



**昆明机床**  
KUNMING MACHINE TOOL

**沈機集團昆明機床股份有限公司**

**SHENJI GROUP KUNMING MACHINE TOOL COMPANY LIMITED**

(A sino-foreign joint stock limited company established in the People's Republic of China with limited liability)  
(Stock Code: 0300)

**Create Classic of  
High Precision Machine Made in China**

---

Annual Report 2011

# CONTENT

1.	IMPORTANT NOTICE	2
2.	OVERVIEW OF THE COMPANY	3
3.	FINANCIAL AND OPERATING HIGHLIGHTS	5
4.	CHANGES IN SHARE CAPITAL AND SHAREHOLDERS	8
5.	DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS	13
6.	CORPORATE GOVERNANCE STRUCTURE	22
7.	CORPORATE GOVERNANCE REPORT	25
8.	SHAREHOLDERS' MEETING	32
9.	DIRECTORS' REPORT	33
10.	SUPERVISORY COMMITTEE'S REPORT	50
11.	SIGNIFICANT EVENTS	52
12.	FINANCIAL STATEMENTS	61
13.	SUPPLEMENTAL INFORMATION	166
14.	DOCUMENTS AVAILABLE FOR INSPECTION	167

## IMPORTANT NOTICE

1. The Board of Directors, Supervisory Committee, Directors, Supervisors and Senior Management Officers of the Company have declared that the information in this report does not contain any false information, misleading statements or material omissions and jointly and severally accept responsibility for the truthfulness, accuracy and completeness of the content of the report.
2. Eleven Directors of the Company attended the board meeting. Director Gao Minghui could not attend the Meeting due to official duties, and he appointed Director Wang Xing to vote on his behalf at the Meeting.
3. KPMG Huazhen has issued unqualified opinions in their auditor's report.
4. Name of chairman of the Company Wang Xing  
Name of chief financial officer of the Company Li Shunzhen  
Name of head of accounting department (accounting supervisor) Zhao Qiongfeng  
  
Mr. Wang Xing, Chairman, Ms. Li Shunzhen, Chief Financial Officer, and Ms. Zhao Qiongfeng, head of accounting department (Accounting Supervisor), have declared that they assured for the truthfulness and completeness of the financial statements in the Annual Report.
5. Any appropriation of non-operating fund by the controlling shareholder and its related parties?  
No
6. Any external guarantee provided not in compliance with the required decision-making procedures?  
No
7. This Annual Report is prepared in both English and Chinese. In the event that different interpretation occurs, the Chinese version shall prevail.

# OVERVIEW OF THE COMPANY

## 1. COMPANY INFORMATION

Name of the Company (Chinese)	沈機集團昆明機床股份有限公司
Abbreviated Name of the Company (Chinese)	昆明機床
Name of the Company (English)	SHENJI GROUP KUNMING MACHINE TOOL COMPANY LIMITED
Abbreviated Name of the Company (English)	kmtcl
Legal Representative	Mr. Wang Xing

## 2. CONTACT PERSON AND CONTACT INFORMATION

	Secretary to the Board	Securities Affairs Representative
Name	Mr. Luo Tao	Ms. Wang Bihui
Correspondence address	23 Ciba Road, Kunming City, Yunnan Province	23 Ciba Road, Kunming City, Yunnan Province
Telephone number	86-871-6166612	86-871-6166623
Facsimile number	86-871-6166288	86-871-6166288
E-mail	luotao@kmtcl.com.cn	wangbh@kmtcl.com.cn

## 3. BASIC INFORMATION

Registered address	23 Ciba Road, Kunming City, Yunnan Province, the PRC
Post code of registered address	650203
Business address	23 Ciba Road, Kunming City, Yunnan Province
Post code of business address	650203
Website	www.kmtcl.com.cn
E-mail	dsh@kmtcl.com.cn

## 4. PLACE OF INFORMATION DISCLOSURE AND DOCUMENT INSPECTION

Designated newspapers for publishing	China Securities Daily, Shanghai Securities News and Securities Times
Designated internet websites by CSRC for publishing annual report	http://www.sse.com.cn, http://kmtcl.com.cn and http://www.hkex.com.hk
Annual report available at	Office Building, 23 Ciba Road, Kunming City, Yunnan Province

# OVERVIEW OF THE COMPANY

## 5. SHARE LISTING

Class of Shares	Particulars of the Company's Shares			Short name before the change
	Stock Exchange	Short Name	Stock Code	
A Shares	Shanghai Stock Exchange	Kunming Machine	600806	
H Shares	The Stock Exchange of Hong Kong Limited	Kunming Machine	0300	

## 6. OTHER RELEVANT INFORMATION

Date of incorporation	19th October 1993	
Place of registration	Yunnan Commercial and Industrial Administration Bureau	
First Change	Date of Change of Registration	29th March 2002
	Place of Change of Registration	Yunnan Commercial and Industrial Administration Bureau
	Business Registration Number	530000400000458
	Tax Registration Number	530111622602196
	Organization Code	62260219-6
Second Change	Date of Change of Registration	1st December 2007
Third Change	Date of Change of Registration	11th October 2010
Fourth Change	Date of Change of Registration	10th August 2011
Appointed Auditor of the Company	KPMG Huazhen	
Address	8/F., Block 2, Dongfang Square, 1 Chang An Street East, Beijing City	

# FINANCIAL AND OPERATING HIGHLIGHTS

## I. PRINCIPAL ACCOUNTING DATA

### 1. In accordance with the PRC accounting standards ("PRC GAAP")

<u>Item</u>	<i>Unit: RMB</i> <b>Amount</b>
Operating profit	65,619,420.72
Total profit	68,784,096.53
Net profit attributable to the equity shareholders of the Company	54,567,125.16
Net profit excluding non-recurring items attributable to the equity shareholders of the Company	51,897,930.57
Net cash flow from operating activities	654,756.70

## II. NON-RECURRING ITEMS AND AMOUNTS

<u>Non-recurring item</u>	<b>Amount 2011</b>	<b>Amount 2010</b>	<i>Unit: RMB</i> <b>Amount 2009</b>
Gain or loss on disposal of non-current assets	<b>1,393,630.93</b>	666,520.12	(265,859.74)
Tax refund or exemption arising from unauthorized approval, without official approval document or contingency	-	-	17,172,846.19
Government grants included in current gains and losses (other than those closely related to the normal operating activities of the Company and those subject to a standard fixed amount or an ongoing lump sum amount in accordance with the government's policies)	<b>2,552,408.50</b>	6,700,335.00	10,514,558.30
Gain or loss from debt restructuring	<b>(905,350.26)</b>	2,568,942.39	54,764.13
Other non-operating income and expenses other than the above items	<b>123,986.64</b>	1,977,437.21	77,281.88
Impact on minority interests	<b>(19,918.60)</b>	-	(3,955,825.48)
Impact on income tax	<b>(475,562.62)</b>	(1,335,565.91)	(1,225,012.60)
Total	<b><u>2,669,194.59</u></b>	<b><u>10,577,668.81</u></b>	<b><u>22,372,752.70</u></b>

# FINANCIAL AND OPERATING HIGHLIGHTS

## III. PRINCIPAL ACCOUNTING DATA AND FINANCIAL HIGHLIGHTS FOR THE LATEST FIVE YEARS UP TO THE END OF THE REPORTING PERIOD

Principal accounting data	2011	2010	Increase/ Decrease as compared with the corresponding period last year (%)	2009	2008	2007
Operating income	1,804,857,564.29	1,597,705,267.19	12.97	1,372,196,639.36	1,563,105,398.47	1,302,385,627.67
Operating profit	65,619,420.72	188,947,210.70	(65.27)	220,419,929.11	292,024,056.18	282,722,373.57
Total profit	68,784,096.53	200,860,445.42	(65.76)	247,973,519.88	318,923,343.07	297,182,435.72
Net profit attributable to equity shareholders of the Company	54,567,125.16	178,324,801.52	(69.40)	215,847,994.25	276,564,904.31	242,957,688.27
Net profit excluding non-recurring items attributable to equity shareholders of the Company	51,897,930.57	167,747,132.71	(69.06)	193,475,241.55	250,747,388.75	209,690,728.85
Net cash flow from operating activities	654,756.70	129,272,783.34	(99.49)	105,749,466.18	120,047,854.09	265,050,299.92
	As at the end of 2011	As at the end of 2010	Increase/ Decrease as compared with the corresponding period last year (%)	As at the end of 2009	As at the end of 2008	As at the end of 2007
Total assets	2,558,664,361.12	2,247,730,361.63	13.83	2,024,433,625.56	1,911,770,243.50	1,779,007,685.99
Total liabilities	1,101,979,563.00	816,707,116.78	34.93	745,660,143.97	806,059,442.86	825,622,757.85
Owner's interest attributable to equity shareholders of the Company	1,402,138,349.42	1,374,125,279.42	2.04	1,217,014,036.12	1,041,230,512.25	879,379,127.95
Total share capital	531,081,103.00	531,081,103.00	-	424,864,883.00	424,864,883.00	424,864,883.00
	2011	2010	Increase/ Decrease as compared with the corresponding period last year (%)	2009	2008	2007
Basic earnings per share (RMB/share)	0.10	0.34	(69.50)	0.41	0.65	0.57
Diluted earnings per share (RMB/share)	0.10	0.34	(69.50)	0.41	0.65	0.57
Earnings per share calculated based on the latest share capital	0.10	0.34	(69.50)	0.41	0.52	0.46
Basic earnings per share excluding non-recurring items (RMB/share)	0.10	0.32	(69.16)	0.36	0.59	0.49
Return on net assets (weighted average) (%)	3.93	13.75	Decreased by 9.82 percentage points	19.06	27.18	32.06
Return on net assets based on net profit excluding non-recurring items (weighted average) (%)	3.74	12.98	Decreased by 9.24 percentage points	19.25	24.64	27.67
Net cash flow per share from operating activities (RMB/share)	0.001	0.24	(99.49)	0.20	0.28	0.62
	As at the end of 2011	As at the end of 2010	Increase/ Decrease as compared with the corresponding period last year (%)	As at the end of 2009	As at the end of 2008	As at the end of 2007
Net assets per share attributable to equity shareholders of the Company (RMB/share)	2.64	2.59	1.93	2.29	2.45	2.07
Gearing ratio (%)	43.07	36.33	Increased by 6.74 percentage points	36.83	42.16	46.41

## FINANCIAL AND OPERATING HIGHLIGHTS

### IV. RETURN ON NET ASSETS AND EARNINGS PER SHARE DISCLOSED ACCORDING TO DISCLOSURE REQUIREMENT SET OUT IN ISSUE NO. 9 OF "THE CONTENT AND FORMAT OF DISCLOSURE INFORMATION BY LISTED COMPANIES" ISSUED BY CSRC

Profit for the reporting period	Return on net assets (%)		Earnings per share (RMB)	
	Fully diluted	Weighted average	Basic earnings per share	Diluted earnings per share
Net profit attributable to ordinary shareholders of the Company	3.89	3.93	0.10	0.10
Net profit excluding non-recurring items attributable to equity shareholders of the Company	3.70	3.74	0.10	0.10

### V. MOVEMENT IN SHAREHOLDERS' EQUITY AND REASONS FOR THE CHANGE DURING THE REPORTING PERIOD

*Unit: RMB'000*

Item	Share Capital	Capital Reserve	Surplus Reserve	Undistributed Profit	Minority interests	Total Shareholders' equity
Opening balance	531,081.10	27,303.32	109,024.82	706,716.03	56,897.97	1,431,023.24
Profit for the year	-	-	-	54,567.13	(2,351.52)	52,215.61
Appropriation of surplus fund	-	-	7,483.18	(7,483.18)	-	-
Distribution of dividends for prior years	-	-	-	(26,554.05)	-	(26,554.05)
Closing balance	<u>531,081.10</u>	<u>27,303.32</u>	<u>116,508.00</u>	<u>727,245.93</u>	<u>54,546.45</u>	<u>1,456,684.80</u>



# CHANGES IN SHARE CAPITAL AND SHAREHOLDERS

## I. CHANGES IN SHARE CAPITAL

### 1. Table of changes in share capital of the Company

During the reporting period, there is no change in share capital.

### 2. Changes in selling restricted shares

Unit: Share

Name of shareholders	Number of selling restricted shares at the beginning of the year	Number of selling restricted shares released for the year	Increase in the number of selling restricted shares	Number of selling restricted shares at the end of the year	Reasons for selling restrictions	Date of release of selling restrictions
Shenyang Machine Tool (Group) Co., Ltd.	106,578,219	133,222,774	26,644,555	/	Committed to hold as stated in the agreement	31st December 2010
Yunnan Industrial Investment Holding Group Co. Ltd.	47,018,331	58,772,913	11,754,582	/	Committed to hold as stated in the agreement	31st December 2010
Total	<u>153,596,550</u>	<u>191,995,687</u>	<u>38,399,137</u>	<u>/</u>	/	/

Notes: 1) Shenyang Machine Tool (Group) Co., Ltd., a shareholder of the Company, was interested in 106,578,219 selling restricted shares of the Company before the change in capital share and 133,222,774 shares of the Company after the change in capital share, with no change in the proportion. The above shares held by such company were released from trading restrictions as of 1st January 2011. The Company has made an application for the listing of the selling restricted circulating shares in issue on 26th September 2011 and the application was only for the listing and circulation of the selling restricted shares in circulation. The Company has no plan to increase or decrease its shareholding recently.

2) Yunnan Industrial Investment Holding Group Co. Ltd., a shareholder of the Company, was interested in 47,018,331 selling restricted shares of the Company before the change in capital share and 58,772,913 shares of the Company after the change in capital share, with no change in the proportion. The above shares held by such company were released from trading restrictions as of 1st January 2011. The Company has made an application for the listing of the selling restricted circulating shares in issue on 26th September 2011 and the application was only for the listing and circulation of the selling restricted shares in circulation. The Company has no plan to increase or decrease its shareholding recently.

## II. ISSUANCE AND LISTING OF SECURITIES

### 1. Issuance of securities in the past three years

As at the end of this reporting period, no securities were issued and listed by the Company in the past three years.

### 2. Changes in total share capital and share structure

Please refer to the changes in share capital and relevant details.

### 3. Information of existing employee shares

As at the end of this reporting period, there were no employee shares.

# CHANGES IN SHARE CAPITAL AND SHAREHOLDERS

## III. SHAREHOLDERS AND BENEFICIAL CONTROLLERS

### 1. Number of shareholders and shares held by them

Total number of shareholders as at the end of the reporting period Unit: Share 44,904 (including 44,781 holders of A shares and 123 holders of H shares)

#### Shares held by the top ten shareholders

Name of shareholders	Nature of shareholders	Proportion (%)	Total number of shares held	Increase/Decrease during the reporting period	Number of selling restricted shares held	Number of shares pledged or frozen
HKSCC Nominees Limited	Foreign legal person	25.42	134,983,815			Unknown
Shenyang Machine Tool (Group) Co., Ltd.	State-owned legal person	25.08	133,222,774			No
Yunnan Industrial Investment Holding Group Co. Ltd.	State-owned legal person	11.07	58,772,913			No
Kunming Jinghua Co.	Domestic non-state-owned legal person	1.46	7,760,000			Unknown
Essence Securities Co. Ltd. – client credit trading guarantee securities account	Others	0.45	2,414,600			No
CHAN KWOK TAI EDDIE	Others	0.43	2,274,000			Unknown
Beijing Haifeng Media Co., Ltd. (北京海豐傳媒文化有限公司)	Others	0.36	1,894,200			Unknown
PICC Property and Casualty Company Limited – Traditional – General insurance products – 008C – CT001Shanghai	Others	0.24	1,253,430			Unknown
CAI QINGSHAN	Others	0.20	1,083,806			Unknown
Liang Kang	Others	0.14	730,000			Unknown

#### Selling unrestricted shares held by the top ten shareholders

Name of shareholders	Number of selling unrestricted shares	Type of shares
HKSCC Nominees Limited	134,983,815	Overseas listed foreign shares
Kunming Jinghua Co.	7,760,000	RMB ordinary shares
Essence Securities Co. Ltd. – client credit trading guarantee securities account	2,414,600	RMB ordinary shares
CHAN KWOK TAI EDDIE	2,274,000	Overseas listed foreign shares
Beijing Haifeng Media Co., Ltd. (北京海豐傳媒文化有限公司)	1,894,200	RMB ordinary shares
PICC Property and Casualty Company Limited – Traditional – General insurance products – 008C – CT001Shanghai	1,253,430	RMB ordinary shares
CAI QINGSHAN	1,083,806	Overseas listed foreign shares
Liang Kang	730,000	RMB ordinary shares
LIN JIANMING	702,306	Overseas listed foreign shares
Jiang Linxi	634,100	RMB ordinary shares

## CHANGES IN SHARE CAPITAL AND SHAREHOLDERS

### **Explanation of the connected relationship or acting in concert relationship among the above shareholders**

There is no connected relationship among the top ten shareholders of selling unrestricted circulating shares, legal person shareholders and state-owned legal person shareholders. The Company was not notified of any connected relationship or acting in concert relationship regulated by “Information Disclosure Management Procedure to Changes of Shareholding of Listed Company” among the above holders of selling unrestricted circulating shares of the Company. Among the top ten shareholders, there is no connected relationship among the holders of selling restricted circulating shares. The Company was not notified of any connected relationship between the holders of selling restricted circulating shares and the public shareholders; and any relationship among the public shareholders.

Other than the substantial shareholders disclosed above, as at 31st December, 2011, there were no other shareholders whose shareholdings exceeded the amount required to be disclosed under Article 60 of “Administration of the Issuing and Trading of Shares Provisional Regulations” of the PRC and Issue no.2 of “The Content and Format of Disclosure of Information of the Listed Companies” (amended in 2005); and under Section 16(1) of the Securities and Futures Ordinance under the Hong Kong Exchanges and Clearing Limited, the Company was not notified of any interests representing 10% or more of the issued share capital of the Company.

Among top ten shareholders, there are three shareholders holding 5% or more of the Company’s shares. They are HKSCC Nominees Limited, which holds the overseas listed foreign shares; Shenyang Machine Tool (Group) Co., Ltd., which holds the state-owned legal person shares; and Yunnan Industrial Investment Holding Group Co., Ltd., which holds state-owned legal person shares. All of the shares held by these shareholders are not pledged, frozen, mortgaged, nor designated.

