and fees payable for the Settlement Services and the Other Financial Services will not exceed 0.1%, such transactions are exempt from the reporting, announcement and Independent Shareholders' approval requirements under Chapter 14A of the Listing Rules. Should such transactions exceed the exemption threshold in future, the Company will comply with the applicable connected transaction regulatory requirements under Chapter 14A of the Listing Rules.

None of the directors have a material interest in the transactions contemplated under the Financial Services Framework Agreement that would have required him to abstain from voting on the board resolutions approving such transactions.

RECOMMENDATION

Your attention is drawn to the letter from the Independent Board Committee as set out on page 17 of this circular which contains its recommendation to the Independent Shareholders in respect of the ordinary resolution set out in the notice of EGM set out on 38 to 39 of this circular to approve the Depository Services to be subject to the annual caps. Each of Harbin Electric and its associates will abstain from voting on the ordinary resolution to be proposed at the EGM.

The advice of the IFA to the Independent Board Committee and the Independent Shareholders as to whether the terms of the Depository Services and the annual caps in respect thereof are fair and reasonable and in the interest of the Company and its Independent Shareholders as a whole is set out on pages 18 to 32 of this circular.

FURTHER INFORMATION

Your attention is drawn to the additional information set out in the Appendix to this circular.

Yours faithfully,
By order of the Board
Harbin Power Equipment Company Limited
MA Sui
Company Secretary

* For identification purposes only



哈尔滨动力设备股份有限公司

HARBIN POWER EQUIPMENT COMPANY LIMITED

(A joint stock limited company incorporated in the People's Republic of China with limited liability)

(Stock Code: 1133)

18 May 2011

To the Independent Shareholders

Dear Sir or Madam,

CONTINUING CONNECTED TRANSACTIONS – FINANCIAL SERVICES FRAMEWORK AGREEMENT

We have been appointed as members of the Independent Board Committee to advise the Independent Shareholders of Harbin Power Equipment Company Limited (the “Company”) in respect of the resolution to approve the Depository Services subject to the annual caps in respect thereof, details of which are set out in the “Letter from the Board” contained in the circular of the Company (the “Circular”) of which this letter forms part. Unless the context otherwise requires, terms defined in the Circular shall have the same meanings when used in this letter.

Your attention is drawn to the “Letter from the Board”, the advice of the IFA in its capacity as the IFA to the Independent Board Committee and the Independent Shareholders in respect of whether (i) the terms of the Depository Services are on normal commercial terms, in the ordinary and usual course of business of the Group, fair and reasonable and in the interest of the Company and its Independent Shareholders as a whole; and (ii) the annual caps to which the Depository Services are subject are fair and reasonable so far as the Company and the Independent Shareholders are concerned, as set out in the “Letter from China Merchants Securities (HK) Co., Limited” as well as other additional information set out in other parts of the Circular.

Having taken into account the advice of, and the principal factors and reasons considered by the IFA in relation thereto as stated in its letter, we consider the terms of the Depository Services and the annual caps in respect thereof to be fair and reasonable and are in the interests of the Company and the Independent Shareholders as a whole. Accordingly, we recommend the Independent Shareholders to vote in favour of the ordinary resolution to be proposed at the EGM in respect of the Depository Services.

Yours faithfully,

Independent Board Committee

Sun Chang-ji

Jia Cheng-bing

Li He-jun

Yu Bo

Liu Deng-qing

Independent Non-executive Directors

The following is the text of a letter from China Merchants Securities (HK) Co., Limited for the purpose of incorporation in this circular, in connection with its advice to the Independent Board Committee and the Independent Shareholders in relation to the Depository Services contemplated under the Financial Services Framework Agreement.



48th Floor,
One Exchange Square,
Central,
Hong Kong

18 May 2011

*To: the Independent Board Committee and
the Independent Shareholders*

Dear Sirs,

**CONTINUING CONNECTED TRANSACTIONS
IN RESPECT OF THE DEPOSITORY SERVICES UNDER
THE FINANCIAL SERVICES FRAMEWORK AGREEMENT**

INTRODUCTION

We refer to our appointment as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in respect of the Depository Services contemplated under the Financial Services Framework Agreement, details of which are set out in the letter from the Board (the "Letter from the Board") contained in the circular dated 18 May 2011 (the "Circular") issued by the Company to the Shareholders, of which this letter forms part. Unless otherwise defined herein, capitalized terms used in this letter shall have the same meanings as defined in the Circular.

As stated in the Letter from the Board, Harbin Electric is the controlling shareholder of the Company and the Finance Company is a subsidiary of Harbin Electric. In accordance with the Listing Rules, (i) the Finance Company is therefore an associate of Harbin Electric and a connected person of the Company; and (ii) the proposed transactions contemplated under the Financial Services Framework Agreement constitute continuing connected transactions of the Company. As one or more of the applicable percentage ratios calculated in accordance with the Listing Rules in respect of the maximum daily amount of the Depository Services exceed 5% and the annual caps exceed HK\$10,000,000, the Depository Services is subject to, among other things, the Independent Shareholders' approval at the EGM. Each of Harbin Electric and its associates will abstain from voting on the relevant resolutions to be proposed at the EGM.

THE INDEPENDENT BOARD COMMITTEE

The Independent Board Committee comprising all the independent non-executive Directors, namely Mr. Sun Chang-ji, Mr. Jia Cheng-bing, Ms. Li He-jun, Mr. Yu Bo and Mr. Liu Deng-qing, has been established to consider and advise the Independent Shareholders on whether (i) the continuing connected transaction in relation to the Depository Services is in the ordinary and usual course of business; (ii) the terms of the Depository Services are on normal commercial terms which are fair and reasonable; and (iii) the proposed annual caps in relation to the Depository Services are fair and reasonable so far as the Independent Shareholders are concerned. We, China Merchants Securities (HK) Co., Limited, have been appointed to advise the Independent Board Committee and the Independent Shareholders in this regard.

BASIS OF OUR OPINION

In formulating our advice and opinion, we have relied on the accuracy of the information and facts supplied, and the opinions and representations expressed to us, by the Company, its executive Directors and its management. We have assumed that all information, facts, statements of belief, opinions and intentions and representations made to us by the executive Directors or referred to in the Circular were reasonably made after due and careful enquiry and are based on honestly-held opinions. We have also assumed that all information, representations and opinions made or referred to in the Circular and provided to us by the Company, its executive Directors and its management, for which they were solely and wholly responsible, were true, accurate and complete at the time they were made and continued to be true, accurate and complete at the date of the EGM. We have no reason to doubt the truth, accuracy and completeness of the information and representations referred to in the Circular and provided to us by the Company, its executive Directors and its management and have been advised by the executive Directors that they have collectively and individually accepted full responsibility for the accuracy of the information contained in the Circular, and have confirmed that no material facts have been omitted from the information provided to us and referred to in the Circular.

We consider that we have reviewed sufficient information to reach an informed view, to justify our reliance on the accuracy of the information contained in the Circular and to provide a reasonable basis for our recommendation. We have not, however, conducted any form of in-depth investigation into the business affairs, financial position and future prospects of the Harbin Electric Group (including the Group) and the Finance Company nor carried out any independent verification of the information supplied, representations made or opinions expressed by the Company and its executive directors and management.

PRINCIPAL FACTORS AND REASONS CONSIDERED

In formulating and giving our advice to the Independent Board Committee and the Independent Shareholders, we have taken into account the following principal factors and reasons:

1. Background to the Financial Services Framework Agreement and reasons for utilizing the Depository Services

(i) Background leading to the Financial Services Framework Agreement

Reference is made to the Company's circular dated 19 April 2010 in respect of the financial services framework agreement dated 9 April 2010 entered into between the Company and Harbin Electric ("Previous Financial Services Framework Agreement"). The resolution to approve the transactions contemplated under the Previous Financial Services Framework Agreement was not passed by Independent Shareholders at the extraordinary general meeting held on 3 June 2010. According to the Letter from the Board, as the Finance Company had not then been established, the Company entered into the Previous Financial Services Framework Agreement with Harbin Electric instead of the Finance Company and therefore provisions in the Previous Financial Services Framework Agreement which sought to impose certain obligations on the Finance Company might not be enforceable against the Finance Company in accordance with the PRC laws.

Subsequently, the Company and the Finance Company entered into financial services framework agreement on 14 December 2010 (the "2010 Financial Agreement") in respect of the Group's utilization of the financial services (including the depository services, loan services, settlement services and other financial services) to be provided by the Finance Company for a term of 3 years from the Board having approved the 2010 Financial Agreement and the transactions contemplated thereunder. The 2010 Financial Agreement is exempt from the then independent shareholders approval requirement because (i) based on the applicable percentage ratios, the depository services, the settlement services and other financial services do not exceed the relevant threshold under the Listing Rules; and (ii) the loan services is for the benefit of the Group on normal commercial terms where no security is granted over the assets of the Group, the loan services is exempt from the independent shareholders' approval requirement.

On 13 April 2011, the Company and the Finance Company entered into the Financial Services Framework Agreement in respect of, among other things, the Finance Company will provide the Financial Services to the Group for a term of 3 years from the Independent Shareholders having approved the Financial Services Framework Agreement and the financial services provided pursuant to the Financial Services Framework Agreement.

We are confirmed by the executive Directors that (i) the Financial Services Framework Agreement will replace the 2010 Financial Agreement and save for the increase in the maximum daily amount of the Depository Services and the

Settlement Services becoming free of charge, all the other major terms in the Financial Services Framework Agreement are the same to the 2010 Financial Agreement; and (ii) in the event that the Depository Services is not approved by the Independent Shareholders at the EGM, the Financial Services Framework Agreement will not proceed.

(ii) Reasons for and benefits of utilizing the Depository Services

We are advised by the executive Directors that the Group has been using the depository services provided by the Finance Company under the 2010 Financial Agreement since December 2010 and given the Finance Company was a newly established company which commenced operation since September 2010, the maximum daily deposit amount under the 2010 Financial Agreement is set at a prudent level.