#### *Notes:*

- 1) HKSCC (Nominees) Limited holds shares on behalf of clients. The Company did not receive any notification that any H shareholder held more than 10% in total share capital of the Company. Holders of H Shares who held more than 5% of total issued H Shares were as follows: on 17th February 2011, FIL Limited held 8,360,000 H Shares of the Company, representing 5.93% of total issued H Shares of the Company and 1.57% of total share capital of the Company.
- 2) Save as disclosed above, the Directors were not notified by any person (who is not a Director or a chief executive officer) who owns the interest or short position in the shares or underlying shares of the Company and shall be disclosed to the Company in compliance with the requirements contained in Divisions 2 and 3 of Part XV of Securities and Future Ordinance (“SFO”), or the interest or short position that shall be included in the prescribed register in accordance with section 336 of SFO.
- 3) As at 31st December 2011, none of the Directors and the Supervisors had any interests or short positions in the shares, underlying shares and/or debentures (as the case may be) of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which have been notified to the Company and the Hong Kong Stock Exchange pursuant to Division 7 and 8 of Part XV of the SFO, including interests or short positions which the Directors or the Supervisors are taken or deemed to have under such provisions of the SFO, or which are required to be and are recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code.

## CHANGES IN SHARE CAPITAL AND SHAREHOLDERS

### 2. Number of shares held by the top ten shareholders of selling restricted shares and the conditions of selling restriction

Unit: Share

No.	Name of shareholders of selling restricted shares	Number of selling restricted shares held	Trading of selling restricted shares		Conditions of selling restriction
			Date of trading	Number of additional shares to be traded	
1.	Shenyang Machine Tool (Group) Co., Ltd.	133,222,774	31st December 2010		Committed to hold as stated in the agreement
2.	Yunnan Industrial Investment Holding Group Co., Ltd.	58,772,913	31st December 2010		Committed to hold as stated in the agreement

Note: The selling restricted shares held by Shenyang Machine Tool (Group) Co., Ltd. and Yunnan Industrial Investment Holding Group Co., Ltd. were released from trading restrictions as of 1st January 2011. The Company has made an application for the listing of the selling restricted circulating shares on 26th September 2011 and the application procedures were only for the listing and circulation of the selling restricted shares in circulation. The Company has no plan to increase or decrease its shareholding recently.

### 3. Strategic investors or general legal persons as top ten shareholders as a result of placing of new shares

Name of strategic investors or general legal person	Commencement of agreed holding	Expiry of agreed holding
Shenyang Machine Tool (Group) Co., Ltd.	1st December 2006	31st December 2010
Yunnan Industrial Investment Holding Group Co., Ltd.	31st December 2005	31st December 2010

Note: Committed to hold until 31st December 2010.

### 4. Controlling shareholder and beneficial controller

#### (1) Controlling shareholder

Unit: RMB'000

Name	Person in charge or legal representative of the company	Date of incorporation	Registered capital	Principle activities
Shenyang Machine Tool (Group) Co., Ltd.	Guan Xiyou	18th December 1995	712,840	Manufacturing of metal cutting machines, CNC machines and mechanical equipment

#### (2) Legal beneficial controller

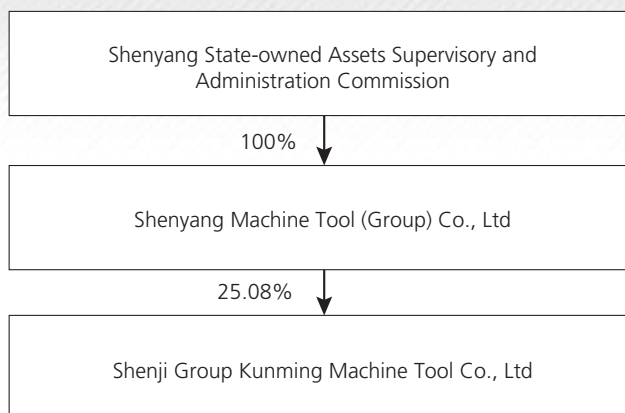
Name: Shenyang State-owned Assets Supervision and Administration Commission

#### (3) Changes in controlling shareholder and beneficial controller

During the reporting period, there was no change in controlling shareholder and beneficial controller.

## CHANGES IN SHARE CAPITAL AND SHAREHOLDERS

(4) Shareholding and controlling relationships between the Company and the beneficial controller



### 5. Other legal person shareholders holding over 10% shares of the Company

Name of legal person shareholder	Legal representative	Date of incorporation	Principal operating or managing activities	Unit: RMB'000
				Registered capital
Yunnan Industrial Investment Holding Group Co., Ltd.	Gong Lidong	October 2000	Engages in investment, financing, and assets operation and management, merger and acquisition of enterprises, stock trading, state-owned assets trusted management and trusted disposal in various industries and different business; domestic and international trade; other businesses approved by the Yunnan Provincial Government	6,000,000

# DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

## I. DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

Name	Title	Gender	Age	Date of appointment	Number of shares held as at 1st January 2011	Number of shares held as at 31st December 2011	Reasons for the change	Remuneration and allowances received	Unit: Share	
									Total emoluments received during the reporting period (RMB ten thousand) (before tax)	Remuneration and allowances received from shareholder's business unit or other associated business unit
Wang Xing	Chairman, Executive director Non-executive director	Male	46	28th July 2011 to 31st October 2014 23rd March 2007 to 28th July 2011				Yes	27.10	Yes
Li Zhenxiong	Vice chairman	Male	49	23rd March 2007 to 31st October 2014				No	0	Yes
Zhang Xiaoyi	Vice chairman, Executive director General manager	Male	47	31st October 2008 to 31st October 2014 29th April 2008 to 31st October 2014				Yes	71.49	No
Ye Nong	Executive director Vice general Manager	Male	51	23rd June 2010 to 31st October 2014 30th December 2006 to 31st October 2014				Yes	65.00	No
Li Shunzhen	Executive director Financial controller	Female	39	31st October 2011 to 31st October 2014 31st October 2011 to 31st October 2014				Yes	8.00	No
Guan Xin	Non-executive director	Male	43	23rd June 2010 to 31st October 2014				Yes	4.50	Yes
Gao Minghui	Non-executive director Chairman, Executive director	Male	48	28th July 2011 to 31st October 2014 30th December 2006 to 28th July 2011				Yes	63.46	Yes
Zhang Tao	Non-executive director	Male	41	31st October 2008 to 31st October 2014				No	0	Yes
Liu Minghui	Independent non-executive director	Male	47	23rd March 2007 to 23rd March 2013				Yes	11.90	No
Li Dongru	Independent non-executive director	Female	56	29th June 2007 to 29th June 2013				Yes	11.90	No
Chen Fusheng	Independent non-executive director	Male	47	18th July 2011 to 31st October 2014				Yes	8.33	No
Xiao Jianming	Independent non-executive director	Male	65	31st October 2011 to 31st October 2014				Yes	2.38	No
Shao Li	Chairman of the Supervisory Committee	Male	53	31st October 2008 to 31st October 2014				Yes	47.29	No
Tang Hua	Supervisor	Female	54	10th May 2011 to 31st October 2014				Yes	2.09	Yes
Fan Hong	Supervisor	Male	48	31st October 2008 to 31st October 2014				No	0	Yes
Cai Zhemin	Supervisor	Male	49	10th May 2011 to 31st October 2014				Yes	2.09	Yes
Qin Jianzhong	Supervisor elected by staff	Male	58	31st October 2011 to 31st October 2014				Yes	33.35	No
Zhu Xiang	Vice general manager	Male	46	20th August 2007 to 31st October 2014				Yes	58.23	No
Zhou Guoxing	Vice general manager	Male	49	10th April 2006 to 31st October 2014				Yes	46.26	No
Xu Kunping	Vice general manager	Male	42	10th February 2009 to 31st October 2014				Yes	53.19	No
Luo Tao	Secretary to the Board	Male	36	28 May 2008 to 31 October 2014				Yes	38.38	No
Pi Jianguo	Executive director Financial controller	Male	40	23rd March 2007 to 31st October 2011 30th December 2006 to 31st October 2011				Yes	50.83	No
Wayne Yu	Independent non-executive director	Male	48	16th June 2005 to 15th June 2011				Yes	7.86	No
Chen Ying	Independent non-executive director	Male	58	23rd March 2007 to 31st October 2011				Yes	9.52	No
Xiang Rong	Supervisor elected by staff	Male	46	31st October 2008 to 31st October 2011				Yes	28.14	No
Gao Xingang	Supervisor	Male	41	31st October 2008 to 18th March 2011				Yes	0.46	Yes

## DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

### Major working experience of Directors, Supervisors and Senior Management in the past 5 years:

1. **Wang Xing**, male, born in 1965. He graduated from Harbin University of Science and Technology majoring in auditing in 1989. He is currently an undergraduate of the MPACC at Dongbei University of Finance and Economics. In 1989, he worked for the Auditing Department of Shenyang First Machine Tool Factory. In early 1996, he worked for the Finance Department of Shenyang Machine Tool (Group) Co., Ltd. Later that year he joined the liquidation team of Shenyang Third Machine Tool Factory. In January 2001, he acted as the vice general manager and the head of Finance Department of Zhong Jie Machine Tool Co., Ltd. At the end of 2003, he worked as the vice general manager and the head of Finance Department of Shenyang CNC Machine Tool Co., Ltd. From 2006, he was the director and the head of Finance Department of Shenyang Machine Tool (Group) Co., Ltd. Since March 2007, he has held the positions of vice general manager and the head of Finance Department of Yunnan CY (Group) Co., Ltd. On 23rd March 2007, he was appointed as the director of the Company. On 28th July 2011, he was appointed as the chairman of the Company. His tenure of appointment will expire on 31st October 2014.
2. **Zhang Xiaoyi**, male, born in April 1964, holding master postgraduate qualification and a bachelor degree and is a senior engineer. He is currently the vice-chairman, executive director, general manager and deputy secretary to the Committee of Communist Party of China ("CPC") of the Company. Mr. Zhang joined Kunming Machine Tool Factory in 1985. He has extensive experience in machinery design and technology management. He worked as the deputy manager, manager of the technical center of the Company, general manager assistant and chief engineer, vice general manager and general manager of the Company. From 29th April 2008 till now, he has been the general manager of the Company. His tenure of appointment will expire on 31st October 2014.
3. **Gao Minghui**, male, born in 1963, holding a bachelor degree and postgraduate qualification. He is currently the non-executive director and secretary to the Committee of CPC of the Company. He graduated from the Northeastern University majoring in engineering in 1988. Mr. Gao was a researcher, deputy manager and manager of the Research and Development Department of Shenyang First Machine Tool Factory. Then he was the deputy chief engineer, assistant to general manager, deputy general manager, and general manager of Shenyang First Machine Tool Factory. Starting from January 2002, he had also been as the deputy general manager of Shenyang Machine Tool Co., Ltd. He had been the chairman of the board of directors of Yunnan Machine Tool Factory (now known as Yunnan CY Group Co., Ltd. since the change of name in 2006) from August 2004. Since 2006, he had been the chairman of Shenyang Machine Tool (Group) Co., Limited. He was appointed as the director of the Company on 30th October 2006. During 23rd October 2007 to 29th April 2008, he was also the general manager of the Company. During 30th December 2006 to 28th July 2011 he was the chairman of the Company. His tenure of appointment will expire on 31st October 2014.
4. **Guan Xin**, male, born in May 1968, holding a master post-graduate diploma, senior economist. Mr. Guan started his career in August 1990. From February 2005 to August 2009, Mr. Guan was the director of securities unit, general manager assistant, head of financial department, secretary to the board, vice general manager of Shenyang Machine Tool Co., Ltd. Meanwhile, he was the director of the Strategic Investment Unit of Shenyang Machine Tool (Group) Co., Ltd. From August 2009 to November 2009, he was the general manager assistant and the head of finance and investment unit of Shenyang Machine Tool (Group) Co., Ltd. Since November 2009, he has been the vice general manager of Shenyang Machine Tool (Group) Co., Ltd. On 23rd June 2010, he was appointed as the director of the Company. His tenure of appointment will expire on 31st October 2014.

## DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

5. **Ye Nong**, male, born in November 1960, holding postgraduate qualification and is an engineer. Mr. Ye currently is the vice general manager of the Company. During February 2000 to May 2002, he was the manager of the Technology Department of Shenyang Machine Tool (Group) and the vice president of Shenyang Machine Tool Design Institute. During May 2002 to December 2003, he was the manager of the Quality Control Department of Zhongjie Machine Tool Co., Ltd. He was the manager of Production Department of Zhongjie Machine Tool Co., Ltd. from December 2003 to June 2006. Since June 2006, he has worked for the Company as general manager assistant and vice general manager. On 23rd June 2010, he was appointed as the director of the Company. His tenure of appointment of vice general manager will expire on 31st October 2014.
6. **Li Zhenxiong**, male, born in May 1962, holding master postgraduate qualification and is an assistant economist. He is currently the vice-chairman of the Company. Mr. Li joined Kunming Machine Tool Factory in 1985 and worked as the technician for construction and the head of construction team. During October 1993 to July 2002, he was the general manager and secretary to the committee of CPC of Kunming Kunji Group Construction Company. Since August 2002, he has acted as the general manager assistant, member of party committee, vice general manager and general manager of Kunming Kunji Group Company. He is now the general manager assistant of Yunnan Industrial Investment Holding Group Co., Ltd. His tenure of appointment will expire on 31st October 2014.
7. **Zhang Tao**, male, born in June 1970, holding a bachelor degree and is an engineer. Mr. Zhang graduated from the Department of Architecture of Yunnan Industrial University majoring in city roads and bridges in 1991. During July 1991 to December 1993, he worked as the technician and subsequently the assistant engineer for the Kunming railroad second maintenance team under Chengdu Railroad Bureau. During December 1993 to May 1996, he was the secretary to the office of Kunming Railroad Bureau. During May 1996 to June 2004, he worked as the vice manager, manager and the vice chairman of the Labor Union of Yunnan Guangda Railroad Co., Ltd. During June 2004 to March 2008, he held the positions of office manager, secretary to the board, general manager assistant and vice chief engineer at Dianxi Railroad Co., Ltd. Since March 2008, he has been the general manager of Investment Department of Yunnan Industrial Investment Holding Group Co., Ltd. His tenure of appointment will expire on 31st October 2014.
8. **Li Shunzhen**, female, born in April 1972, holding a bachelor degree, certified public accountant, senior accountant. Ms. Li graduated at Jiangxi University of Finance and Economics in 1995 in the major of investment and economic management. From July 1995 to March 1998, she worked at the First Engineering Company under Yunnan Railway Construction handling project budget and as an accountant. From March 1998 to July 2002, she worked at Yunnan Guang Da Railway Maintenance Company as an accountant. From July 2002 to August 2008, she worked at Yunnan State-owned Assets Operation Company Limited as an accountant in finance department. From August 2008 to June 2011, she worked at Yunnan Industrial Investment Holding Group Company Limited as an accountant in finance department. Since June 2011, she has worked at Shaoyang Industrial Development Co., Ltd. under Yunnan Industrial Investment Holding Group Company Limited as a chief financial officer. Her tenure of appointment will expire on 31st October 2014.
9. **Liu Minghui**, male, born in 1964, is a professor and tutor of doctoral students and certified public accountant. During August 1987 to May 2000, he was an assistant lecturer, lecturer, associate professor and professor in Dongbei University of Finance and Economics. Since May 2000, he has been a tutor of doctoral students. During March 2001 to January 2004, he was the head of Jinqiao Faculty of Business at Dongbei University of Finance and Economics. During January 2004 to October 2004, he was the general manager of Dongbei University of Finance and Economics Magazine Company. From October 2004, he has held the positions of vice president of Dalian Newspaper Group and president of Dalian Publisher. He is also the director, vice-secretary general of China Accounting Association, a president of a branch of Cost Accounting Association, a president of a branch of Cost Accounting Association, director of China Auditing Association etc. His tenure of appointment will expire on 23rd March 2013.



## DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

10. **Li Dongru**, female, born in 1955, Han nationality, member of the CPC, professor level senior engineer, holding postgraduate qualification. Ms. Li is working at the China Machinery Industry Federation (the "Federation"). Starting from January 2001, she has been the manager of the Science and Technology Department of the Federation and is responsible for the management of the machinery industry. During the periods of the Ninth and Tenth Five-year plans, she organized or managed the implementation of "Research and Development in Engineering of CNC Technology and Equipment (數控技術與裝備工程化的研究與開發)", a key project for the state-level science and technology development plan of the Ninth Five-year plan such as and "Development and Studies of New Generation CNC System Platform(新一代數控系統平台的開發研究)", a the key project for the national technological innovation plan of the Ninth Five-year plan. She organized the feasibility evaluation and implementation of key projects for the state-level science and technology development plan of Tenth Five-year plan, namely "Research and Practical Demonstration of Precision Manufacturing and Key CNC Technology (精密製造與數控關鍵技術研究和應用示範)" and "Research and Development of Advanced Production Technique for Basic Components and Its Application (先進製造基礎件技術研究開發與應用)". She also participated in the feasibility evaluation and annual implementation of "Key CNC Technology and Supporting Technology for Equipment Industrialization and Their Applications (數控關鍵技術與裝備產業化支持技術及應用)", a project focused on the subject field of technologies on robots under the area of advanced manufacturing and automation technology of 863 Program. Her tenure of appointment will expire on 29th June 2013.
11. **Chen Fusheng**, male, born in 1965, doctor of accountancy, master of economics, member of American Accounting Association, member of Hong Kong Academic Accounting Association. During 1996 to 1998, he was a part-time demonstrator of the Faculty of Business at University of Alberta in Canada. In 2006, he was a visiting professor at Tsinghua University. He is now an associate professor in accounting of the Faculty of Business at the Hong Kong University of Science and Technology, editor of "International Accounting Research Journal", specialized professor of the Faculty of Business at Nanjing University and the Faculty of Accounting at Shanghai University of Finance and Economics. His tenure of appointment will expire on 31st October 2014.
12. **Xiao Jianming**, male, born in November 1947, holding a bachelor degree, senior political officer, part-time professor of Kunming Polytechnic University Management College. From September 1968 to May 1971, he worked for a construction brigade under the fourteen metallurgy construction group second construction company. From May 1971 to August 1978, he worked at the material supply department of the fourteen metallurgy construction group. From September 1982 to February 1984, vice division chief of secretary department under the office of committee of CCP of the fourteen metallurgy construction group. From February 1984 to July 1987, he was the vice section chief of publicity section. From July 1987 to January 1993, he was the secretary to the committee of CCP of the equipment and materials company under the fourteen metallurgy construction group. From January 1993 to December 1997, he was the secretary to the committee of CCP of Kunming Prospecting Design Institute of China Nonferrous Metal Industry. From December 1997 to November 1998, he was the secretary to the committee of CCP of Yunnan Stannum Industry Company. From November 1998 to September 2001, he was the secretary to the committee of CCP and general manager of Yunnan Stannum Industry Company. From September 2001 to December 2007, he was the secretary to the committee of CCP and chairman of Yunnan Stannum Industry Group. From December 2007 to February 2011, he was the vice section chief of the finance and economic committee under the people's congress of Yunnan province. He retired on March 2011. His tenure of appointment will expire on 31st October 2014.
13. **Shao Li**, male, Han nationality, born in 1958, holding a master degree and is deputy researcher. He is currently the deputy secretary to the Committee of CPC of the Company and chairman of the Supervisory Committee. Mr. Shao joined the Second Light Industry Bureau of Kunming City in February 1984 as a deputy office manager. In May 1987, he worked for Publicity Department under the Committee of CPC in Kunming City as the office manager, and subsequently the assistant to the director of the department. In December 1992, he worked for Research Center of Kunming City Government as a deputy director. In August 2000, he worked for the Enterprises Union Department under the Committee of CPC in Yunnan Province as the deputy office manager and subsequently the director of the research center. In February 2003, he worked for Yunnan State-owned Assets Supervision and Administration Commission as the director of Policy and Statute Department. Since October 2007, Mr. Shao has been the deputy secretary to the Committee of CPC of the Company. His tenure of appointment will expire on 31st October 2014.

## DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

14. **Fan Hong**, male, born in June 1963, holding a bachelor degree and is an engineer. Mr. Fan graduated from Jiangxi University of Finance & Economics majoring in finance in 1987. During July 1987 to September 1992, he worked for the Provincial Department of Finance of Yunnan. During August 1992 to February 2005, he worked as the department manager for Yunnan International Trust and Investment Company. Since February 2005, he has held the positions of trust department manager, risk control department manager and policy and statute department manager and general manager assistant. On August 2011, he was appointed as chairman of Yunnan Equity Exchange Co. Ltd.. His tenure of appointment will expire on 31st October 2014.
15. **Tang Hua**, female, born in 1957, member of the CPC, holding postgraduate qualification, senior engineer, senior political officer, now is the chairman of the labor union of Shenyang Machine Tool (Group) Company Limited. Ms. Tang went into workforce in 1975. In 1994, she joined Shenyang Machine Tool (Group) Company Limited and has successively held the posts of sales person, executive officer in overseas business unit. From 1997 to 2007, she was the office manager of the union and vice chairman of the union. From 2007 to 2008, she was the secretary to the Third Committee of CPC, secretary of Discipline Inspection Commission and the Chairman of the labor union. She has been the vice chairman and chairman of the labor union since 2008. Her tenure of appointment will expire on 31st October 2014.
16. **Cai Zhemin**, male, born in 1962, member of the CPC, holding college diploma, engineer, now is the head of the strategy planning department of Shenyang Machine Tool (Group) Company Limited. Mr. Cai went into workforce in 1981. In 1996, he joined Shenyang Machine Tool (Group) Company Limited and was successively the official of technology department, production department, planning department. From 2007 to 2008, he was the manager of the planning department. From 2008 to 2009, he was the manager of engineering planning department of Shenyang Machine Tool Company Limited. From 2009, he has been the head of the strategy planning department of Shenyang Machine Tool (Group) Company Limited. His tenure of appointment will expire on 31st October 2014.
17. **Qin Jianzhong**, male, born in September 1954, holding a postgraduate qualification, senior economist. He is currently the chairman of the Union and the supervisor elected by staff of the Company. He joined Kunming Machine Tool Factory in 1982 and has held the position of technician, deputy director and the director of Workshop, deputy head and head of the Labour and Personnel Section, Supervisor of the Supervisory Committee of the Company, director of the Board, vice general manager and secretary to the Committee of CPC of the Company. His tenure of appointment will expire on 31st October 2014.
18. **Zhu Xiang**, male, born in April 1966, holding master postgraduate qualification and is a senior engineer. He is currently the vice general manager. He joined Kunming Machine Tool Factory in 1988. He has extensive experience in machine tool products design and sales management. He has held the positions of vice director of Assembly Sub-Plant of Kunming Machine Tool Factory, deputy director of the Technology Centre, vice manager of the Sales Department, manager of Sales Company, general manager assistant, and from 20th August 2007, the vice general manager of the Company. His tenure of appointment will expire on 31st October 2014.
19. **Zhou Guoxing**, male, born in November 1962, holding a master degree and is a senior engineer. He is currently the vice general manager of the Company. Mr. Zhou joined Kunming Machine Tool Factory in 1987 and has extensive experience in machine tool design and production management. He was the manager of the Laboratory of the Company; vice manager and manager of the Technical Center; deputy chief engineer; manager of the Manufacture Center; general manager assistant and the head of the assembly sub-plant; chief engineer and from 10th April 2006, the vice general manager of the Company. His tenure of appointment will expire on 31st October 2014.
20. **Xu Kunping**, male, born in November 1969, holding a bachelor degree and currently engaged in postgraduate study for a master degree, a senior engineer. He is currently the vice general manager of the Company. Mr. Xu joined Kunming Machine Tool Factory in 1991 and has extensive experience in machine tool R&D and design, technical management and sales management. From 1993, he was the designer, machine room manager, vice director, director and general manager assistant of the Technical Center. Since 24th March 2010, he has been the vice general manager of the Company, responsible for the marketing efforts. His tenure of appointment will expire on 31st October 2014.

## DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

21. **Luo Tao**, male, born in July 1975, holding a master degree and postgraduate qualification. He is currently the secretary to the Board of the Company (joint company secretary) and affiliate member of the Hong Kong Institute of Chartered Secretaries. Starting from October 2005, he has held the positions of assistant secretary to the Board and the manager of the office of the Board of the Company, manager of the office of general manager and securities affairs representative. Since May 2008, he has been the secretary to the Board of the Company. His tenure of appointment will expire on 31st October 2014.
22. **Wayne Yu**, male, born in 1963, holding a doctorate degree in finance and is a tutor of doctoral students. He is a professor of the Faculty of Accounting and Finance at Hong Kong Polytechnic University and an associate dean of the Graduate School of Business of Hong Kong Polytechnic University; chartered financial analyst; the Chief Editor of "China Accounting and Finance Review"; and specialized professor of the Faculty of Accounting at Shanghai University of Finance and Economics. During 1998 to 1999, he was an associate professor of the Faculty of Business at Queen's University in Canada; during 1996 to 1998, he was an associate professor of the Faculty of Management at University of Lethbridge in Canada; during 1994 to 1995, he was a visiting professor of the Faculty of Management of Xi'an Jiaotong University; during 1992 to 1996, he was a part-time lecturer of the Faculty of Business at University of Alberta in Canada. His tenure of appointment expired on 15th June 2011.
23. **Chen Ying**, male, born in 1953, is a senior engineer. During 1997 to 1999, he was the chairman and general manager of Yunnan Transformer Co., Ltd. During 1999 to 2003, he was the chairman of Yunnan Transformer Electric Co., Ltd. During 2000 to 2003, he was the chairman and general manager of Kunming Securamid Electric Co., Ltd. During 2003 to 2004, he was the Mayor Assistant of Kunming City. During 2004 to 2006, he was the vice mayor of Kunming City. Since April 2006, he has been the chairman of Yunnan Transformer Electric Co., Ltd. His tenure of appointment expired on 31st October 2011.
24. **Pi Jianguo**, male, born in July 1971, holding a bachelor degree and is a certified public accountant, certified assets valuer, certified tax commissioner and senior accountant. He is currently the executive director and chief financial officer of the Company. During October 1999 to January 2002, Mr. Pi worked in the Industrial Department of Chuxiong State-owned Assets Company. During January 2002 to April 2005, he was the vice manager of the Auditing Department of Yunnan Huitong Accounting Firm. During May to December, 2005, he worked for Yunnan State-owned Assets Operation Co., Ltd. His tenure of appointment expired on 31st October 2011.
25. **Xiang Rong**, male, born in April 1965, holding a bachelor degree. He is currently the secretary to the Committee of CPC and director of the Committee of CPC Affairs Department. During August 2003 to May 2005, Mr. Xiang was a member of the Committee of the CPC of Kunming Kunji Group, integrated office manager, and the director of the Committee of CPC Affairs Department. During May 2005 to December 2007, Mr. Xiang was a member of the Committee of the CPC of Kunming Kunji Group, chairman of the Union and the manager of the integrated office. On 31st October 2008, he was appointed as the supervisor of the Company elected by the staff. His tenure of appointment expired on 31st October 2011.
26. **Gao Xingang**, male, born in 1970, holding a bachelor degree and is a senior accountant. He graduated from Dongbei University of Finance & Economics majoring in accounting in 1990. Starting from 1994, he had been the accountant of Liaoning Trust and Investment Company and the head of the Financial Department of an enterprise under Liaoning Trust and Investment Company. Since 2004, he had been the associate director of the Financial Department of Shenyang Machine Tool (Group) Co., Ltd., head of the Financial Department and chief financial officer of the Whole Machine Business Department of Shenyang Machine Tool Co., Ltd. Since June 2008, he has been the director of the Internal Audit Department of Shenyang Machine Tool (Group) Co., Ltd. His tenure of appointment expired on 18th March 2011.

# DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

## II. POSITIONS IN SHAREHOLDER'S BUSINESS UNIT

Name	Shareholder's business unit	Position	Remuneration and allowances received
Li Zhenxiong	Yunnan Industrial Investment Holding Group Co., Ltd.	General manager assistant	Yes
Guan Xin	Shenyang Machine Tool. (Group) Co., Ltd.	Vice general manager	Yes
Zhang Tao	Yunnan Industrial Investment Holding Group Co., Ltd.	Vice manager of Investment Department	Yes
Fan Hong	Yunnan Equity Exchange Co. Ltd.	Chairman	Yes
Tang Hua	Shenyang Machine Tool. (Group) Co., Ltd.	Chairman of the Union	Yes
Cai Zheming	Shenyang Machine Tool. (Group) Co., Ltd.	Head of the Strategy Planning department	Yes

### Positions in Other Companies

Name	Other companies	Position	Remuneration and allowances received
Gao Minghui	Shenyang Machine Tool (Group) Kunming Co., Ltd.	Chairman	Yes
Zhang Xiaoyi	Yunnan CY Group Co., Ltd.	Chairman	Yes
	Xi'an Ser Turbo Machinery Manufacturing Co., Ltd.	Vice chairman	Yes
	TOS Kunming Machine Tool Manufacturing Co., Ltd.	Vice chairman	Yes
Ye Nong	TOS Kunming Machine Tool Manufacturing Co., Ltd.	Director	Yes
Pi Jianguo	Xi'an Ser Turbo Machinery Manufacturing Co., Ltd.	Director	Yes
	Fujian Kunji Conventional Machine Tool Co., Ltd.	Director	Yes
Wang Xing	Yunnan CY Group Co., Ltd.	Vice general manager	Yes
	Shenyang Machine Tool (Group) Kunming Limited	Vice general manager	Yes
	Xi'an Ser Turbo Machinery Manufacturing Co., Ltd.	Director	Yes
Wayne Yu	Kunming Kunji General Machine Co., Ltd.	Chairman	No
	Faculty of Finance at Hong Kong Polytechnic University	Professor, CFA	Yes
Liu Minghui	Dalian Newspaper Group	Vice president	Yes
	Dalian Publisher	President	Yes
Chen Ying	Yunnan Transformer Co., Ltd.	Vice chairman	Yes
Li Dongru	China Machinery Industry Federation	Vice secretary-general	Yes
Chen Fusheng	"International Accounting Research Journal" of the Accounting Department of the Faculty of Business at the Hong Kong University of Science and Technology	Associate professor Editor	Yes
Zhou Guoxing	TOS Kunming Machine Tool Manufacturing Co., Ltd.	Member of controlling committee	Yes
	Fujian Kunji Conventional Machine Tool Co., Ltd.	Chairman	Yes
Zhu Xiang	Kunming Kunji General Machine Co., Ltd.	Director and general manager	Yes
	Xi'an Ser Turbo Machinery Manufacturing Co., Ltd.	Director	Yes
	Xi'an Ruite Laser Prototyping Manufacturing & Engineering Research Co., Ltd.	Director	Yes
Luo Tao	Xi'an Ruite Laser Prototyping Manufacturing & Engineering Research Co., Ltd.	Director	Yes

## DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

### III. EMOLUMENTS OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

#### 1. The procedures for the determination of directors, supervisors and senior management's emoluments

The emoluments of directors and supervisors of the Company will be considered and approved at the shareholders' meeting; the emoluments of senior management officers are determined based on the terms of reference of the senior management officers in accordance with the remuneration policies formulated by the Remuneration and Assessment Committee of the Company, and assessed with reference to the profit indicators, operating indicators and business development indicators accomplished by the senior management officers for the year, and the improvement in quality of the assets of the Company. The results of the performance assessment results for the year, together with rewards and penalties proposed by the Remuneration and Assessment Committee, will be implemented with the approval from the Board.

#### 2. Basis for emoluments of directors, supervisors and senior management officers

- (1) general information of the emoluments of domestic directors and supervisors;
- (2) general information of the emoluments of Hong Kong directors and supervisors;
- (3) emoluments of senior management officers are based on the domestic industry practice and emoluments of the comparable listed companies in the region;

### IV. CHANGE OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

Name	Position	Change	Reason for the change
Chen Fusheng	Independent non-executive director	New appointment	
Xiao Jianming	Independent non-executive director	New appointment	
Li Shunzhen	Executive director, Financial controller	New appointment	
Qin Jianzhong	Supervisor elected by staff	Election	
Wayne Yu	Independent non-executive director	Resignation	Expiration of the independent term of office
Chen Ying	Independent non-executive director	Resignation	Expiration of the term of office
Pi Jianguo	Executive director, Financial controller	Resignation	Expiration of the term of office
Xiang Rong	Supervisor elected by staff	Resignation	Expiration of the term of office
Gao Xingang	Supervisor	Resignation	Job reallocation

# DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS

## V. COMPANY STAFF

No. of existing staff 2490

### Areas of specialization

Areas of specialization	Number of Employees
Of which: Production worker	1558
Skilled technician	403
Sales and marketing	58
Finance	56
Management	155
General services	28
Early retirement	171
Staff pending for duties	59
Others	2

### Education level

Education level	Number of Employees
Qualifications	Numbers
Of which: Postgraduate	21
University graduate	410
College diploma	411
Diploma	361
High school or vocational school	420
Junior high school or below	867
Title	
Of which: Senior	64
Intermediate	127
Junior	268

# CORPORATE GOVERNANCE STRUCTURE

## I. CORPORATE GOVERNANCE

The Company strictly complies with the "Company Law", the "Securities Laws", relevant laws and regulations issued by the CSRC and the Listing Rules of Shanghai Securities Exchange to establish a modern enterprise system, continuously improve its corporate governance and regulate the operations of the Company. Various systems of the Company are substantially in compliance with the requirements of the "Corporate Governance Standards of Listed Company" promulgated by the CSRC and the State Economic and Trade Commission. The Company will continue to improve and strengthen the internal control system in the course of ordinary operation so as to strive for the highest standards of corporate governance.

## II. INDEPENDENT DIRECTORS AND THEIR DUTIES

### 1. Attendance of Independent Directors at the Board Meetings

Please refer to the board meetings for the year and attendance for details

### 2. Objections raised by Independent Directors

During the reporting period, there were no objections raised by independent directors at the board meetings and other non-board meetings for the year.

## III. SEGREGATION OF THE COMPANY AND THE COMPANY'S CONTROLLING SHAREHOLDER ON THE OPERATIONS, PERSONNEL, ASSETS, STRUCTURE AND FINANCE

Operations	The Company has established an independent and complete system of procurement, production and sales such that its operations are independent and complete with its own operating capacity.
Personnel	The human resources and payroll management of the Company are completely independent of the controlling shareholder. No emoluments are received by the operating personnel of the Company from the shareholders' business unit or other business unit.
Assets	The Company and the controlling shareholder have clearly defined rights to the assets where the assets of the Company are completely independent of the controlling shareholder with legal person property rights.
Organizational structure	The organizational structure of the Company is independent of the controlling shareholder where the Company and the controlling shareholder do not share the same line function.
Finance	The Company has established an independent system for accounting and finance management with separate bank accounts.

# CORPORATE GOVERNANCE STRUCTURE

## IV. THE ESTABLISHMENT AND IMPROVEMENT OF THE COMPANY'S INTERNAL CONTROL SYSTEM

### **General plan for the establishment of internal control system**

In accordance with the regulatory requirements on the listed companies under the Company Law, the Securities Law, the Listing Rules of Shanghai Securities Exchange and the Internal Control Guidelines of the Shanghai Securities Exchange on Listed Companies, Supplementary Guidelines of Corporate Internal Control and Internal Control Guidelines for Companies Listed in the Shanghai Stock Exchange, the Company has established and formulated the Documents of Internal Control System and put in place a sound and effective internal control system. In establishing and implementing the internal control system, the Company has taken into the fundamental factors as follows: objective setting; internal environment; risk assessment; regulatory activities; information & communication; internal supervision. Based on the fundamental system, the Company's internal control system involves the formulation of corporate governance structure, rules of procedures, organizational structure and terms of reference of each department, fundamental management system, duties, workflow procedures and quality manual, covering all aspects from daily and usual production, operation and management. The internal control system is comprehensive with well-defined structure.

### **Establishment of a sound work plan in the internal control system and its implementation**

The Company has conducted tests and assessments on the present status of the internal control. Based on the features of the corporate structure and business procedures, the Company can also identify the major risks of internal control and set up objectives of internal control, rationalize internal procedures, spot defects and make improvement. The Company has outlined the annual work plan based on the key issues and accomplished them. Currently, the Company continues to make rectification to strive for excellence.

### **Establishment of the inspection and supervision department for internal control**

The Board office of the Company is the daily operation office of the Audit Committee. In addition, the Company has also established the audit department, which is responsible for special audit work on the Company; and assessment and random inspection of the implementation of the internal control system.