As the utilization of depository services between the Group and the Finance Company has been carried out smoothly since the implementation of the 2010 Financial Agreement, we are advised by the executive Directors that they consider to increase the maximum daily amount of the depository services between the Group and the Finance Company would enable the Group to enjoy benefits such as (i) enjoying an additional financial option but not obligation for the Group and the Group may in turn enhance cost saving by obtaining more Financial Services on terms no less favourable than those offered by other commercial banks; and (ii) the Group would enjoy more profits sharing through its shareholding in the Finance Company as a result of the Finance Company having a larger operating scale. Furthermore, the executive Directors are of the view that the continuing connected transaction in relation to the Depository Services is entered into in the ordinary and usual course of business of the Group and is in the interests to the Company and its Shareholders given (i) the Finance Company is a licensed non-banking financial institution approved and regulated by the People's Bank of China and the CBRC; (ii) the Finance Company has customer base limited to members of the Harbin Electric Group and will therefore be exposed to a lower level of potential risk than other PRC commercial banks dealing with customers of various credit ratings; (iii) the Finance Company will provide a series of internal control and risk management measures under the Financial Services Framework Agreement; (iv) Harbin Electric and the Finance Company agreed to provide the guarantee/undertakings in order to protect the Group's deposits place with the Finance Company; (v) the terms of the services available to the Group will be no less favourable than those offered by other PRC commercial banks, the Group can benefit from the lower cost of funding and other financial services charges and thereby enhancing the profitability of the Group; and (vi) the China National Association of Finance Companies (中國財務公司協會) and China Banking Regulatory Commission (中國銀行業監督管理委員會) have published information stating that corporate group finance companies industry as a whole had a lower bad loan ratio than commercial banks for the years 2007-2009. We concur with the executive Directors' view in this regard.

2. Information on the Finance Company

(i) Background and business scope

The Finance Company is a non-bank financial institution approved and regulated by the People's Bank of China and the CBRC and is engaged in providing various financial services in compliance with the rules and other operational requirements set by these regulatory authorities. The principal business of the Finance Company includes the provision of, among others, deposit services, loan services, settlement services and other financial services.. The Finance Company will be required under 企業集團財務公司管理辦法 (Measures for the Administration of the Finance Companies of Enterprise Groups) promulgated by the CBRC on 27 July 2004 (as amended on 28 December 2006) to satisfy the following major operation conditions in respect of various assets and liabilities ratios:

- (a) the capital adequacy ratio is not less than 10%;
- (b) the balance of borrowings shall not exceed the total capital;
- (c) the total amount of outstanding guarantees provided shall not exceed the total capital;
- (d) the short-term securities investment to total capital ratio is not more than 40%;
- (e) the long-term investment to total capital ratio is not more than 30%; and
- (f) the self-owned fixed assets to total capital ratio is not more than 20%.

As advised by the executive Director, based on the unaudited financial statements of the Finance Company as at 31 December 2010 and the latest management account of the Finance Company as at 28 February 2011, the Finance Company was in compliance with all the ratio requirements as mentioned above as at 31 December 2010 and 28 February 2011.

(ii) Customer base

Since the customer base of the Finance Company is limited to members of the Harbin Electric Group, the executive Directors are of the view that to place deposit with the Finance Company will therefore be exposed to a lower level of potential risk than other PRC commercial banks dealing with customers of various credit ratings. The executive Directors further advised that the Finance Company did not experience bad debts so far.

(iii) *Shareholding*

As at the Latest Practicable Date, the Finance Company is owned as to 51% by Harbin Electric, 21% by the Company, 4% by an indirect non-wholly owned subsidiary of Harbin Electric, and collectively 24% by three non-wholly owned subsidiaries of the Company.

(iv) *Financial information*

As the Finance Company commenced operation in September 2010, it does not have full year financial results. According to the unaudited financial statements of the Finance Company prepared under the generally accepted accounting principles in the PRC for the four months ended 31 December 2010, the Finance Company recorded turnover, profit before tax and profit after tax of approximately RMB4.69 million, RMB1.03 million and RMB0.77 million respectively. In addition, the unaudited total assets and net assets value of the Finance Company as at 31 December 2010 amounted to approximately RMB1,192.73 million and RMB300.77 million respectively. The registered and paid-up capital of the Finance Company is RMB300 million.

Given the short operating history of the Finance Company, we have discussed with the executive Directors and understood that enlarging the proposed annual caps were considered acceptable given that based on the relevant regulations promulgated by the CBRC and the articles of association of the Finance Company, Harbin Electric, being the holding company of the Finance Company, has the obligation to take all required steps (including but not limited to injecting capital to the Finance Company based on its funding needs) to restore the financial position of the Finance Company in the event that the Finance Company experiences liquidity problems. Furthermore, in connection with the Financial Services Framework Agreement, Harbin Electric has issued a letter of undertaking to the Company to unconditionally and irrevocably undertake and guarantee that it will assume the liabilities of the Finance Company under the Financial Services Framework Agreement in certain situation, details of which are set out in the section headed "4. Principal terms of the Depository Services – (viii) Undertaking given by Harbin Electric to the Company" below. For background of Harbin Electric, please refer to the paragraph headed "3. Information on Harbin Electric" below.

(v) *Internal controls and risk management system*

As advised by the executive Directors, management of the Finance Company is carried out by its own board of directors, supervisory committee and senior management, which has established various functional committees including connected transaction control committee, risk management committee, audit committee, remuneration committee, nomination committee, credit review committee and investment committee. The board of directors of the Finance Company comprises 7 directors, 4 and 3 of which are nominated by Harbin Electric and the Group respectively, all of them possess relevant industry experience and/or

academic qualifications in economics, finance or accounting. There are seven departments in the Finance Company which include customer service department, settlement department, planning and finance department, risk management department, treasury department, internal audit department and administrative department.

As advised by the executive Directors, it is known that the various committees and departments have clearly defined roles in respect of maintaining the Finance Company's internal control and risk management system. Set out below is a summary of the respective key roles of each of the relevant committees/departments responsible for maintaining the risk management function and internal control environment of the Finance Company.

The risk management committee is responsible for (1) submitting risk management annual report; (2) reviewing the risk management strategy and major risk management solutions of the Finance Company; (3) reviewing the assessment criteria and mechanism relating to major decision making, major risk, major events and major operating process, and the risk assessment report on major decision; (4) reviewing the organization and the proposed responsibility of the risk management department; and (5) dealing with other matters on risk management authorized by the board of directors.

The credit review committee is responsible for (1) reviewing the manual on assessing credit rating and credit facility for the member companies; (2) reviewing credit related issues such as loans, trade finance, financial lease, guarantee and discounting, factoring, and performance bond, on both local and foreign currency; (3) reviewing the credit rating, credit facility and other credit related issues of the member companies; (4) supervising the relevant departments to implement the decisions made by the credit review committee; (5) reviewing and deciding on the classification of the assets under the loan business; (6) reviewing and deciding on the disposal and the parties responsible for doubtful loans; and (7) reviewing other matters as thought appropriate by the general manager, deputy general manager and chief professional.

The investment committee is responsible for (1) assessing the risk tolerance level of the Finance Company on securities investment, formulating principles on securities investment, investment strategy, investment objective, investment scale and asset allocation; (2) reviewing the scope and limit on securities investment; (3) reviewing long term equity investment proposals; (4) reviewing capital expenditure exceeding RMB500,000; (5) analyzing the result on the execution of investment decisions; (6) adjusting investment strategy on securities investment according to changes in investment market; (7) reviewing and deciding on the classification of the assets quality under the investment business; (8) reviewing and deciding on the disposal and the parties responsible for impaired investment; and (9) reviewing other matters as thought appropriate by the general manager, deputy general manager and chief professional.

The risk management department is responsible for the identification, measurement, monitor, assessment and report of various business risks. It (1) sets up the internal control system and the risk management system of the Finance Company, and carries out the works related to the risk management committee; (2) exercises risk control function o the Finance Company’s course of business activities including investment, loans, settlements and agency businesses; (3) manages the doubtful loans and the pledged assets; and (4) coordinates with the regulatory authorities, and consolidates and submits the relevant reports.

The internal audit department is responsible for (1) reviewing and auditing the business and the business procedure of the Finance Company; (2) inspecting the internal control function regularly; (3) reviewing and auditing the records on the carrying out of the Finance Company’s business activities; and (4) controlling the financial risk of the Finance Company.

(vi) *Guarantee given by Harbin Electric*

We are advised by the executive Directors that based on the relevant regulations promulgated by the CBRC and the articles of association of the Finance Company, in the event that the Finance Company falls into financial difficulty, Harbin Electric, being the holding company of the Finance Company, has the obligation to take all required steps, including but not limited to injecting capital to the Finance Company based on its funding needs, to restore the financial position of the Finance Company. In connection with the Financial Services Framework Agreement, Harbin Electric issued a letter of undertaking to the Company to unconditionally and irrevocably undertake and guarantee that it will assume the liabilities of the Finance Company under the Financial Services Framework Agreement in certain situation, details of which are set out in the section “4. Principal terms of the Depository Services – (viii) Undertaking given by Harbin Electric to the Company” below.

3. Information on Harbin Electric

Harbin Electric Group is principally engaged in the businesses of manufacturing power plant equipment, power system for ships and electrical driving system, its principal products include (i) thermal power equipment; (ii) hydro power equipment; (iii) nuclear power equipment; (iv) power system for ships; and (v) construction of integrated power generation sets. We are advised by the executive Directors that Harbin Electric is a state-owned enterprise established in the PRC which is directly supervised by the State Owned Assets Supervision and Administration Commission of the State Council of the PRC (中國國務院國有資產監督管理委員會). Furthermore, to the best of the executive Directors’ understanding, knowledge and belief, having made all reasonable enquiries, Harbin Electric Group is one of the largest power plant equipment manufacturers in the PRC.

4. Principal terms of the Depository Services

Set out below are the major terms relating to Depository Services contemplated under the Financial Services Framework Agreement:

(i) *Term*

The Financial Services Framework Agreement shall be for a term of 3 years from the date on which Independent Shareholders having approved the Financial Services Framework Agreement and the financial services provided pursuant to the Financial Services Framework Agreement. The 2010 Financial Agreement will be terminated upon the Financial Services Framework Agreement becoming effective.

Subject to the compliance with applicable laws and the Listing Rules, the term of the Financial Services Framework Agreement will upon expiry automatically be renewed for a further term of 3 years unless terminated by either party before the expiry of each term.

(ii) *Discretion given to the Group*

The Group is not under any obligation to obtain, among other things, the Depository Services from the Finance Company and may obtain such Depository Services based on its business needs.