### **Internal supervision and self-assessment on internal control**

The Articles of Association of the Company sets out the provisions on internal audit and the Implementation Rules of Audit Committee and Internal Audit System are formulated. The internal audit department will conduct special audit work on the Company. In the fourth quarter of 2011, the audit department commenced self assessment for internal control system.

### **The Board's work arrangement on internal control**

The Board of the Company reviews the internal control assessment report and makes advice for improvement. The Company has also engaged an audit firm to make assessment on the internal control in respect of financial reports of the Company.

### **Improvement of internal control system associated with financial audit**

In accordance with the relevant laws and regulations under the Accounting Law, the General Rules Governing Enterprise Financial Affairs and Accounting Standards for Business Enterprise, the Company has established an accounting and audit mechanism and set up a more reasonable and regulated audit system through ERP instruments. The Company has complied with the relevant financial management requirements and formulated the relevant systems, which set out strict requirements on internal control procedures relating to finance, and the system has been put in place effectively.



## CORPORATE GOVERNANCE STRUCTURE

### V. DISCLOSURE OF THE BOARD'S SELF-ASSESSMENT REPORT AND THE AUDIT OPINIONS OF THE AUDITOR ON THE COMPANY'S INTERNAL CONTROL

#### 1. The Company disclosed the Board's self-assessment report on the Company's internal control.

The Board of the Company conducted the self-assessment on the internal control during 2011 and no material defects were discovered in terms of the design or implementation of the internal system. As of 31st December 2011, the Company maintained effective internal control in all material aspects pursuant to the "Basic Standard for Enterprise Internal Control" and relevant requirements. (See the Appendix to the Annual Report published on the website of the Company ([www.kmtcl.com.cn](http://www.kmtcl.com.cn)) and the website of Shanghai Stock Exchange ([www.sse.com.cn](http://www.sse.com.cn)) on 30th March 2012 for details).

#### 2. The auditor issued the audit opinions on the internal controls in respect of financial reporting of the Company.

The Company engaged the auditor to audit the effectiveness of internal control in relation to the financial reporting as at 31st December 2011, and the auditor has issued the audit report on the internal controls in relation to the financial reporting according to the requirements. (See the appendix to the annual report published on the website of the Company ([www.kmtcl.com.cn](http://www.kmtcl.com.cn)) and the website of Shanghai Stock Exchange ([www.sse.com.cn](http://www.sse.com.cn)) on 30th March 2012 for details).

### VI. ASSESSMENT OF THE SENIOR MANAGEMENT OFFICERS AND REWARDS

The resolution on the determination of the remuneration of the management for the year was considered and approved by the Remuneration and Assessment Committee of the Company with reference to the accomplishment of the profit indicators and other operation indicators for the year, pursuant to which the remuneration of senior management for 2011 was reduced by 7.75%.

### VII. THE COMPANY DISCLOSED THE REPORT ON SOCIAL RESPONSIBILITIES

(See the report on social responsibilities of the Company published on the website of the Company ([www.kmtcl.com.cn](http://www.kmtcl.com.cn)) and the website of Shanghai Stock Exchange ([www.sse.com.cn](http://www.sse.com.cn)) on 30 March 2012 for details).

### VIII. ESTABLISHMENT OF ACCOUNTABILITY SYSTEM FOR MATERIAL ERRORS IN ANNUAL REPORT INFORMATION DISCLOSURE

The Company has formulated the Measures on the Accountability for Material Errors in Annual Report Information Disclosure, which set out the provisions on the accountability subject, procedures, conditions and types. The implementation of such measures can enhance the level of annual report information disclosures and the quality of the Company's information disclosure.

# CORPORATE GOVERNANCE REPORT

## 1. CORPORATE GOVERNANCE PRACTICE

The Company complies with the relevant provisions as set out in the “Code on Corporate Governance Practices” (“Code”) of the Appendix 14 to the Listing Rules of the Stock Exchange of Hong Kong Limited and strives to improve its level of corporate governance. The implementation of the provisions as set out in the Code is as follow:

### A. Directors

#### A.1 Board Meetings

The Company holds at least one board meeting each quarter. 16 board meetings were held during 2011 and 13 of them were in written resolutions, please refer to page 28 for details of directors’ attendance. The secretary to the Board would consult each director for discussion issues and include them in the agenda for every board meeting to be held. During the reporting period, the notice and preliminary agenda were distributed to the directors at least 14 days before the date of meeting.

All directors keep close contact with the Company Secretary. The Company Secretary is responsible for ensuring that the compliance of the operations of Board with the procedures and advising on the corporate governance and compliance issues. The minutes of the board meetings are compiled and kept by the Company Secretary. Minutes are passed to each director for reference within a reasonable period after the meeting. Directors may seek for professional advice at the cost of the Company.

If a substantial shareholder or a director has a conflict of interest in respect of any material matters, a board meeting shall be held. The subject director shall abstain from voting and be excluded from the quorum of the meeting.

#### A.2 Chairman and Chief Executive Officer

The positions of Chairman and Chief Executive Office were held by Mr. Wang Xing and Mr. Zhang Xiaoyi respectively.

#### A.3 Composition of the Board

The Company discloses the composition of members of Board in its communications by the director category including Chairman, Executive Directors, Independent Non-Executive Directors and Non-Executive Directors. The Board currently comprises 4 independent non-executive directors, representing 1/3 of the total number of directors. During 2011, 4 directors took up the role of management, representing more than 1/3 of the total number of directors. This enabled the Board to strictly review and monitor the management procedures of the Company. In order to enrich the shareholders’ understanding of the directors and the composition of the Board of the Company, the Company has published the role of directors and their responsibilities in related media.

#### A.4 Appointment, Election and Removal

The directors of the Company (including non-executive directors) have specific term of appointment. According to the Articles of Association, directors are elected at shareholders’ meeting for a term of three years, subject to re-election upon expiry. However, the term of appointment for independent directors shall not exceed 6 years. The appointment of all directors of the Company shall be approved by the shareholders.

#### A.5 Directors’ Responsibilities

In order to ensure the directors’ sufficient understanding of the operations and businesses of the Company, each newly appointed director is given a comprehensive induction materials kit upon appointment. This kit sets out the business profile of the Company, responsibilities and obligations of directors and other legal requirements. Apart from that, each non-executive director will receive strategic proposals, business reports, and economics activities analysis regularly in order to execute their functions effectively (including making independent recommendations at board meetings). The non-executive directors shall give directions in the event of any potential interest conflicts; act as members of the committees under the Board; and carefully assess the performance of the issuer.

The Company Secretary is responsible for ensuring that all directors receive the latest updates on the Listing Rules and other statutory requirements.

# CORPORATE GOVERNANCE REPORT

## A.6 *Provision and Usage of Information*

In order to ensure that obligations are duly performed and informed decision are made by the directors of the Company, the agenda and relevant documents of the board meetings are distributed to all directors within ten days before the date of the meeting. The directors may meet the senior management officers formally or informally before the board meetings. The directors and committee members may review the relevant documents and minutes of the board meetings.

## B.1 **Remuneration of Director and Senior Management Officers**

Since the establishment of Remuneration and Assessment Committee of the Company, the remuneration and assessment of directors, supervisors and senior management officers are based on the rules of procedure of such committee. Independent professional advice may be sought if necessary in accordance with the stated procedures at the cost of the Company.

## C. **Accountability and Auditing**

### C.1 *Financial Reporting*

The directors would regularly receive integrated reports including strategic proposals, latest updates on various operations, financial objectives, plans and measures from the management. In the annual or interim report, or other announcements regarding price sensitive information and other discloseable financial information, the Board would make a balanced, clear and reasonable review for the Company's state of affairs and prospects.

### C.2 *Internal Control*

The Supervisory Committee of the Company exercises its supervisory rights independently in accordance with laws and regulations to safeguard the legal rights of shareholders, the Company and employees. The number of members and composition of the Supervisory Committee shall comply with the laws and regulations. During 2011, 3 meetings were held and full attendances were recorded in every meeting where the supervisors supervised on behalf of the shareholders the financial conditions of the Company and the performance of obligations of directors and senior management officers and their compliance, and sat in on the board meetings to perform the duties of the Supervisory Committee in a diligent manner.

The Board is responsible for the establishment and maintenance the internal control system of the Company for reviewing the financial, operational and supervisory control procedures so as to safeguard the interests of the shareholders and the assets of the Company. The Board may delegate the authority to the management for implementation of the internal control system. The Audit Committee is responsible for reviewing its effectiveness.

The Internal Audit Department regularly conducts inspection, supervision and assessment on the risks relating to and the importance of various businesses and procedures and when necessary. In addition, corresponding internal management system and procedures are established for monitoring, operation, construction, finance and administration. Inspection will be carried out on a random basis.

### C.3 *Audit Committee*

Since its establishment, the Audit Committee has functioned its important role of improving the financial reporting and the transparency of financial arrangement. The Company attaches great attention to the documentation of minutes of the Audit Committee. The minutes draft is prepared by a designated person and will be delivered to the members of the committee within a reasonable period. The draft is prepared for collecting the comments from the members and will be kept as minutes once finalized.

# CORPORATE GOVERNANCE REPORT

## **D. Transfer of Right of the Board**

### *D.1 Management Function*

The Board and the management of the Company both have clearly defined terms of reference and their respective functions are set out in the Articles of Association.

### *D.2 Committees under the Board*

The Strategic Committee, Audit Committee, Nomination Committee, Remuneration and Assessment Committee of the Company are established under the board of directors with respective terms of reference. Each committee performed its duties separately during the reporting period.

## **E. Communication with Shareholders**

### *E.1 Effective Communication*

The Board endeavors to maintain communications with its shareholders. During the Annual General Meeting in 2010, all Executive Directors, and part of the Non-Executive Directors and senior management officers attended the meeting to communicate with its shareholders.

### *E.2 Voting by poll*

Shareholders are informed regularly of the procedures of voting by poll. The procedures of voting by poll are set out in the notice of annual general meeting and circular. Relevant procedures will be also explained at the annual general meeting.

## **2. SECURITIES TRANSACTION OF DIRECTORS**

During the reporting period, the Company adopted the "Model Code for Securities Transactions by Directors of Listed Issuers" ("Model Code") of the Appendix 10 to the Listing Rules of the Stock Exchange of Hong Kong Limited as regulation for securities transaction of directors. The directors and supervisors of the Company complied with the Model Code and standards on securities transaction of directors as stated in its code of conduct during the reporting period.

## **3. BOARD OF DIRECTORS**

### **(1) Composition of the Board**

Currently, there are 12 directors in the Company and 4 of them are independent non-executive directors. This is the seventh session of Board of Directors since the establishment of the Company. The term of directors begins from 1 November, 2011 or the date of appointment to the date of next election of directors.

## CORPORATE GOVERNANCE REPORT

16 board meetings (13 of them were in written resolutions) were held during the year and members of the board meetings are as follows:

Name	Position	Required attendance	Attended in person	Attended via electronic communication	Attended by representative	Absence	Failed to be present at two meetings in a row
Wang Xing	Chairman and executive director	16	3	13	0	0	No
Li Zhenxiong	Vice chairman and non-executive director	16	3	13	0	0	No
Zhang Xiaoyi	Vice chairman and executive director	16	3	13	0	0	No
Guan Xin	Non-executive director	16	2	13	1	0	No
Gao Minghui	Non-executive director	16	2	13	1	0	No
Ye Nong	Executive director	16	3	13	0	0	No
Pi Jianguo	Executive director	14	2	12	0	0	No
Li Shunzhen	Executive director	2	2	0	0	0	No
Zhang Tao	Non-executive director	16	2	13	1	0	No
Liu Minghui	Independent non-executive director	16	3	13	0	0	No
Li Dongru	Independent non-executive director	16	2	13	1	0	No
Chen Fusheng	Independent non-executive director	8	2	5	1	0	No
Xiao Jianming	Independent non-executive director	3	1	1	1	0	No
Wayne Yu	Independent non-executive director	8	3	5	0	0	No
Chen Ying	Independent non-executive director	13	2	10	1	0	No

No. of board meetings held during 2011	16
Including: No. of meetings held on-site	3
No. of meetings held via electronic communication	13
No. of meetings held on-site with electronic communication	0

During the reporting period, the directors attended substantially all the board meetings. Representatives were appointed to attend the board meetings and express opinions on the behalf of directors if the directors were unable to attend the board meetings due to office duties.

In addition, according to the Article of Association, notice of a regular board meeting shall be given to all directors at least 10 days before the board meeting. In the course of practical operations, the Company complied with the requirements under the Appendix 14A.1.3 to the Listing Rules of the Stock Exchange of Hong Kong Limited where all notices of the regular board meetings were despatched 14 days before the board meetings.

The secretary to the Board is responsible for distributing the details of the regular board meetings (including the information of the committees under the Board) to the directors no later than 5 days before the date of meetings to ensure that all directors understand the issues to be considered at the meetings.

Details of any temporary board meetings held based on the needs of the management of the Company in the form of communication shall be despatched to all directors by means of e-mail and facsimile, and shall allow sufficient time for directors' consideration. The secretary to the Board shall respond to the directors' queries in a timely manner and take proper actions to assist the directors to ensure compliance with the requirements such as the Company Law, Articles of Association and Listing Rules.

Minutes of the board meetings shall be signed by the directors and the minutes-taker attending the meetings, and maintained over a long period of time for inspection by the directors if necessary.

Where the directors consider that material conflicts of interests arise in respect of the connected transactions discussed, the directors involved shall take measures of side-stepping and abstain from voting in respect of such matters.

# CORPORATE GOVERNANCE REPORT

## (2) Appointment of Directors

Each director of the Company is elected for a term of three years, subject to re-election upon expiry. The term of appointment of the independent non-executive directors shall not exceed six years. The Company shall enter into a Directors' Service Contract with the directors for a term of three years where the term of appointment of any additional directors during the term is less than three years. The appointment or removal of directors shall be approved at the shareholders' meeting. The appointment or removal of directors during 2011 is set out in "Change of Directors, Supervisors and Senior Management Officers" on page 20 of the Annual Report.

## (3) Duties of the Board

The duties and responsibilities of the Board are clearly defined and set out in the Articles of Association of the Company.

Details of the work of the board and its board committees are set out in "ORDINARY OPERATIONS OF THE BOARD" on page 42.

## (4) Qualifications and Independence of Independent Directors

Members of independent board committee have different professional backgrounds. They have professional expertise, sound qualifications and extensive experience in the areas of corporate management, financial accounting and manufacturing of machine tools.

The independent non-executive directors are independent of the Company pursuant to the guidelines on independence as set out in Rule 3.13 of the Listing Rules.

## (5) Implementation of Measures for Ensuring the Performance of Directors' Responsibilities

The secretary to the Board shall give all the directors relevant materials and updates on the statutory, regulatory and other ongoing responsibilities that the directors of the listed companies shall comply in a timely manner to ensure thorough understanding of their responsibilities, consistent execution of the procedures of the Board and proper compliance with applicable laws and regulations. The Board of the Company is entitled to engage independent professional bodies for such duties based on its power of authority for the performance of its responsibilities or business needs at the reasonable expense of the Company.

## (6) Relationship between the Members of the Board

There is no relationship between the members of the Board, particularly between the chairman and the general manager, in terms of finance, business, family and others.

## 4. CHAIRMAN AND GENERAL MANAGER

The roles of chairman and general manager shall not be taken by the same person with clearly segregated duties. The chairman is responsible for the management of the affairs of the Board such as inspecting the implementation progress of the issues approved by the Board. The general manager is responsible for management of operations of the Company and implementation of strategies formulated by the Board. The duties and responsibilities of the general manager are clearly defined and set out in the Articles of Association of the Company.

## 5. TERM OF NON-EXECUTIVE DIRECTORS: According to the Articles of Association, Rules of Procedure for the General Meetings of the Shareholders, and Rules of Procedure for the Meetings of the Board of Directors, the term of the non-executive directors under the 7th session of the Board will expire on 31st October 2014.

# CORPORATE GOVERNANCE REPORT

## 6. STRATEGIC COMMITTEE, AUDIT COMMITTEE, NOMINATION COMMITTEE AND REMUNERATION AND ASSESSMENT COMMITTEE ARE UNDER THE BOARD OF DIRECTORS. DETAILS ARE AS FOLLOWS:

No.	Committee under the Board of directors	Major responsibilities	Chairman	Committee members	Annual meeting and work details
1.	Strategic Committee	Conducting research and providing suggestions on the Company's strategic planning, significant investment and financing issues, significant usage of capital and asset utilization	Wang Xing	Wang Xing, Gao Minghui, Li Zhenxiong, Zhang Xiaoyi, Li Dongru and Xiao Jianming	Conducted research and analysis on the changes in the machine tool market and on the product mix adjustment
2.	Audit Committee	Issuing work reports based on regularly reporting, annual performance results and implementation of the internal control system	Liu Minghui	Liu Minghui, Chen Fusheng and Guan Xin	Convened special auditing meetings for annual report, interim report and internal control system
3.	Nomination Committee	Formulating policies for directors' nomination including nomination procedures, handling steps and criteria for selection of director candidates	Liu Minghui	Liu Minghui, Xiao Jianming and Zhang Tao	Reviewed and nominated senior management officers for appointment or removal for the year
4.	Remuneration and Assessment Committee	Formulating remuneration policy for executive directors, assessing performance of executive directors and approving clauses in executive directors' service contract	Xiao Jianming	Xiao Jianming, Chen Fusheng and Gao Minghui	Formulated assessment and appraisal system based on operational objectives

Notes: The chairman of the Company's Strategic Committee is Mr. Wang Xing, Chairman and executive director;

The chairman of the Company's Audit Committee is Mr. Liu Minghui, independent non-executive director;

The chairman of the Company's Nomination Committee is Mr. Liu Minghui, independent non-executive director;

The chairman of the Company's Remuneration and Assessment Committee is Mr. Xiao Jianming, independent non-executive director.

## 7. DIRECTORS' AND SUPERVISORS' SERVICE CONTRACTS

None of the Directors or Supervisors has entered into any service contract which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

## 8. DIRECTORS' AND SUPERVISORS' INTERESTS IN CONTRACTS

In 2011, none of the Directors or Supervisors had a material interest in the contracts entered into with the Company, its controlling company or subsidiaries of its controlling company.