(iii) *Nature of services*

The scope of services to be provided by the Finance Company under the Financial Services Framework Agreement includes, among other things, the Depository Services. Under the Financial Services Framework Agreement, the Group may from time to time deposit money with the Finance Company.

(iv) *Interest rates on deposits to be placed by the Group*

The Finance Company shall accept deposit from the Group at an interest rate not less than the interest rate as may be offered by any independent third party to the Group for the same type of deposits.

In addition, the Finance Company undertakes that the terms of, among other things, the Depository Services to be provided by the Finance Company to the Group will be no less favourable than those offered by independent third parties to the Group and the benchmark rates determined by PBOC (if applicable).

Based on our discussion with the executive Directors, we are given to understand that in the PRC, the deposit rates set by the PBOC represent the benchmark rates which serve as an upper limit for deposit rates for all financial institutions in the PRC. The financial institutions may offer deposit rates that are no higher than the benchmark rates. The executive Directors further advises that

during the period when the 2010 Financial Agreement has been in force, the Group's deposits placed with the Finance Company all enjoy the benchmark rates as stipulated by the PBOC without any downward adjustment. Furthermore, in connection with the Financial Services Framework Agreement, the Finance Company has provided an irrevocable undertaking to the Company that the interest rate for the deposits placed by the Group will be equal to the benchmark rates determined by the PBOC from time to time and will not be downward adjusted. In order to assess the interest rates offered by the Finance Company, we have checked the interest rate information in the website of PBOC and noted the PBOC announced three benchmark rates changes during the period from 14 December 2010 (being the date of the 2010 Financial Agreement) to 13 April 2011 (being the date of the Financial Service Framework Agreement), and we have reviewed the corresponding notices sent by the Finance Company to the members companies of Harbin Electric Group informing correspondence changes, among other things, in relation to the deposit interest rates offered and noted that the Finance Company changed the deposit interest rates offered whenever the PBOC adjusted the benchmark rates, and made the deposit interest rates equal to the benchmark rates without any downward adjustment.

(v) Usage of the deposits place by the Group

Moneys deposited by the Group with the Finance Company may only be deployed for services or products provided by PBOC or one or more other commercial banks in the Finance Company's ordinary course of business.

(vi) Credit to be extended to the Group

The annual credit that may be extended by the Finance Company to the Group should in principal not be less than the maximum amount of deposits made by the Group for each of the three years ending 31 December 2013.

(vii) Right to set-off deposits against loans

The Group is entitled to, to the extent permitted under the laws, to set-off any amount owing by the Group to the Finance Company and/or Harbin Electric and its subsidiaries (other than the Group) against the deposit (including the accrued interest) placed by the Group with the Finance Company. On the other hand, the Finance Company does not have the right to set-off any amount owing by the Group to it against any deposit (including the accrued interest) placed by the Group with the Finance Company. As stated in the Letter from the Board, the Company has been advised by its PRC legal advisers that there is no existing legal restrictions to set-off arrangement under the PRC laws.

(viii) Undertaking given by Harbin Electric to the Company

Harbin Electric has irrevocably and unconditionally provided a separate letter of undertaking to the Company that, where the Finance Company fails to pay any amounts when due or perform any of its obligations under the Financial Services Framework Agreement:

1. Harbin Electric will immediately pay such amounts and perform such obligations on demand of the Company as if Harbin Electric is the primary obligor;
2. to the extent permitted under the laws, in the event that the amount owing by the Group to Harbin Electric and any of its members (other than the Group) does not exceed the capital and accrued interest of the deposits placed by the Group with the Finance Company in accordance with the Financial Services Framework Agreement, the Company is entitled to set off such amount owing by the Group to Harbin Electric and any of its members (other than the Group) against the deposits placed by the Group. Harbin Electric shall sign and procure any of its member (other than the Group) to execute any document to effect such agreement in relation to such set-off; and
3. Harbin Electric will, on demand of the Group, promptly indemnify the Group for any losses suffered as a result of the non-performance of the Finance Company of its obligations under the Financial Services Framework Agreement, or invalidity or illegality of such obligations (which have caused any expenses, loss or liability incurred by the Group).

As stated in the Letter from the Board, the guarantee given by Harbin Electric under the letter of undertaking is a joint liability guarantee. The guarantee period shall be two years from the due date of the performance period of each principal indebtedness. Harbin Electric also agrees that if the Company and the Finance Company changes the performance period of any principal indebtedness, the guarantee period will commenced from the amended performance period. For the background of Harbin Electric, please refer to the paragraph headed "3. Information on Harbin Electric" above.

(ix) Guarantee given by Harbin Electric to CBRC

Harbin Electric has given a guarantee to the CBRC that it will make further capital contributions in the event that the Finance Company has difficulty in fulfilling its payment obligations to ensure normal operation of the Finance Company.

(x) *Internal controls and risk management measures*

As stated in the Letter from the Board, the Financial Services Framework Agreement provides for the following internal controls and risk management measures in order to safeguard the interests of the Shareholders.

- to ensure security of the deposits made by the Group in the Finance Company, the Finance Company is required to make sure the safe operation of the deposit management information systems which have passed all safety tests in relation to online bank interfaces of commercial banks, used direct dedicated line when connecting to commercial banks and reached safety standards of the PRC commercial banks and complied with the specifications under the CA safety certification;
- the Finance Company shall be operated in strict compliance with the risk monitoring indicators required by the CBRC and the major risk monitoring indicators such as the gearing ratio and liquidity ratio of the Finance Company shall adhere to the requirements of the CBRC and other applicable laws and regulations;
- a copy of each internal control report to be submitted by the Finance Company to the CBRC shall also be provided to the Company;
- if there occurs any circumstance that may affect the deposits placed by the Group with the Finance Company or any significant hidden danger which may undermine the safety of such deposits, the Finance Company shall inform the Group of the same within 2 working days from the date of such occurrence and adopt measures to prevent any loss or to minimize loss. On receipt of such notice, the Group is entitled to forthwith withdraw the deposit (together with interests accrued thereon). If the deposit (together with interests accrued thereon) could not be withdrawn, the deposit may be set-off against loans from the Finance Company;
- the Finance Company will by 10 a.m. on each working day provide the Company with a daily report on the status of the Group's deposits with the Finance Company to allow the Company to monitor and ensure that the average daily deposit balance with the Finance Company would not exceed the upper limit;
- the Finance Company will on the fifth working day of each month provide a monthly financial report of the previous month to the Company for review and the Finance Company will provide to the Company a copy of each regulatory report submitted to the CBRC within three working days after submission; and

- The Company may unilaterally terminate the Finance Service Framework Agreement if the Company and/or its subsidiaries may face material risk or loss as a result of the Finance Company's breach or possible breach of PRC laws and regulations, or the Finance Company's non-performance or breach of any provision of the Finance Service Framework Agreement, or the occurrence or possible occurrence of material operation problem or payment difficulty on the part of the Finance Company.

Given that (1) the Group is not under any obligation to obtain, among other things, the Depository Services from the Finance Company and may obtain such services based on its business needs; (2) the Finance Company shall accept deposit from the Group at an interest rate not less than the interest rate as may be offered by any independent third party to the Group for the same type of deposits; (3) the undertaking given by Harbin Electric as mentioned above; and (4) the implementation of internal controls and risk management measures under the Financial Services Framework Agreement, we are of the view that the terms in relation to the Depository Services are on normal commercial terms and are fair and reasonable and in the interests of the Company and the Independent Shareholders as a whole.

The proposed annual caps

The daily maximum outstanding balance of deposit (including accrued interest and handling fees) to be placed by the Group with the Finance Company is proposed to be RMB7,000 million for each of the three years ending 31 December 2013. This proposed annual caps (the "Annual Caps") of HK\$7,000 million represents approximately 58% of the average unpledged cash of the Group over the last three years ended 31 December 2010.

In addition, the Annual Caps were determined with reference to the following factors:

- (i) the amount of unpledged deposit the Group has placed with independent commercial banks as at 31 December 2008, 31 December 2009 and 31 December 2010;
- (ii) the utilization of the Depository Services when considered in the context of the Loan Services and the Settlement Services that are available to the Group can greatly facilitate deployment of surplus funds within the Group which can have a material impact as the business of the Group grows and its cash resources increase; and

- (iii) the possible favourable interest rate to be obtained by the Group from the Finance Company compared with interest rate that could otherwise be obtained by placing deposits with independent commercial banks.

In order to assess the reasonableness of the Annual Caps, we have discussed with the executive Directors and management of the Company and are advised that as the depository services between the Group and the Finance Company has been carried out smoothly since the implementation of the 2010 Financial Agreement, the relevant maximum daily deposit amount that was set at a prudent level could be increased so as to enable the Group to enjoy more benefits of utilizing the Financial Services provided by the Finance Company. Given that the Group may not be able to enjoy the benefits of utilizing the Financial Services provided by the Finance Company if the Annual Caps are set to low and that it may not be in the interests of the Company and its Shareholders as a whole if the Annual Caps are set too high, the executive Directors are of the view that through the Financial Services Framework Agreement, the Group can benefit from the flexibility in the allocation of its unrestricted cash should the terms be attractive to the Company and therefore to determine the Annual Caps in between the range of 50% and 100% of such average is reasonable and in the interests of the Company and its Shareholders as a whole.

In addition, we are further advised by the executive Directors that given the Financial Services Framework Agreement (i) has restricted the usage of the deposit placed by the Group (for details, please refer to the section headed “4. Principal terms of the Depository Services – (v) Usage of the deposits place by the Group” above); (ii) enables the Group to set-off any amount owing by it to the Finance Company and/or Harbin Electric and its subsidiaries (other than the Group) against the deposit placed by the Group; (iii) the respective undertaking and guarantee given by Harbin Electric to the Company and CBRC; and (iv) the internal controls and risk management measures as mentioned above, the executive Directors believe that the risk profile of placing deposit and enlarging the Annual Caps with the Finance Company is no greater than those of other independent commercial banks in the PRC.

Based on the aforesaid factors which have been taken into account by the executive Directors, we consider the basis in determining the Annual Caps were fair and reasonable and the Annual Caps of RMB7,000 million for each of the three years ending 31 December 2013, which are slightly higher than 50% of the Group’s average unrestricted and unpledged bank deposits, and cash and cash equivalents as at 31 December 2008, 2009 and 2010 to be acceptable to the Company and its Shareholders as a whole.