# CORPORATE GOVERNANCE REPORT

## 9. AUDITOR'S FEE

The auditor's fee for the audit on financial statements and internal control for 2011 included the following:

Name of the accounting firm: KPMG Huazhen

Amount: RMB2,700,000

The major factors for the basis of determination of the auditor's fee paid by the Company are as follows:

- (1) General remuneration offered for auditing service;
- (2) General work load on audit work for the previous accounting period;
- (3) General work load on audit work for the previous engagement.

## 10. RIGHTS OF SHAREHOLDERS

The Company maintains good communication with its shareholders. The major communication channels include the Annual General Meeting, website and email of the Company, office facsimile and telephone of the secretary to the Board to enable shareholders to express their opinions or exercise their rights.

## 11. RESPONSIBILITY FOR FINANCIAL STATEMENTS

The Directors are responsible for the preparation of accounts for each financial period which shall present a true and fair view of the state of affairs, results and cash flow of the Group during such period.

The duties of the external auditor of the Company, KPMG Huazhen, are set out in the annual report.



# SHAREHOLDERS' MEETING

## I. GENERAL MEETING

<b>Meeting session</b>	<b>AGM date</b>	<b>Publishing newspaper resolved for information disclosure</b>	<b>Publishing date resolved for information disclosure</b>
2010 annual general meeting	10th May 2011	China Securities Daily, Shanghai Securities News and Securities Times	11th May 2011
The first extraordinary general meeting of 2011	18th July 2011	China Securities Daily, Shanghai Securities News and Securities Times	19th July 2011
The second extraordinary general meeting of 2011	21st September 2011	China Securities Daily, Shanghai Securities News and Securities Times	22nd September 2011
The third extraordinary general meeting of 2011	31st October 2011	China Securities Daily, Shanghai Securities News and Securities Times	1st November 2011

# DIRECTORS' REPORT

## I. BUSINESS REVIEW DURING THE REPORTING PERIOD

### 1. Overview of Operations during the Reporting Period:

In 2011, the European sovereign debt crisis continued to spread. Although Chinese economic fundamentals remained positive, the overall macroeconomic situation got more complicated and market competition intensified. The Consumer Price Index (CPI) grew by 5.4% and the Producer's Price Index (PPI) increased by 6.0% over the year. As the inflationary pressures lessened, the Purchase Management Index (PMI) recovered to over 50% in December, making the Gross Domestic Product (GDP) grow by 9.2% over the year. The domestic machine tool industry in the year continued the rapid growth from 2010, albeit with a slowly dipping momentum since the second half of the year. Significant progress was made on industrial restructuring, and high-end machine tools targeting high-end users witnessed an undersupply. Alongside the accelerating product demand upgrading, the import volume hit another record high in contrast with a noticeable decrease in the demand for low-end domestic products. As international markets showed different degrees of recovery, the export of machine tool products from China to emerging markets gained a steady increase. According to the statistics from 214 key enterprises in China's machine tool industry for the period from January to December 2011, CNC products accounted for 55.4% of metal-cutting machine tools in terms of production value, and the production volume of metal-cutting machine tools and CNC metal-cutting machine tools posted a year-on-year increase of 14.3% and 17.6% respectively. The product homogeneous tendency and increasingly keen price competitions implied opportunities and challenges as well.

Addressing the complicated macroeconomic conditions and intensified market competition, Kunming Machine Tool experienced a "pull-back" pattern as most of peers did. However, under the proper leadership of the Board and the senior management, the business units firmly joined their efforts to secure smooth business operations of the Company as a whole. As such, the Company achieved record high in sales and production volume and attained progresses and breakthroughs in the following aspects:

(1) *Marketing:*

The Company pressed forward the marketing channel construction, stabilized and expanded the domestic market share and strived to explore emerging markets and overseas sales. With active innovations in new marketing modes, 10 flagship stores of sales alliance were jointly set up. By tapping on key industries and customers, the Company gained contracts of over RMB300,000,000 from Sany Heavy Industry again. Meanwhile, the Company improved its after-sale system and strengthened the after-sale service and team building to effectively uplift customer satisfaction.

(2) *Production:*

To restructure its development pattern and explore internal potential, the Company staged a series of reforms including resource integration, production process reengineering and system function improvements. A leapfrog growth in scale production was achieved, with production volume of horizontal boring machines exceeding 100 units per month. To make full use of external resources, the Company proactively supported and cultivated core outsourcing partners, and thus solved the production bottlenecks to meet market demands.

(3) *Technology:*

The Company vigorously reinforced its technology innovation capability to step up product mix restructuring and upgrading. It undertook four major national special science and technology projects on technology of "high-end CNC machine tool and fundamental manufacturing machinery", participated in five major national special projects and one project under the "863 Program", and was responsible for five provincial science research projects. The Company expanded and perfected the gantry boring miller series and high performance machine tool components, which strengthened its competitiveness in the main engine market. Attaching importance to intellectual property, the Company has 16 patents on hand. Furthermore, it has successfully applied for the certification of national enterprise technology center.

## DIRECTORS' REPORT

(4) *Quality Control:*

The Company initiated a "quality control storm", organizing company-wide brainstorms on quality by reference to typical case of quality fault. Placing great emphasis on product quality and operational performance, the Company promoted precision manufacturing and lean production to consolidate product quality in full swing, hence obtaining the national mechanical industry award.

(5) *Technological Renovation:*

The Company pressed ahead with technological renovation and construction of production bases in a proactive and prudent manner according to its strategic development and product mix restructuring plans.

(6) *Financial and Human Resource Management:*

With a focus on re-establishing the product costs accounting and financial accounting systems, the Company reinforced its internal control system and information technology system to upgrade full-scope corporate management practices.

### 2. Major products accounting for 10% or above of the total operating income or gross profits of main operations

Sub-business or sub-product	Operating income	Operating expenses	Operating margin	Unit: RMB		
				Percentage change in operating income	Percentage change in operating expenses	Percentage change in operating margin
Sales and processing of machine tool products	1,543,019,054.78	1,142,044,017.59	25.99%	13.83%	18.50%	decreased by 2.91 percentage points
Sales, installation and technical services of highly efficient compressors	256,733,820.85	219,505,120.44	14.50%	27.86%	22.55%	increased by 3.71 percentage points

During the reporting period, the net profit decreased by 69.40%, and the gross profit margin decreased by 2.91 percentage points whilst the sales revenue increased over the same period last year, the decrease of the gross profit margin was due to:

- (1) The "pull-back" pattern of domestic market in the year led to further intensified market competition. During the first half year, general machine tools and small and medium CNC products saw robust demand, while large and heavy products still suffered from sluggish demand. In the second half of the year, market demand came into a downturn, and slumped especially in the fourth quarter. Due to the changes in demand structure, the Company recorded a growth in sales volume of digital display horizontal boring machine series with lower margin in the year, and a decrease in sales volume of high added value large floor-type boring machines year-on-year.
- (2) Wage costs in operating expenses increased year-on-year due to the higher labour costs.
- (3) The hiking prices of raw material including pig iron and scrap steel for castings of machine tools resulted in an average 20% increase in major material costs and a 13% increase in casting costs, leading to about 4% change in the costs of finished products.
- (4) In the fourth quarter, the significantly increased inventories due to slowdown in market demands, less orders and delayed delivery affected the Company's cash flows while increasing its finance costs.

## DIRECTORS' REPORT

### 3. Reasons for changes to the market of the principle business and the composition of its cost

Item	2011	Proportion (%)	2010	Unit: RMB'000	
				Proportion (%)	Increase/Decrease (%)
Raw materials	680,203.59	50.16	673,585.53	57.94	0.98
Direct labor costs	80,145.82	5.86	71,032.23	6.11	12.83
Benefit expenses	41,287.24	3.02	31,272.78	2.69	32.02
Fuel	2,825.36	0.21	0	0	–
Power	12,764.18	0.93	0	0	–
Manufacturing costs	264,431.89	18.87	250,182.27	21.52	5.70
Internal processing expenses	0	0	0	0	–
External processing expenses	286,718.03	20.95	136,484.19	11.74	110.07
Total	1,368,376.11	100.00	1,162,557.00	100	17.70

Analysis:

During the reporting period, the operating costs increased by RMB205,819,100 or 17.70% over the same period last year, the items experiencing large increase are external processing expenses, direct labor costs and benefit expenses, which were due to:

- (1) During the reporting period, the increase of machine tool production and the insufficient capacity of production led to many parts processing outsourced, which resulted in external processing charges increased RMB150,233,000 or 110% over that in the same period last year.
- (2) During the reporting period, the labour cost increased by RMB19,128,040 or 19% over that in the same period last year, as a result of increasing production and productive worker salary.

### 4. Analysis of sales of major products of the parent company:

Business segments or product	Turnover for 2011	Turnover for 2010	Unit: RMB'000	
			Increase/Decrease (%)	
Business segments				
General facilities production	546,268	574,708		(4.95)
Specified facilities production	735,246	545,100		34.88
Transportation facilities production	72,031	66,662		8.05
Electric mechanical equipment production	139,618	79,340		75.97
Other production	49,856	101,460		(50.86)
Products				
Horizontal boring and milling machines	590,131	562,723		4.87
Floor-type boring and milling machines	620,895	599,292		3.60
Table-type boring and milling machines	109,099	125,433		(13.02)
Horizontal products machining center	151,289	0		–
Gantry boring and milling machine tool	60,514	59,244		2.14
Others	11,091	20,576		(46.09)
Total	1,543,019	1,367,268		12.85

## DIRECTORS' REPORT

### 5. Major suppliers and customers

The total purchases from the top 5 suppliers for 2011 amounted to RMB237,476,000, representing 28.36% of the total purchase for the year. In particular, the largest supplier Siemens (German-based) accounted for RMB107,102,000 or 12.79% of the total purchases for the year.

The total sales revenue of the top 5 customers for 2011 amounted to RMB364,575,000, representing 20.21% of the total sales revenue for the year. In particular, the largest customer Sany Heavy Machinery Co., Ltd accounted for RMB152,673,000 or 8.46% of the total sales for the year. Shanxi Aowei Qianyuan Chemical Co., Ltd (陝西奧維乾元化工有限公司) accounted for RMB93,060,000 or 5.16% of the total sales for the year.

### 6. Analysis of the material changes in asset structure and proportion during the reporting period

Unit: RMB'000

Item	Closing balance	Opening balance	Amount Increase/Decrease	Increase/Decrease (%)
A Cash at bank and on hand	192,200.33	296,294.41	(104,094.08)	(35.13)
B Prepayments	79,699.34	53,337.72	26,361.62	49.42
C Inventories	983,679.39	752,776.01	230,903.38	30.67
D long-term deferred expenses	1,365.12	678.21	686.91	101.28
E Other non-current assets	79,737.13	0	79,737.13	–
F Short-term loans	100,000.00	46,000.00	54,000.00	117.39
G Bills payable	46,596.91	20,426.97	26,169.94	128.11
H Accounts payable	363,932.00	230,256.41	133,675.59	58.06
I Taxes payable	7,310.30	4,870.64	2,439.66	50.09
J Other payables	40,665.64	20,662.05	20,003.59	96.81
K Special payables	15,267.57	100.00	15,167.57	15,167.57
L Business tax and surcharges	8,024.32	1,558.29	6,466.04	414.95
M Impairment losses	62,921.70	1,356.47	61,565.23	4538.64
N Investment income	7,334.82	9,859.06	(2,524.24)	(25.60)
O Non-operating income	5,090.59	14,068.31	(8,977.72)	(63.82)
P Income tax expenses	16,568.49	27,397.12	(10,828.63)	(39.52)

Analysis:

- A. The decrease in cash at bank and on hand was due to a significant increase of construction project payment made by the Company for Yanglin Heavy Gear Base for the period.
- B. The increase in prepayments was due to the increase in prepayments paid to suppliers as a result of producing and purchasing imported parts.
- C. The increase in inventories was due to the increase in finished products as a result of shrinking market demand for machine tools in the fourth quarter.
- D. The increase in the long-term deferred expenses was due to the increase in the renovation expense for the manufacturing workshops.
- E. Other non-current assets represents the prepayments paid by the Company for the land use right and construction of Yanglin Heavy Gear Base.
- F. The increase in the short-term loans was due to the increase in the short-term loans borrowed by the Company from the bank to meet liquidity requirements.
- G. The increase in the bills payable was due to the increase in the use of the bills to settle the outstanding payables.

## DIRECTORS' REPORT

- H. The increase in the accounts payable was due to the increase in the amounts payables for raw material purchase as a result of increased output.
- I. The increase in the taxes payable was mainly due to the increase in the value-added tax payable.
- J. The increase in the other payables was mainly due to increase in the social security costs as a result of increasing bidding deposit for infrastructure projects.
- K. Special payable represents the tax refund as a result of receiving import tariff and import value-added tax for the key parts of machine tools.
- L. The increase in business tax and surcharges was due to the increase in city construction tax, education additional tax and local education additional tax.
- M. The impairment losses was due to the significant increase in the provision for bad debt and inventory impairment.
- N. The decrease in investment income was due to the decrease in the profit of TOS (a jointly controlled enterprise) over the same period last year.
- O. The decrease in non-operating income was due to the decrease in government grant and the reduction in tax refund due to the cancelation of tax refund policy for CNC machine tool.
- P. The decrease in the income tax expenses was due to the decrease in taxable income for this year.

### 7. Analysis of material changes in major financial data during the reporting period

Unit: RMB'000

Item	Closing balance	Opening balance (same period last year)	Amount Increase/Decrease	Increase/Decrease (%)
Total assets	2,558,664.36	2,247,730.36	310,934.00	13.83
Operating profit	65,619.42	188,947.21	(123,327.79)	(65.27)
Net profit attributable to the owners of the parent	54,567.13	178,324.80	(123,757.67)	(69.40)

Analysis:

The total assets increased by RMB310,934,000 over the same period last year mainly attributable to the fixed assets investment increase, for, example, the investment for Yanglin Heavy Gear Base and the purchase of equipment increased by RMB165,856,000. Moreover, the current assets in raw material and work-in-progress increased by RMB230,903,000.

## DIRECTORS' REPORT

The operating profit increased by RMB207,152,000 over the same period last year, the operating profit decreased by RMB123,327,790 or 65.27%, the net profit attributable to the owners of the parent decreased by RMB123,758,000 or 69.40%, which were due to:

- 1) By restructuring the product mix and increasing the input for new products to cope with the change of market needs, the new products like gantry milling machines were at the marketing stage, which reduced some profits as a result of the weak price advantage caused by high cost.
- 2) On account of the fierce competition, the Company altered the marketing strategy to reduce the sales price of the previous high value-added products, such as Floor-type boring and milling machines, which resulted in the decrease in the sales profit.
- 3) The sales profits decreased by 3 percentage points, being the key factor for decreased operating profit, mainly attributable to the rising price of raw materials, thus the basic material cost generally increased by about 20%, which made the cost of finished goods varied by about 4%.
- 4) During the reporting period, the provision for bad debt increased by RMB55,455,000 as a result of the increase of RMB90,572,000 in the accounts receivables. In addition, the provision for inventory impairment was increased by RMB4,537,000. Both of which made the profit reduced by RMB59,992,000 in total.
- 5) Non-operating income decreased by RMB8,978,000 over that in the same period last year, being the key factor for decreased profit for this year as well, mainly attributable to the impact of cancelled preferential tax policy for CNC machine tool tax refund.

### 8. Analysis of cash flow structure and its material changes, and reasons for net profit fluctuation during the reporting period:

*Unit: RMB'000*

Item	2011	2010	Amount Increase/Decrease	Increase/Decrease (%)
Net cash flow from operating activities	654.76	129,272.78	(128,618.02)	(99.49)
Net cash flow from investment activities	(162,814.72)	(69,581.90)	(93,232.82)	133.99
Net cash flow from financing activities	55,194.79	(48,136.52)	103,331.31	(214.66)

Analysis:

- 1) Net cash flow from operating activities decreased largely over that in the same period last year, which was mainly because of the shrinking market demand, decrease of orders, delayed delivery of goods since the fourth quarter of 2011. Inventory and goods in progress increased largely as the inventory increased by RMB235,440,000 as compared with the beginning of the period, resulting in the large decrease in net cash flow from operating activities.
- 2) Net cash flow from investment activities increased by RMB93,233,000 over that in the same period last year, mainly attributable to the increase in the payments for construction projects of Yanglin Heavy Gear Base.
- 3) Net cash flow from financing activities increased by RMB103,331,000 over that in the same period last year, mainly attributable to the increase in liquidity loans.

## DIRECTORS' REPORT

### 9. Discussion and analysis of important issues relating to the operations of the Company, including the utilization of the Company's facilities, securing of purchase orders, product sales or inventory turnover and changes in the profile of key technicians

The amount of new contracts for 2011 amounted to RMB1,927 million and 65.40% was attributable to CNC products. There was delay for the delivery of a few CNC machine tool products but no change in the profile of key technicians.

### 10. Review of operations and business analysis for major controlling companies and invested companies

*Unit: RMB'000*

Name	Nature of business	Major products or services	Registered capital	Total assets	Net profit
Xi'an Ser Turbo Machinery Manufacturing Co., Ltd.	Manufacturing	Energy saving compressor and turbo machines	50,000	398,345	(3,776)
Xi'an Ruite Laser Prototyping Manufacturing & Engineering Research Co., Ltd.	Manufacturing	Laser prototyping machine	60,000	131,077	(857)
Winko Machines Co., Ltd.	Manufacturing	Intelligent color display computerized embroidery machine and rotary table	20,230	0	9,860
TOS Kunming Machine Tool Manufacturing Co., Ltd.	Manufacturing	Development, design, production and sales of self-produced machine tool series products and accessories	5,000,000 Euros	185,522	15,070
Kunji Transportation Co., Ltd.	Transportation	General cargo transportation	500	0	(659)
Kunming Kunji General Machine Co., Ltd.	Manufacturing	Development, design and sales of machine tool products and accessories	3,000	35,632	2,697
Fujian Kunji Conventional Machine Tool Co., Ltd.	Manufacturing	Development, design, production and sales of self-produced machine tool series products and accessories	5,000	8,308	(1,232)



# DIRECTORS' REPORT

## II. OUTLOOK ON FUTURE DEVELOPMENT OF THE COMPANY

As China is to implement "the 12th Five-year Plan" comprehensively in 2012, it is expected that the mechanical industry will grow by 18-20% where domestic machine tool market will grow by 20%. The prudent fiscal policy should steer the domestic economy into an uptrend. However, the Company still faces a myriad of challenges, given the global machine tool giants taking new edges in China, product structure upgrading, fiercer market competition, ever-changing customer needs and the even mixed economic environment.