RECOMMENDATION

Having taking into account the above principal factors and reasons, we consider that (i) the Depository Services are in the ordinary and usual course of business of the Company; (ii) the terms of the Depository Services contemplated under the Financial Services Framework Agreement are on normal commercial terms, fair and reasonable and in the interests of the Company and its Shareholders as a whole; and (iii) the Annual Caps are fair and reasonable so far as the Independent Shareholders are concerned. Accordingly, we advise the Independent Board Committee to recommend the Independent Shareholders to vote in favour of the ordinary resolution to be proposed at the EGM to approve the Depository Services contemplated under the Financial Services Framework Agreement and the Annual Caps.

Yours faithfully
For and on behalf of
China Merchants Securities (HK) Co., Limited
Tony Wu
*Managing Director &
Head of Investment Banking Department*

1. RESPONSIBILITY STATEMENT

This circular, for which the directors of the issuer collectively and individually accept full responsibility, includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that to the best of their knowledge and belief the information contained in this circular is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement herein or this document misleading.

2. DISCLOSURE OF INTERESTS**I. Interests of Directors**

As at the Latest Practicable Date, so far as the Directors or supervisor of the Company are aware, none of the Directors or supervisor of the Company has interests and short positions in the Shares, underlying Shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO) which were required (a) to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they are taken or deemed to have under such provisions of the SFO); or (b) pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (c) pursuant to the Model Code for Securities Transactions by Directors of Listed Companies to be notified to the Company and the Stock Exchange.

II. Interests of Shareholders discloseable pursuant to the SFO

As at the Latest Practicable Date, so far as is known to the Directors or supervisor of the Company and based on the Company's register required to be maintained pursuant to section 336 of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong), the following persons (other than a Director or supervisor of the Company) had an interest or short position in the Shares and underlying Shares which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO or who were, directly

or indirectly, interested in 10 per cent. or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any other members of the Group are as follows:

(a) *Interests in the Shares*

Name of Shareholder	Number of Shares held (Class of Shares) Long position	Nature of Interest	Approximate % of the Company's issued total domestic share capital	Approximate % of the Company's total issued H share capital	Approximate % of the Company's total issued share capital
Harbin Electric	701,235,000 (Domestic Shares)	Beneficial owner	100%	-	50.93%
FMR LLC (<i>Note 1</i>)	42,856,000 (H Shares)	Investment manager	-	6.34%	3.11%
The Capital Group Companies Inc.	46,030,000	Investment manager	-	6.81%	3.34%

Notes:

1. Based on the filings made under the SFO, FMR LLC wholly-owns Fidelity Management & Research Company and Fidelity Management Trust Company, Pyramis Global Advisors LLC, which is interested in 46,742,000 H Shares and 1,874,000 H Shares respectively.
2. Based on the filings made under the SFO, The Capital Group Companies, Inc. wholly-owns Capital Group International. Inc., which in turn wholly-owns Capital Guardian Trust Company, Capital International, Inc., Capital International Limited, Capital International Sarl and Capital International K.K. Capital Guardian Trust Company, Capital International, Inc., Capital International Limited, Capital International Sarl are interested in 15,298,000 H Shares, 27,726,000 H Shares, 2,270,000 H Shares and 736,000 H Shares respectively.

(b) *Substantial Shareholders of other members of the Group*

As at the Latest Practicable Date, save as disclosed below and so far as is known to the Directors or supervisor of the Company, no person (not being a Director or supervisor of the Company) was interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of the other members of the Group.

Name of entitles holding 10% or more interest in a member of the Group	Interest in relevant company	Name of subsidiary of the Company
華融資產管理公司 (Huarong Asset Management Company*)	10.37%	哈爾濱電機廠有限責任公司 (Harbin Generators Company Limited*)
	26.96%	哈爾濱汽輪機廠有限責任公司 (Harbin Turbines Company Limited*)
Harbin Electric	40%	哈電發電設備國家工程研究中心有限公司 (Harbin Generator Equipment National Engineering Research Centre Company Limited*)
Harbin Electric	34.63%	哈爾濱電機廠(昆明)有限責任公司 (Harbin Electric Machinery (Kunmin) Company Limited*)
通用電氣(中國)有限公司 GE (China) Co. Ltd.)	49%	哈電通用風能(江蘇)有限公司 (Harbin General Wind Power (Jiangsu) Company Limited*)

Save as disclosed above, the Directors of the Company are not aware that there is any person (other than a Director or chief executive of the Company) who, as at the Latest Practicable Date, had an interest or short position in the Shares and underlying Shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who is, directly or indirectly, interested in 10 per cent. or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at a general meeting of any other member of the Group.

As at the Latest Practicable Date:

- (i) none of the Directors had any direct or indirect interests in any assets which have since 31 December 2010 (being the date to which the latest published audited consolidated financial statements of the Group were made up) been acquired or disposed of by or leased to any members of the Group, or are proposed to be acquired or disposed of by or leased to any members of the Group;

- (ii) none of the Directors was materially interested in any contracts or arrangements entered into by any members of the Group subsisting as at the Latest Practicable Date which is significant in relation to the business of the Group.

III. Directors' interests in competing business

As at the Latest Practicable Date, so far as is known to the Directors or supervisor of the Company, no other Directors or any of their respective associates had any interests in a business, which competes or may compete with the business of the Group.