In the principle of "being the best instead of the largest, the Company will carry out its business strategy focusing on "uniqueness, brand, profitability" towards the targets of "large-scale, precise, complex and full-spectrum". In light of its unique product strategy with an aim at major performance indicators ranking top in China and leading in the world, the Company seeks to integrate precision into CNC products and excellence into general products. The Company will focus on the following seven aspects:

1. Seizing market share and orders is still the top priority of the Company. The Company will accelerate to build up the flagship stores and specialty stores, while implementing the product manager system to improve marketing and after-sales services. The annual sales target of 24 series gantry boring and milling machines is set at 100 sets.
2. The Company will refine the production and operation models, improve operating efficiency and make the castings and machine tool components a specialized, strong and large business arm. The streamline assembly model will be promoted for horizontal boiling machine products according to the requirements for definite time, location and quantity. Through intensive and lean production, the Company will seek to ensure the delivery cycle for key contract products and trim down the inventory of semi-processed products by 50%. Moreover, safe and civilized production and on-site management will be intensified.
3. The Company will strengthen the technological service and support to market function and production sites. While earnestly implementing the national key special projects, the Company will expedite the introduction of the SCHIESS technology, push ahead the process team building and management on standard processes, and upgrade the technological development capability and level.
4. The Company will deepen the "quality management storm", advocate innovations in quality management system and extend the quality-based reward and punishment mechanism to suppliers and collaborative manufacturers to enhance the supporting level.
5. The Company will take initiatives to promote corporate fundamental management centering on financial management, including the overall budget management and the ERP project as well as the comprehensive performance assessment, reforms in remuneration management methods and optimisation of human resources structure. At the same time, the Company expects to improve capital operations and broaden financing channels to shore up the product mix restructuring and technological renovations.
6. Taking all-around consideration of the development plans for machine tools and the existing production and operation conditions, the Company will actively and prudently expedite the construction progress of the heavy equipment plant and cast base projects.
7. Operating objective for 2012:

*Unit: RMB100 million*

Item	Operating income	Net Profit
		Attributable to the Parent Company
2011 operating results	18	0.54
2012 operating objectives	20	1.2

# DIRECTORS' REPORT

## III. INVESTING ACTIVITIES

### 1. Information of invested companies

Name	Place of registration	Scope of business	Registered capital RMB ten thousand	Investment Proportion	Nature	Date of investment	Relationship with the Company
Xi'an Ser Turbo Machinery Manufacturing Co., Ltd. ("Xi'an Ser")	Xi'an city	Design, development and sales of turbo machines, energy saving sintering fans, compressor equipment, research and re-modification of imported equipment and its parts, automated control system engineering, CNC engineering, mechanical and chemical equipment, meter technology development, whole machine production and sales	5,000	45.00%	Limited liability	2001.12	Subsidiary
Kunming Kunji General Machine Co., Ltd.	Kunming city	Development, design and sales of machine tool products and accessories	300	100.00%	Limited liability (wholly owned by legal person)	2007.10	Subsidiary
Winko Machines Co., Ltd. ("Winko")	Kunming city	Development, application and system integration of hardware and software; retail, wholesale and distribution of general machinery and electronic machines	2,023	96.74%	Limited liability	2002.11	Subsidiary
TOS Kunming Machine Tool Manufacturing Co., Ltd. ("TOS Kunming")	Kunming city	Development, design, production and sales of self-produced machine tool series products and accessories; development of high-tech products, transfer of self-developed technology, provision of technical services and technical advisory; provision of repairs and processing of machine tool products for third parties	5,000,000 Euros	50.00%	Limited liability	2005.4	jointly controlled enterprise
Changsha Ser Turbo Equipment Co., Ltd. ("Changsha Ser")	Changsha city	Production and sales of centrifugal compressors, centrifugal blowers, sintering fans and its accessories	1,000	100%	Limited liability	2004.01	Subsidiary of Xi'an Ser
Hangzhou Ser Gas Engineering Co., Ltd. ("Hangzhou Ser")	Hanzhou city	Contracting: design, development, sales and technology support of gas equipment engineering, compressors, sintering fans, whole sintering fan equipment, low-temperature machines, automated control system equipment and its parts; wholesale and retail: mechanical and electrical products, building materials, hardware tools, metal materials; operation of import/export businesses; all legally valid projects not subject to review and approval	120	51.00%	Limited liability	2004.04	Subsidiary of Xi'an Ser
Kunji Transportation Co., Ltd. ("Kunji Transportation")	Kunming city	General cargo transportation	50	100%	Limited liability	2006.10	Subsidiary
Xi'an Ruite Laser Prototyping Manufacturing & Engineering Research Co., Ltd. ("Xi'an Ruite")	Xi'an city	Laser prototyping machine	6,000	23.34%	Limited liability	2006	Associate
Fujian Kunji Conventional Machine Tool Co., Ltd.	Nanan city	Development, design, production and sales of self-produced machine tool series products and accessories	500	50.00%	Limited liability	2008	Subsidiary

# DIRECTORS' REPORT

## IV. RAISED FUND

### 1. Use of proceeds from raised fund

During the reporting period, there were no proceeds from new raised funds, nor any proceeds from previous raised funds being utilized for the year.

### 2. Use of proceeds from non-raised fund

During the reporting period, there were no proceeds from new raised funds, nor any proceeds from previous raised funds being utilized for the year.

## V. ORDINARY OPERATIONS OF THE BOARD

### 1. Board meeting and resolution

Session	Board meeting date	Resolution	Publishing newspaper	Publishing date
23rd meeting of the 6th session of the Board	7th January 2011	Approved the liquidation of Winko Machines Co., Ltd.		
24th meeting of the 6th session of the Board	30th January 2011	Approved the written resolution on the continuing connected transaction regarding the land and buildings between the Company and Kunming Kunji Group.	China Securities Daily, Shanghai Securities News and Securities Times	1st February 2011
25th meeting of the 6th session of the Board	18th February 2011	Approved the written resolution on the package of connected transactions between the Company and Kunming Kunji Group		
26th meeting of the 6th session of the Board	22nd March 2011	Annual Resolutions of the Board	China Securities Daily, Shanghai Securities News and Securities Times	23rd March 2011
27th meeting of the 6th session of the Board	20th April 2011	Approved the proposal of appointing KPMG Huazhen as the Company's auditor and internal control auditor for the year 2011	China Securities Daily, Shanghai Securities News and Securities Times	21st April 2011
28th meeting of the 6th session of the Board	28th April 2011	Approved the written resolutions on the "First Quarterly Report and Summary for 2011"	China Securities Daily, Shanghai Securities News and Securities Times	29th April 2011
29th meeting of the 6th session of the Board	27th May 2011	Approved the notice of general meeting regarding the conclusion of Transfer Agreement of Proprietary Technologies with German Shies (a related party)	China Securities Daily, Shanghai Securities News and Securities Times	27th May 2011

## DIRECTORS' REPORT

Session	Board meeting date	Resolution	Publishing newspaper	Publishing date
30th meeting of the 6th session of the Board	28th June 2011	Approved the written resolution on the supplementary resolution regarding the election of independent directors at the general meeting	China Securities Daily, Shanghai Securities News and Securities Times	29th June 2011
31st meeting of the 6th session of the Board	4th August 2011	Approved the written resolution on the ordinary continuing connected transactions between the Company and related parties and notice of general meeting	China Securities Daily, Shanghai Securities News and Securities Times	5th August 2011
32nd meeting of the 6th session of the Board	28th July 2011	Approved the written resolution on the resignation of the position of chairman and appointment of Mr. Wang Xing as the new chairman	China Securities Daily, Shanghai Securities News and Securities Times	29th July 2011
33rd meeting of the 6th session of the Board	22nd August 2011	Approved the "Interim Report and Summary for 2011"	China Securities Daily, Shanghai Securities News and Securities Times	23rd August 2011
34th meeting of the 6th session of the Board	14th September 2011	Approved the written resolutions on convening the third extraordinary general meeting	China Securities Daily, Shanghai Securities News and Securities Times	15th September 2011
35th meeting of the 6th session of the Board	17th October 2011	Approved the written resolutions on connected transactions between the Company and Kunming TOS (A jointly controlled enterprise) and foreign shareholders in 2011	China Securities Daily, Shanghai Securities News and Securities Times	18th October 2011
36th meeting of the 6th session of the Board	27th October 2011	Approved the written resolution on the "Third Quarterly Report and Summary for 2011"	China Securities Daily, Shanghai Securities News and Securities Times	28th October 2011
1st meeting of the 7th session of the Board	31st October 2011	The resolution regarding the election at the expiration of terms of office	China Securities Daily, Shanghai Securities News and Securities Times	1st November 2011
2nd meeting of the 7th session of the Board	18th November 2011	Approved the written resolution on the 2011 amendments to the articles of association of the Company	China Securities Daily, Shanghai Securities News and Securities Times	19th November 2011

## DIRECTORS' REPORT

### 2. Implementation of resolutions at the shareholders' meeting by the Board

During the reporting period, the Board exercised the rights granted to them at the shareholders' meeting in a sound manner and all resolutions at the shareholders' meeting were duly executed.

### 3. Overall reporting on the performance of duties of Audit Committee of the Board

(For details, please refer to the Work Summary of the Audit Committee for 2011 of the Company dated 30th March 2012 on the website of the Company ([www.kmtcl.com.cn](http://www.kmtcl.com.cn)) and the website of Shanghai Stock Exchange ([www.sse.com.cn](http://www.sse.com.cn)).

### 4. Overall reporting on the performance of duties of Remuneration and Assessment Committee of the Board

On 28th March 2011, the Remuneration and Assessment Committee under the Board held a meeting. Having diligently reviewed the remuneration of directors, supervisors, and senior management officers, the Remuneration and Assessment Committee of the Board considered that the remuneration of the senior management officers as disclosed in the annual report for 2011 was determined according to the implementation of the growth strategies and investment decisions as formulated by the Board and the completion of the operating objectives as framed by the Board.

### 5. Establishment and improvement of the system for the administration of external information users

The System of Shenji Group Kunming Machine Tool Company Limited for the Administration of External Information Users has been formulated and approved at the 15th meeting of the 6th session of the Board held on 24th March 2010. The system clearly regulates the approval, reporting and confidentiality in relation to the use of external information and has been effectively implemented by the Company.

### 6. Statement of directors' responsibilities on internal control

(See the self-assessment report on the internal control for 2011 of the Company published on the website of the Company ([www.kmtcl.com.cn](http://www.kmtcl.com.cn)) and the website of Shanghai Stock Exchange ([www.sse.com.cn](http://www.sse.com.cn)) on 30th March 2012 for details).

## VI. IMPLEMENTATION OF PROFIT DISTRIBUTION PLAN OF THE COMPANY DURING THE REPORTING PERIOD

### 1. Proposal on profit distribution of the company for the year of 2010

As proposed by the 6th session of the board of directors at its 26th meeting, the proposal on profit distribution of the Company for the year of 2010 was approved at the 2010 annual general meeting of the Company held on 10th May 2011. In accordance with the PRC accounting standards, in 2010, the Group recorded a net profit of RMB178,325,000. After deducting the transfer of RMB18,774,000 to surplus reserves, the distributable profit realized by the Group in 2010 was RMB159,551,000, and the accumulated profit available for distribution amounted to RMB706,716,000. In particular, the Company recorded a net profit of RMB187,738,000. After deducting the transfer of RMB18,774,000 to surplus reserves, the Company realized a net profit of RMB168,964,000 and accumulated profit available for distribution amounted to RMB653,918,000. In accordance with the Hong Kong Accounting Standards, the Group recorded a net profit of RMB178,370,000. After deducting the transfer of RMB18,774,000 to surplus reserves, the distributable profit realized for the year amounted to RMB159,596,000, and the accumulated profit available for distribution amounted to RMB704,975,000. In particular, the Parent recorded a net profit of RMB183,218,000. After deducting the transfer of RMB18,774,000 to surplus reserves, the realized distributable profit of the Company for the year amounted to RMB164,444,000 and accumulated profit available for distribution amounted to RMB629,343,000. Accordingly, the profit of the Company available for distribution for this year is under the PRC accounting standards amounted to RMB159,551,000.

## DIRECTORS' REPORT

Proposal on the distribution of cash dividends for the year of 2010: a cash bonus dividend of RMB0.5 (tax inclusive) is proposed for every 10 shares held by Shareholders of the Company based on the existing total share capital of 531,081,103 shares (including 390,186,291 A Shares and 140,894,812 H Shares), totaling RMB26,554,055.15 in cash. The actual cash dividend after tax to be distributed to the individual shareholders, investment fund and qualified overseas institutional investors for A Shares would be RMB0.45 for every 10 shares held. For other holders of A Shares who are nonresident enterprises, no withholding tax is deducted by the Company and such tax shall be paid by the shareholders of the relevant jurisdictions.

On 13th June 2011, the Company paid cash bonus dividend to holders of A Shares whose names appeared on the register of members of the Company on the record date (i.e. 3rd June 2011). The Shanghai Branch of China Securities Depository and Clearing Corp. Ltd. was entrusted by the Company to pay the cash dividend on its behalf to the holders of the A Shares without selling restrictions. With respect to the A Shares subject to selling restrictions, the cash dividend was directly paid to the holders of such shares.

Due to the recent change of PRC tax laws and regulations, the Circular on the Questions Concerning Tax on the Profits Earned by Enterprises with Foreign Investment, Foreign Enterprises and Individual Foreigners from the Transfer of Stocks (Stock Rights) and on Dividend Income (Guo Shui Fa [1993] No. 45) issued by the State Administration of Taxation (the "Circular") was repealed under the Announcement on the List of Fully and Partially Invalid and Repealed Tax Regulatory Documents dated 4th January 2011. Therefore, the Circular can no longer be the basis for the natural person holders who hold the Company's H shares and whose names appear on the register of members of H shares of the Company to be exempted from the individual income tax when the Company distributes the final dividends for the year ended 31st December 2010. Pursuant to the PRC Individual Income Tax Law, the Implementation Regulations of the Individual Income Tax Law, the Tentative Measures on Withholding and Payment of Individual Income Tax and other relevant laws and regulations, in view of opinions from relevant PRC tax authorities, the Natural Person Holders of H Shares shall pay individual income tax upon their receipt of distribution of dividends or bonus from the Company, which shall be withheld and paid by the Company on behalf of the Natural Person Holders of H Shares. Under the premise of the confirmation by the tax authority in accordance with the information provided by individual holders of H Shares of the Company, the individual holders of H Shares of the Company are entitled to the relevant preferential tax treatment pursuant to the provisions in the tax agreements (arrangements).

Because of the above matters, the date of distributing the dividends was adjusted from 20th July 2011 to 5th August 2011 or before, the Company paid final dividends to the holders of H Shares whose names appeared on the register of holders of H Shares of the Company on the record date (i.e. 8th April 2011). The final dividends payable to the holders of H Shares were denominated and declared in Renminbi and were paid in Hong Kong dollars. The exchange rate was HK\$100 to RMB83.626, which was based on the benchmark exchange rates for Hong Kong dollar to Renminbi as announced by the People's Bank of China for one calendar day prior to the date of approval for the payment of such dividends (i.e. 10th May 2011). The final dividend per H Share was HK\$0.05979 (including tax). ICBC (Asia) Trustee Company Limited was appointed by the Company as the receiving agent (the "Receiving Agent") in Hong Kong to receive the dividends on behalf of the holders of H Shares. The Company would pay the final dividends declared in respect of H Shares of the Company to the Receiving Agent, who would hold such dividends in trust on behalf of the relevant holders of H Shares until the payment is received.

Presently, the payment of dividend has been completed.

## DIRECTORS' REPORT

### VII. DISTRIBUTION OF CASH DIVIDENDS OF THE COMPANY FOR THE PRECEDING THREE YEARS (Unit: RMB'000)

Year	Distributable profits	Cash dividend amount	Cash dividend/distributable profit
2009	191,995	21,243	11%
2010	159,551	26,554	16.64%
2011	47,084	10,621	22.56%

Proposal on the distribution of cash dividends for the year of 2011 during the reporting period: a cash bonus dividend of RMB0.2 (tax inclusive) is proposed for every 10 shares held by Shareholders of the Company based on the existing total share capital of 531,081,103 shares (including 390,186,291 A shares and 140,894,812 H shares), totaling RMB10,621,622.06 in cash. The actual cash dividend after tax to be distributed would be RMB0.18 for every 10 shares held.

The cash dividends policy of the Company was proactively prepared and implemented in compliance with the Company's Articles of Association or resolutions of the general meeting. The definite and clear distribution standards and proportion, all-round decision process and mechanism and the due diligence of independent directors provide minority shareholders with opportunities to fully express opinions and appeals, thus fully safeguarding minority shareholders' legitimate rights and interests.

## DIRECTORS' REPORT

### VIII. CERTIFIED PUBLIC ACCOUNTANTS' STATEMENT ON THE SUMMARY OF THE COMPANY'S FUNDING TRANSACTIONS WITH THE CONTROLLING SHAREHOLDER AND OTHER RELATED PARTIES

#### **Statement on the Summary of Shenji Group Kunming Machine Tool Company Limited's Funding Transactions with the Controlling Shareholder and Other Related Parties for the Year Ended 31 December 2011**

##### **To the board of directors of Shenji Group Kunming Machine Tool Company Limited**

We have been engaged to audit the financial statements of Shenji Group Kunming Machine Tool Company Limited (the "Company") for the year ended 31 December 2011, which comprise the consolidated balance sheet and balance sheet as at 31 December 2011, the consolidated income statement and income statement, the consolidated cash flow statement and cash flow statement and consolidated statement of changes in shareholders' equity and statement of changes in shareholders' equity for the year then ended 31 December 2011, and notes to the financial statements according to China Standards on Auditing for the Certified Public Accountants. And we issued the unqualified audit opinion on 29 March 2012.

In accordance with the requirements as stated in the "Notice of Certain Issues Relating to Regulating Listed Companies' Transactions with Related Parties and the Guarantees Provided to Third Parties" (Zheng Jian Fa [2003] No. 56) as promulgated by the China Securities Regulatory Commission and State-owned Assets Supervision and Administration Commission of the State Council, the Company prepared the accompanying summary of the Company's funding transactions with the controlling shareholder and other related parties for the year ended 31 December 2011 (the "Summary").

It is the responsibility of the Company to prepare and disclose the Summary whilst ensure its authenticity, legitimacy and completeness. We have checked the stated amounts on the Summary to the accounting information the Company provided us when we were auditing the Company's financial statements for the year ended 31 December 2011 and the audited financial statements on a sample basis, and we were not aware of any discrepancies in material aspect.

To gain a better understanding of the Company's funding transactions with the controlling shareholder and other related parties for the year ended 31 December 2011, the Summary should be read in conjunction with the audited financial statements.

This statement is intended solely for the purpose of assisting the Company's disclosure of the annual report for the year ended 31 December 2011. This statement is not intended for any other purposes unless our written consent is obtained.

**KPMG Huazhen**

China, Beijing

*Certified Public Accountants*  
*Registered in the People's Republic of China*  
Peng Jing  
Zhong Dan  
29 March 2012

*Attachment:* Summary of Shenji Group Kunming Machine Tool Company Limited's Funding Transactions with the Controlling Shareholder and Other Related Parties for the Year Ended 31 December 2011



# DIRECTORS' REPORT

## Summary of Shenji Group Kunming Machine Tool Company Limited's Funding Transactions with the Controlling Shareholder and other Related Parties for the Year Ended 31 December 2011

Unit: RMB ten thousand

				Opening balance of funding transactions for 2011	Accumulated funding transactions incurred (exclusive of interests) for 2011	Interests of funding transactions for 2011 (if any)	Accumulated repayment incurred for 2011	Closing balance of funding transactions for 2011	Purpose of funding transactions	Nature of funding transactions	
<b>Non-operating funding transactions</b>											
Current controlling shareholder and its affiliates	None	N/A	N/A							N/A	N/A
	Sub-total	N/A	N/A							N/A	N/A
Former controlling shareholder and its affiliates	N/A	N/A	N/A							N/A	N/A
	Sub-total										
Total											
<b>Other related funding transactions</b>											
Controlling shareholder and its affiliates	Schiess GmbH Co., Ltd. ("Schiess GmbH") (note 1)	Affiliate of the controlling shareholder	Other non-current assets	-	1,824.66	-	-	1,824.66	Payment of technology license fee	Operating	
	Yunnan CY Group Electrical Products Trade Center	Subsidiary of affiliate of the controlling shareholder	Accounts receivable	0.90	97.73	-	97.73	0.90	Purchase of goods	Operating	
Company's subsidiaries and their respective affiliates	Kunming Kunji General Machine Co., Ltd. ("General Machine") (note 2)	Subsidiary	Dividends receivable	-	2,913.08	-	-	2,913.08	Dividend	Operating	
	Xi'an Ser Turbo Machinery Equipment Company Limited ("Xi'an Ser") (note 3)	Subsidiary	Dividends receivable Other receivables	1,540.89	157.15	58.41	-	1,756.45	Dividend and interest	Non-operating	
	Changsha Ser Turbo Machinery Equipment Company Limited	Subsidiary	Accounts receivable	24.40	-	-	-	24.40	Temporary payment	Non-operating	
	Fujian Kunji Conventional Machine Tool Co., Ltd.	Subsidiary	Accounts receivable Other receivables	542.51	20.47	-	-	562.98	Temporary payment	Non-operating	
	Kunji Transportation Company Limited	Subsidiary	Other receivables	1.80	-	-	1.80	-	Temporary payment	Non-operating	
	Winko Machines Co., Ltd	Subsidiary	Other receivables	283.36	-	-	283.36	-	Temporary payment	Non-operating	
Related natural persons	N/A	N/A	N/A						N/A	N/A	
Other related persons and their respective affiliates	Kunming TOS Machine Tool Company Limited ("Kunming TOS") (note 4)	jointly controlled enterprise	Accounts receivable Other receivables	686.59	1,022.53	-	1,007.52	701.60	Purchase of goods	Operating	
	Total				3,080.45	6,035.62	58.41	1,390.41	7,784.07		

## DIRECTORS' REPORT

*Note 1:* The first extraordinary general meeting for 2011 held on 18th July 2011 approved Shenji Group Kunming Machine Tool Company Limited ("the Company") and Schiess GmbH concluded Technologies License Contract, under which the Company introduced from Schiess GmbH the design, manufacture and installation technical know-how of the double column portals for cross rail profile of 2000 mm, and obtained exclusive and non-transferable license right to manufacture in China by using the technical know-how and sell the contract products in Asia. According to the terms and conditions of the Contract, the Company paid 30% of license fee (i.e. 1,980,000 Euros, which equivalent to RMB18,246,600) to Schiess GmbH as at August 2011 and have received partial technical information including design drawing, process and content of the first prototype machine. The amount was presented in balance sheet as other non-current asset as at 31st December 2011.

*Note 2:* General Machine held the board meeting on 31st December 2011, and approved to distribute cash dividends of RMB29,130,800 to the Company.

*Note 3:* Xi'an Ser has declared but has not paid dividends of RMB11,000,000 to the Company as at 31st December 2010 and 2011.

*Note 4:* The Company entered into the Normal Continuous Operating Framework Agreement 2011 for the sales of goods and provision of services with Kunming TOS in 2011. The agreement was effective from 31st October 2011 to 31st December 2011.

### IX. DETAILS OF AND INDEPENDENT OPINIONS ON THE EXTERNAL GUARANTEE OF THE COMPANY EXPRESSED BY THE INDEPENDENT DIRECTORS

For the details of and independent opinions on the external guarantee of the Company for 2011 expressed by the independent directors, we conducted a due diligence investigation on the external guarantee of the Company and its subsidiaries in accordance with the requirements of the "Notice of Issues Regarding Fund Transactions between Listed Companies and Related Parties and External Guarantees of Listed Companies" (Zheng Jian Fa [2003] No. 56) as promulgated by the CSRC. The results of the due diligence were as follows:

There was no external guarantee, nor any other guarantee incurred prior to and subsisting during the reporting period.

Independent directors: Liu Minghui  
Li Dongru  
Chen Fusheng  
Xiao Jianming

29th March 2012

# SUPERVISORY COMMITTEE'S REPORT

## I. Work review of the Supervisory Committee

Number of meetings held

3

<b>Description of meetings of the Supervisory Committee</b>	<b>Agenda of the meetings of the Supervisory Committee</b>
The 8th meeting of the 6th session of the Supervisory Committee	Reviewed and approved the 26th meeting of the 6th session of the Board
The 9th meeting of the 6th session of the Supervisory Committee	Reviewed and approved the interim report and summary for 2011
The 1st meeting of the 7th session of the Supervisory Committee	Elected the chairman of the Supervisory Committee

## II. Independent opinions of the Supervisory Committee on the Company's compliance in operations

The Supervisory Committee attended all general shareholders' meetings and board meetings, and supervised the procedures of such meetings held, resolutions to be reviewed and approved, procedures of decision-making, implementation of resolutions, occurrence of connected transactions, undertaking of duties by the senior management officers and functioning of internal management systems. The Supervisory Committee considered that, the Board, all Directors and senior management officers had duly exercised all resolutions passed at the general shareholders' meetings and the board meetings; all decisions-making procedures were in compliance with the laws and Articles of Associations; and all management systems were effectively in force. The Company's internal control systems were continuously improving. During the supervision and inspection process, none of the Board, Directors or any senior management officers were found to have breached any laws or regulations, or infringed upon the interests of the Company and its shareholders.

## III. Independent opinions of the Supervisory Committee on the review of the Company's financial conditions

During the reporting period, the Supervisory Committee of the Company diligently examined the Company's 2011 Annual Report and auditors' reports prepared by the accounting firm. The Supervisory Committee considered that the Company's 2011 Annual Financial Report had truly and fairly reflected the financial conditions and operating results of the Company. The Supervisory Committee consented to the auditors' reports prepared by the auditors.

## IV. Independent opinions of the Supervisory Committee on the use of proceeds from the latest fundraising

During the reporting period, no changes were made to the proposed use of proceeds raised

## V. Independent opinions of the Supervisory Committee on the Company's acquisition and sale of assets

During the reporting period, there was no major acquisition or sale of assets

## SUPERVISORY COMMITTEE'S REPORT

### **VI. Independent opinions of the Supervisory Committee on the Company's connected transactions**

The Supervisory Committee diligently examined the connected transactions that arose during the reporting period and considered that such connected transactions were all conducted on an arm's length basis and on reasonable commercial terms, the pricing was reasonable and were in the interests of the Company and its shareholders.

### **VII. Independent Opinions of the Supervisory Committee on material differences between realized profit of the Company and estimate**

There was material difference between the realized profit of the Company for 2011 and the estimate.

### **VIII. Review of the internal control self-assessment by the Supervisory Committee**

The Supervisory Committee has considered and passed the internal control self-assessment report.

# SIGNIFICANT EVENTS

## I. PRE-EMPTIVE RIGHTS

Since there is no provision for pre-emptive rights under the Company's Articles of Association, the Company did not have any arrangement for the pre-emptive rights scheme during the reporting period.

## II. WARRANTS AND OTHERS

Neither the Company nor its subsidiaries issued any warrants, convertible securities, options or other securities with similar rights, nor did any person exercise any rights as stated above.

## III. PURCHASE, SALE AND REDEMPTION OF SECURITIES OF THE COMPANY

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any securities issued by the Company during reporting period.

## IV. BANK LOANS, OVERDRAFT AND OTHER BORROWINGS

Details of bank loans, overdrafts and other borrowings as at 31st December 2011 are set out in the Notes to the financial statements.

## V. FINANCIAL RESOURCES AND CAPITAL STRUCTURE OF THE GROUP

For the year ended 31st December 2011, the Group had no long-term borrowings and the Group had borrowing due within one year of RMB100,000,000. The Group maintains a sound credit condition with a high margin product mix and has sufficient cash flow for future repayment of liabilities due.

As at the end of 2011, the shareholders' equity of the Group was RMB1,456,685,000, compared to RMB1,431,023,000 as at the end of 2010.

## VI. GEARING RATIO

The shareholders' equity to debt ratio of the Group for 2011 was 1.32, compared to 1.75 in 2010.

## VII. CONTINGENT LIABILITIES

Details of contingent liabilities of the Company as at 31st December 2011 are set out in the notes to the financial statements.

## VIII. MAJOR LITIGATIONS AND ARBITRATIONS

There was no major litigation or arbitration in the reporting period.

## IX. THE COMPANY'S EQUITY INTEREST HELD IN OTHER LISTED COMPANIES AND INVESTMENT IN FINANCIAL ENTERPRISES

There was no equity interest held by the Company in other listed companies, nor any investment in financial enterprises during the reporting period.

## X. PURCHASE AND DISPOSAL OF ASSETS OR MERGER AND ACQUISITION ACTIVITIES DURING THE REPORTING PERIOD

There was no purchase or sale of assets, nor any merger and acquisition activity during the reporting period.

# SIGNIFICANT EVENTS

## XI. CONNECTED TRANSACTIONS DURING THE REPORTING PERIOD

- 1) The Company entered into the leasing contract with Yunnan State-owned Assets Property Management Company Limited (“Property Management Co.”), which is the subsidiary of the Company’s shareholder – Yunnan Industrial Investment Holding Group Co., Ltd., to lease the man-made cavern, originally used as the fleet repair workshop and place of the Company. The leasing area is 10,465.96 square meters. Presently, the Property Management Co., requested to adjust the rental referring to the fair market value. After negotiation, the following terms have been achieved: a. the rental of the first year will be RMB989,150; b. the rental of the next year will be increased 10% based on the previous year, i.e. the rental of the second year will be RMB1,088,065 and the third year will be RMB1,196,871; c. the rental is effective for three years, from 1st January 2011 to 11th November 2013.
- 2) The Company entered into the agreements on a series of connected transactions such as Property Management Service and Machine Tool Strip Plant Lease with Kunming Kunji General Machine Co., Ltd. After negotiation, the following terms have been achieved: 1. RMB569,525.86 per year was charged for six service items in living quarters, with RMB422,759.05 and RMB146,766.81 paid by Shenji Group Kunming Machine Tool Company Limited and Kunji Group respectively per year; 2. water and electricity fee was RMB19,110 per month; 3. staff dormitory management fee was RMB6,483.41 per month; 4. plant lease rent was RMB100,000 per year; and 5. the rental is effective for one year, from 1st January 2011 to 31st December 2011.
- 3) The first extraordinary general meeting for 2011 held on 18th July 2011 approved the Company entered into Technologies License Contract with Schiess GmbH, under which the Company introduced from Schiess GmbH the design, manufacture and installation technical know-how of the double column portals for cross rail profile of 2000 mm, together with a exclusive and non-transferable license right to use the technical know-how to manufacture in China and sell the contract product in Asia. According to the Technologies License Agreement, contract expenses consist of 6,600,000 Euros of one-off license fee, 700,000 Euros of staff training fee and 200,000 Euros paid for technical services of two prototype machines with Machine Models VMG6 and VM8;

The Company will solely enter into agreement with Schiess GmbH for purchasing assembly part of VMG6 and VM8 prototype machines with a total amount of 7,360,651 Euros.

According to the terms and conditions of the contract, in August 2011, the Company paid 30% of license fee (i.e. 1,980,000 Euros, which equivalents to RMB18,246,610.80) to Schiess GmbH and have received partial of technical information, including design drawing, process and content of the first machine tool. The amount was presented in balance sheet as other non-current asset as at 31st December 2011.

The Company paid 400,000 Euros (equivalent to RMB3,483,152.00) of technical training fee to Schiess GmbH in November 2011.

## SIGNIFICANT EVENTS

- 4) On 4th August 2011, the Company entered into (1) Lathes Supply Framework Agreement with Yunnan CY Group; (2) Packaging Materials Supply Framework Agreement with Yunnan CY Group Jinhui Coating Factory; and (3) Vertical Lathes and Radial Drilling Lathes Supply Framework Agreement with Shenyang Machine Tool Holding Company Limited. The term of the agreements was effective from the date approved at the general meeting to 31st December 2013 (the Framework Agreement signed with Shenyang Machine Tool Holdings Limited should also be subject to the approval at the general meeting of the Company) and the annual caps of purchasing are listed as follows:

*Unit: RMB ten thousand*

Related party	Yunnan CY Group Co., Ltd.	Yunnan CY Group Jinhui Coating Factory	Shenyang Machine Tool Holding Company Limited	Total
As at 31st December 2011	400	400	1600	2400
As at 31st December 2012	500	500	1800	2800
As at 31st December 2013	600	600	2000	3200
Total	1500	1500	5400	8400

- 5) a. The Company entered into Normal Operating Framework Agreement for purchasing of goods, receipt of services, sales of goods and provision of services in 2011 with TOS VARNSDORF a.s. ("Czech Tos"). The anticipated trading amount was RMB3,000,000 as at 31st December 2011.
- b. The Company entered into Normal Continuous Operating Framework Agreement for purchasing of goods, receipt of services, sales of goods and provision of services in 2011 with TOS Kunming Machine Tool Manufacturing Co., Ltd. ("Kunming TOS"). The anticipated trading amount was RMB146,115,500 as at 31st December 2011;
- c. Kunming TOS entered into Normal Operating Framework Agreement for purchasing of goods, receipt of services, sales of goods and provision of services in 2011 with Czech Tos. The anticipated trading amount was RMB46,715,300 as at 31 December 2011.

## XII. BANKRUPTCY RESTRUCTURING

There was no bankruptcy restructuring of the Company during the year.

## XIII. ANALYSIS OF OTHER MAJOR MATTERS AND ITS IMPACTS AND SOLUTIONS

The was no other major matters relating to the Company during the year.

## XIV. MATERIAL CONTRACTS AND THEIR PERFORMANCE

### 1. Escrow agency, contracting and lease matters

(1) *Escrow agency*

There was no escrow agency of the Company during the year.

(2) *Contracting*

There was no contracting of the Company during the year.

(3) *Lease*

There was no lease of the Company during the year.

## SIGNIFICANT EVENTS

### 2. Guarantee

The Company did not provide any guarantee during the year.

### 3. Entrusted investment

There was no entrusted investment of the Company during the year.

### 4. Other material contracts

There was no other material contract of the Company during the year.

## XV. PERFORMANCE OF COMMITMENTS

1. Shenyang Machine Tool (Group) Co., Ltd. and Yunnan Industrial Investment Holding Group Co., Ltd. undertook that the shares held by them would not be sold through the stock exchange for trading from listing to 31st December 2010. As at 31st December 2010, the shares held by the above two shareholders were not tradable. From 1st January 2011, the selling restricted period for the selling restricted shares held by the above shareholders is expired. The Company has applied for the listing of shares with selling restrictions on 26th September 2011. The application is for the listing of shares with selling restrictions and there is no recent plan to increase or reduce shareholding.
2. Shenyang Machine Tool (Group) Co., Ltd. and Yunnan Industrial Investment Holding Co. Ltd. undertook that the resolution on the transfer of capital reserves to issue new shares be proposed and approved at the general meeting within one year after the completion of share reform on the basis of no less than five new shares for every 10 shares held. Such resolution was approved at the general meeting and relevant class meetings for 2006 held on 29th June 2007 and the transfer was completed.
3. Shenyang Machine Tool (Group) Co., Ltd. and Yunnan Industrial Investment Holding Co. Ltd. Undertook that the resolution on the distribution of profits of no less than 50% of profits in the form of cash bonus dividend be proposed and approved at the general meeting if the performance of the Company in 2006 or 2007 fulfils the conditions for distribution of profits to shareholders. Such distribution of profits was completed in July 2008.
4. Shenyang Machine Tool (Group) Co., Ltd. undertook that it would provide full support to the business development of the Company in terms of technology, business and resources and would consolidate the relevant resources and markets leverage on its own unique strengths based on the principles and models favorable to accelerating the growth of the listed company within two years after the share transfer and share reform with a view to developing Kunming Machine Tool as an important platform for technological upgrade, business expansion and sector growth to provide comprehensive support and facilitate the sustainable and healthy development of the listed company. Currently, Shenyang Machine Tool (Group) Co., Ltd. has introduced production management officers to the Company in order to facilitate the increase in the production management capabilities and provide convenience for the exports of the Company in terms of market expansion.