3. DIRECTORS' SERVICE CONTRACTS

As at the Latest Practicable Date, none of the Directors or proposed Directors had entered into or proposed to enter into any service contract with any member of the Group (excluding contracts expiring or determinable by the employer within one year without payment of compensation (other than statutory compensation)).

4. MATERIAL ADVERSE CHANGE

The Directors are not aware of any material adverse change in the financial or trading position of the Group since 31 December 2010, being the date up to which the latest published audited consolidated financial statements of the Group were made up.

5. EXPERT

The following is the qualification of IFA, which has given its opinion or advice which is contained in this circular:

Name	Qualification
China Merchants Securities (HK) Co., Limited	a licensed corporation under the SFO authorised to carry out Type 1 (dealing in securities), Type 2 (dealing in futures contracts), Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities under the SFO

As at the Latest Practicable Date, the IFA did not have:

- (a) any direct or indirect interest in any assets which have since 31 December 2010 (being the date to which the latest published audited consolidated financial statements of the Group were made up) been acquired or disposed of by or leased to any member of the Group, or are proposed to be acquired or disposed of by or leased to any member of the Group; and

- (b) any shareholding in any member of the Group or the right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Group.

The IFA has given and has not withdrawn its consent to the issue of this circular with the inclusion of its letter and reference to its name in the form and context in which they respectively appear.

6. MISCELLANEOUS

In any event of inconsistency, the English language text of this circular shall prevail over the Chinese language text.

7. DOCUMENTS AVAILABLE FOR INSPECTION

A copy of the Financial Services Framework Agreement will be available for inspection during normal business hours on any weekday (except public holidays) at the office of Reed Smith Richards Butler at 20th Floor, Alexandra House, 18 Chater Road, Central, Hong Kong from the date of this circular, for a period of 14 days.

* *For identification purposes only*

NOTICE OF EGM



哈尔滨动力设备股份有限公司

HARBIN POWER EQUIPMENT COMPANY LIMITED

(A joint stock limited company incorporated in the People's Republic of China with limited liability)

(Stock Code: 1133)

NOTICE OF EXTRAORDINARY GENERAL MEETING

NOTICE IS HEREBY GIVEN that an extraordinary general meeting (the "EGM") of Harbin Power Equipment Company Limited (the "Company") will be held at 17th Floor Meeting Room, Block B, 39 Sandadongli Road, Xiangfang District, Harbin, Heilongjiang Province, the People's Republic of China on Wednesday, 6 July 2011 at 9:00 a.m. for the purposes of considering and, if thought fit, passing, with or without modifications, the following resolution of the Company:

ORDINARY RESOLUTION

1. "THAT:

- (A) the transactions contemplated under the financial services framework agreement entered into between the Company and 哈爾濱電氣集團財務有限責任公司 (HE Finance Company Limited*) on 13 April 2011 (the "Financial Services Framework Agreement") (a copy of which is produced to the meeting marked "A" and initialled by the chairman for the purpose of identification) and the annual caps for each of the three years ending 31 December 2011, 2012 and 2013 in respect of the receipt of depository services by the Company and its subsidiaries from 哈爾濱電氣集團財務有限責任公司 (HE Finance Company Limited*) in accordance with the terms of the Financial Services Framework Agreement be and are hereby approved; and
- (B) the directors of the Company be and are hereby authorised to take all actions and execute all documents which they deem necessary, desirable or appropriate in order to implement or give effect to the Financial Services Framework Agreement and transactions contemplated thereunder."

By order of the Board of
Harbin Power Equipment Company Limited
Ma Sui
Company Secretary

18 May 2011

* *For identification purposes only*

NOTICE OF EGM

Notes:

1. For the purpose of determining the list of shareholders entitled to attend and vote at the EGM, the Company shall temporarily suspend changes to the register of shareholders from 4 June 2011 to 5 July 2011 (both days inclusive). Shareholders whose names appear on the register at the time of the suspension of registration shall be entitled to attend and vote at the EGM. Person who purchased shares of the Company during the period of suspension of registration shall not be entitled to attend the EGM. In order to qualify the attendance at the EGM, all transfers documents, accompanied by the relevant share certificates, must be lodged with the Company's Registrar, namely, Hong Kong Registrars Limited at Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong no later than 4:00 p.m. on 3 June 2011.
2. Shareholders intending to attend the EGM shall give written notice of the same to the Company, which shall be lodged at the office address of the Company before 5:00 p.m. on 13 June 2011.
3. A Shareholder entitled to attend and vote at the EGM is entitled to appoint one or more persons (whether or not a shareholder of the Company) as his proxy to attend and vote on behalf of him.
4. To be valid, the form of proxy, together with a duly notarized power of attorney or other document of authority, if any, under which the form is signed must be deposited at the office address of the Company not less than 24 hours before the time appointed for holding the EGM.

As at the date of this notice, the Directors of the Company are:

Executive Directors:

Mr. Gong Jing-kun, Mr. Zou Lei, Mr. Duan Hong-yi,
Mr. Wu Wei-zhang and Mr. Shang Zhong-fu

*Independent non-executive
Directors:*

Mr. Sun Chang-ji, Mr. Jia Cheng-bing, Ms. Li He-jun,
Mr. Yu Bo and Mr. Liu Deng-qing