## XVI. APPOINTMENT AND REMOVAL OF AUDITORS

Any change of auditor:	Yes
Domestic auditor	Formerly engaged
Term of domestic auditor	Zonzun Accounting Office Limited
Foreign auditor	4 years
Term of foreign auditor	KPMG (Hong Kong CPA)
Auditor	4 years
Term of auditor	Currently engaged
	KPMG Huazhen
	1 year



## SIGNIFICANT EVENTS

### **XVII. PENALTIES ON THE LISTED COMPANY, ITS DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS, SHAREHOLDERS AND BENEFICIAL CONTROLLER OF THE COMPANY, AND RECTIFICATION ISSUES**

During the reporting period, there were no penalties on the Company, its directors, supervisors and senior management officers.

### **XVIII. DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT OFFICERS, AND SHAREHOLDERS HOLDING OVER 5% SHARES OF THE COMPANY INVOLVED IN IRREGULAR TRADING OF SHARES OF THE COMPANY AND DISCLOSURE OF THE RECOVERY OF SUCH GAIN ARISING FROM SUCH IRREGULAR TRADING**

During the reporting period, no directors, supervisors, senior management and shareholders holding over 5% shares of the Company were involved in the irregular trading of the shares of the Company.

### **XIX. PUBLIC FLOAT**

Based on the information that is publicly available to the Company and to the knowledge of the directors, the Company has, during the year and up to the date of this report, maintained a public float of not less than 25% of the Company's issued shares as required under the Listing Rules.

### **XX. OTHER SIGNIFICANT EVENTS**

#### **1. Explanation on matters of Winko**

Winko Machines Co., Ltd. convened an extraordinary general meeting of 2008 on 30th June 2008 and a resolution regarding the dissolution of Winko was considered and passed at the meeting. The liquidation team for liquidation of Winko was established which comprised of all shareholders. As at 28th February 2011, the liquidation team has completed the cancellation procedures. The operating results of Winko from 1st January 2011 to the date of cancellation have been consolidated into the Group's consolidated income statement.

2. According to the resolution passed at the 15th meeting of the 6th session of the Board, Kunji Transportation Company Limited ("Kunji Transportation"), a wholly-owned subsidiary of the Company was cancelled. The liquidation team of Kunji Transportation was established on 1st May 2010. In accordance with audit report from Yunnan Hui Tong Accounting Firm (Yun Hui Shen Bao Zi [2011] no. 076), as at 10th June 2011, the total assets and liabilities of the Kunji Transportation have been liquidated completely. The residual assets of Kunji Transportation was RMB1,150,286.89, of which, monetary assets was RMB870,925.66, other accounts receivable was RMB300,000.00 (receivable from the Company), other liabilities was RMB20,638.77 (payable to the Company). All residual assets belong to the only shareholder – Shenji Group Kunming Machine Tool Co., Ltd., of which, paid in capital was RMB500,000.00 and undistributed profit was RMB650,286.89. Offsetting agreement for current account was signed and bank deposit has been paid to the Company on 30th May 2011. At the same time, liquidation team has completed the cancellation procedure with business registration, taxation authorities and banks.

As at the date of this report, the liquidation of the Kunji Transportation has been completed.

## SIGNIFICANT EVENTS

3. At the 33rd meeting of the 6th session of the Board held on 22nd August 2011, the resolution regarding the proposal on implementing the first stage construction of the 60 thousand tons heavy casting workshop under the phase two of the CNC heavy and precision machine tool manufacturing and heavy casting base project by investing RMB414,630,000 was considered and passed. The resolution was submitted to the 2011 the second extraordinary general meeting held on 21st September 2011 and was passed at the meeting. The proposal was then implemented. The proposal this time on the first stage construction of heavy casting workshop project (the "Project") under the phase two also belongs to the whole project of the CNC heavy and precision machine tool manufacturing and heavy casting base and will be implemented in phases. The purpose of this Project is to improve the production capacity in heavy casting and undertake the hardware condition requirements in the project of technology co-operation with Schiess GmbH.
4. The 191,995,687 circulating shares with selling restrictions of the Company (i.e. the shares of the Company held by the largest shareholder Shenyang Machine Tool (Group) Co., Ltd. and the second largest shareholder Yunnan Industrial Investment Holding Group Co., Ltd.) was approved to be listed on 26th September 2011. The largest shareholder and the second largest shareholder jointly declared that the application was for the listing of shares with selling restrictions and they have no recent plans to increase or reduce shareholding.
5. According to the Notice No. 29 of 2011 issued by National Development and Reform Commission, the Ministry of Science and Technology, the Ministry of Finance, General Administration of Customs and State Administration of Taxation, after validation, the Company is the enterprise (group) technology center of the eighteen batch which can enjoy the preferential policies.

## XXI. INFORMATION DISCLOSURE

Event	Publishing newspaper	Publishing date	Website
Announcement on receiving 2010 budgetary investment of central government for the project of heavy cast base	China Securities Daily, Shanghai Securities News and Security Times	25th January 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on continuing connected transaction for the lease of land and property	China Securities Daily, Shanghai Securities News and Security Times	31st January 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on liquidation and cancellation of the subsidiary, Winko Machines Company Limited	China Securities Daily, Shanghai Securities News and Security Times	11th March 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on resolutions passed at the 26th meeting of the 6th session of the Board of directors of the Company	China Securities Daily, Shanghai Securities News and Security Times	22nd March 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>

## SIGNIFICANT EVENTS

Event	Publishing newspaper	Publishing date	Website
Announcement on resolutions passed at the 8th meeting of the 6th session of supervisory committee of the Company	China Securities Daily, Shanghai Securities News and Security Times	22nd March 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Notice of annual general meeting 2010	China Securities Daily, Shanghai Securities News and Security Times	22nd March 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Notice of connected transactions with Schiess GmbH regarding technology transfer	China Securities Daily, Shanghai Securities News and Security Times	22nd March 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Clarification announcement for the 2010 annual report	China Securities Daily, Shanghai Securities News and Security Times	6th April 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Regular report	China Securities Daily, Shanghai Securities News and Security Times	23rd April 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on resolutions passed at the of 2010 AGM	China Securities Daily, Shanghai Securities News and Security Times	10th May 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Notice of first extraordinary general meeting of 2011	China Securities Daily, Shanghai Securities News and Security Times	26th May 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on payment of dividends for A Shares for the year 2010	China Securities Daily, Shanghai Securities News and Security Times	27th May 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement of the Company	China Securities Daily, Shanghai Securities News and Security Times	15th June 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Notice of supplementary resolutions for the first extraordinary general meeting of 2011	China Securities Daily, Shanghai Securities News and Security Times	28th June 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Supplemental notice of supplementary resolutions for the first extraordinary general meeting of 2011	China Securities Daily, Shanghai Securities News and Security Times	29th June 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>

## SIGNIFICANT EVENTS

Event	Publishing newspaper	Publishing date	Website
Announcement on resolutions passed at the first extraordinary general meeting of 2011	China Securities Daily, Shanghai Securities News and Security Times	18th July 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement of the Board	China Securities Daily, Shanghai Securities News and Security Times	28th July 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Ordinary continuing connected transactions	China Securities Daily, Shanghai Securities News and Security Times	4th August 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Notice of the second extraordinary general meeting of 2011	China Securities Daily, Shanghai Securities News and Security Times	4th August 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on resolutions passed at the 33rd meeting of the 6th session of the Board	China Securities Daily, Shanghai Securities News and Security Times	22nd August 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on resolutions passed at the 9th meeting of the 6th session of the supervisory committee	China Securities Daily, Shanghai Securities News and Security Times	22nd August 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
The proposal on implementing the first stage construction of the 60 thousand tons heavy casting workshop under the phase two of the CNC heavy and precision machine tool manufacturing and heavy casting base project by investing RMB414,630,000	China Securities Daily, Shanghai Securities News and Security Times	22nd August 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Notice of supplementary resolutions for the second extraordinary general meeting of 2011	China Securities Daily, Shanghai Securities News and Security Times	30th August 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Notice of the third extraordinary general meeting of 2011	China Securities Daily, Shanghai Securities News and Security Times	14th September 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>

## SIGNIFICANT EVENTS

Event	Publishing newspaper	Publishing date	Website
Indicative announcement on prohibition of circulation of shares with selling restrictions	China Securities Daily, Shanghai Securities News and Security Times	15th September 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on resolutions passed at the second extraordinary general meeting of 2011	China Securities Daily, Shanghai Securities News and Security Times	21st September 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement of ordinary continuing connected transactions	China Securities Daily, Shanghai Securities News and Security Times	17th October 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Notice of supplementary resolutions for the third extraordinary general meeting of 2011	China Securities Daily, Shanghai Securities News and Security Times	17th October 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Notice of the Board	China Securities Daily, Shanghai Securities News and Security Times	17th October 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Regular report	China Securities Daily, Shanghai Securities News and Security Times	27th October 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on resolutions passed at the third extraordinary general meeting of 2011	China Securities Daily, Shanghai Securities News and Security Times	31st October 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on resolutions passed at the 1st meeting of the 7th session of the Board	China Securities Daily, Shanghai Securities News and Security Times	31st October 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on resolutions passed at the 1st meeting of the 7th session of the supervisory committee	China Securities Daily, Shanghai Securities News and Security Times	31st October 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on resolutions passed at the of the 2nd meeting of the 7th session of the Board	China Securities Daily, Shanghai Securities News and Security Times	18th November 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>
Announcement on the passing of the validation as a state-level enterprise technology center	China Securities Daily, Shanghai Securities News and Security Times	23rd November 2011	<a href="http://www.sse.com.cn">http://www.sse.com.cn</a> , <a href="http://www.hkex.com.hk">http://www.hkex.com.hk</a> , <a href="http://www.kmtcl.com.cn">http://www.kmtcl.com.cn</a>

# AUDITORS' REPORT

## Auditors' Report

KPMG-C (2012) AR No.0080

### All Shareholders of Shenji Group Kunming Machine Tool Company Limited

We have audited the accompanying financial statements of Shenji Group Kunming Machine Tool Company Limited ("the Company"), which comprise the consolidated balance sheet and balance sheet as at 31 December 2011, the consolidated income statement and income statement, the consolidated cash flow statement and cash flow statement, the consolidated statement of changes in shareholders' equity and statement of changes in shareholders' equity for the year then ended, and notes to the financial statements.

## 1. MANAGEMENT'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The Company's management is responsible for the preparation and fair presentation of these financial statements. This responsibility includes: (1) preparing these financial statements in accordance with Accounting Standards for Business Enterprises issued by the Ministry of Finance of the People's Republic of China, and fairly presenting them; (2) designing, implementing and maintaining internal control which is necessary to enable that the financial statements are free from material misstatement, whether due to fraud or error.

## 2. AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with China Standards on Auditing for Certified Public Accountants. Those standards require that we comply with China Code of Ethics for Certified Public Accountants, and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## 3. OPINION

In our opinion, the financial statements present fairly, in all material respects, the consolidated financial position and financial position of the Company as at 31 December 2011, and the consolidated financial performance and financial performance and the consolidated cash flows and cash flows of the Company for the year then ended in accordance with the requirements of Accounting Standards for Business Enterprises issued by the Ministry of Finance of the People's Republic of China.

**KPMG Huazhen**

China, Beijing

*Certified Public Accountants*  
*Registered in the People's Republic of China*  
Peng Jing  
Zhong Dan  
29 March 2012

# CONSOLIDATED BALANCE SHEET

As at 31st December 2011

Unit: RMB

Item	Note	2011	2010
<b>CURRENT ASSETS:</b>			
Cash at bank and on hand	V. 1	192,200,330.65	296,294,409.56
Bills receivable	V. 2	104,034,946.22	115,906,620.42
Accounts receivable	V. 3	284,945,522.91	249,828,811.68
Prepayments	V. 5	79,699,344.86	53,337,722.23
Other receivables	V. 4	14,229,856.33	16,619,229.09
Inventories	V. 6	983,679,390.52	752,776,010.82
<b>TOTAL CURRENT ASSETS</b>		<b>1,658,789,391.49</b>	<b>1,484,762,803.80</b>
<b>NON-CURRENT ASSETS:</b>			
Long-term equity investments	V. 7	61,924,580.95	60,589,759.15
Fixed assets	V. 8	548,781,349.24	486,847,924.98
Construction in progress	V. 9	119,146,793.10	122,304,905.59
Intangible assets	V. 10	35,378,639.17	35,195,153.39
Goodwill	V. 11	7,296,277.00	7,296,277.00
Long-term deferred expenses	V. 12	1,365,116.55	678,209.81
Deferred tax assets	V. 13	46,245,088.62	50,055,327.91
Other non-current assets	V. 14	79,737,125.00	–
<b>TOTAL NON-CURRENT ASSETS</b>		<b>899,874,969.63</b>	<b>762,967,557.83</b>
<b>TOTAL ASSETS</b>		<b>2,558,664,361.12</b>	<b>2,247,730,361.63</b>
<b>CURRENT LIABILITIES:</b>			
Short-term loans	V. 17	100,000,000.00	46,000,000.00
Bills payable	V. 18	46,596,910.09	20,426,973.00
Accounts payable	V. 19	363,932,002.93	230,256,410.68
Advances from customers	V. 20	433,353,771.35	414,725,123.22
Employee benefits payable	V. 21	33,498,389.64	34,656,409.79
Taxes payable	V. 22	7,310,302.86	4,870,643.57
Dividends payable	V. 23	135,898.49	135,898.49
Other payables	V. 24	40,665,636.99	20,662,047.15
Non-current liabilities due within one year	V. 26	418,509.00	–
Other current liabilities		–	79,817.18
<b>TOTAL CURRENT LIABILITIES</b>		<b>1,025,911,421.35</b>	<b>771,813,323.08</b>
<b>NON-CURRENT LIABILITIES:</b>			
Long-term payables	V. 27	1,918,881.90	2,345,300.00
Special payables	V. 28	15,267,565.87	100,000.00
Provisions	V. 25	17,390,990.97	16,301,190.59
Other non-current liabilities	V. 29	41,490,702.91	26,147,303.11
<b>TOTAL NON-CURRENT LIABILITIES</b>		<b>76,068,141.65</b>	<b>44,893,793.70</b>
<b>TOTAL LIABILITIES</b>		<b>1,101,979,563.00</b>	<b>816,707,116.78</b>

The financial statement notes set out on page 72 to page 165 forms an integral part of these financial statements.

# CONSOLIDATED BALANCE SHEET

As at 31st December 2011

Unit: RMB  
2010

Item	Note	2011	2010
<b>Shareholders' equity:</b>			
Share capital	V. 30	531,081,103.00	531,081,103.00
Capital reserve	V. 31	27,303,321.72	27,303,321.72
Surplus reserve	V. 32	116,508,002.60	109,024,823.62
Retained earnings	V. 33	727,245,922.10	706,716,031.08
Total equity attributable to shareholders of the company		1,402,138,349.42	1,374,125,279.42
Minority interests		54,546,448.70	56,897,965.43
<b>TOTAL SHAREHOLDERS' EQUITY</b>		<b><u>1,456,684,798.12</u></b>	<b><u>1,431,023,244.85</u></b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b><u>2,558,664,361.12</u></b>	<b><u>2,247,730,361.63</u></b>

The financial statements were approved by the Board of Directors of the Company on 29th March 2012.

Legal representative of the Company:  
Wang Xing

The person in charge of accounting affairs:  
Li Shunzhen

The head of the accounting department:  
Zhao Qiongfeng

(Seal of the Company)

Notes to the financial statements set out on pages 72 to 165 form part of these financial statements.



# BALANCE SHEET

As at 31st December 2011

Unit: RMB

Items	Notes	2011	2010
<b>CURRENT ASSETS:</b>			
Cash at bank and on hand		147,087,572.52	248,304,966.05
Bills receivable		87,154,946.22	85,692,620.42
Accounts receivable	XI. 1	197,668,708.57	193,467,126.14
Prepayments		45,024,333.22	9,145,017.82
Dividends receivable		40,130,802.55	11,000,000.00
Other receivables	XI. 2	19,977,210.82	22,497,529.81
Inventories		830,051,956.13	585,789,448.80
<b>TOTAL CURRENT ASSETS</b>		<b>1,367,095,530.03</b>	<b>1,155,896,709.04</b>
<b>NON-CURRENT ASSETS:</b>			
Long-term equity investments	XI. 3	87,617,846.80	88,283,025.00
Fixed assets		498,566,837.42	433,479,837.52
Construction in progress		119,146,793.10	122,304,905.59
Intangible assets		23,215,536.70	22,725,913.32
Long-term deferred expenses		1,058,172.55	640,217.12
Deferred tax assets		38,085,867.83	47,637,778.82
Other non-current assets		79,737,125.00	–
<b>TOTAL NON-CURRENT ASSETS</b>		<b>847,428,179.40</b>	<b>715,071,677.37</b>
<b>TOTAL ASSETS</b>		<b>2,214,523,709.43</b>	<b>1,870,968,386.41</b>
<b>CURRENT LIABILITIES:</b>			
Short-term loans		80,000,000.00	21,000,000.00
Bills payable		20,000,000.00	–
Accounts payable		298,667,958.42	167,607,105.93
Advances from customers		281,112,591.02	264,996,242.49
Employee benefits payable		32,029,264.98	32,938,912.49
Taxes payable		5,888,997.79	4,497,424.19
Other payables		50,833,320.18	13,807,715.82
Non-current liabilities due within one year		418,509.00	–
<b>TOTAL CURRENT LIABILITIES</b>		<b>768,950,641.39</b>	<b>504,847,400.92</b>
<b>NON-CURRENT LIABILITIES:</b>			
Long-term payables		1,918,881.90	2,345,300.00
Special payables		15,167,565.87	–
Provisions		17,390,990.97	16,301,190.59
Other non-current liabilities		41,490,702.91	26,147,303.11
<b>TOTAL NON-CURRENT LIABILITIES</b>		<b>75,968,141.65</b>	<b>44,793,793.70</b>
<b>TOTAL LIABILITIES</b>		<b>844,918,783.04</b>	<b>549,641,194.62</b>

Notes to the financial statements set out on pages 72 to 165 form part of these financial statements.

# BALANCE SHEET

As at 31st December 2011

Items	Notes	2011	Unit: RMB 2010
<b>Shareholders' equity</b>			
Share capital		531,081,103.00	531,081,103.00
Capital reserve		27,303,321.72	27,303,321.72
Surplus reserve		116,508,002.60	109,024,823.62
Retained earnings		<u>694,712,499.07</u>	<u>653,917,943.45</u>
<b>TOTAL SHAREHOLDERS' EQUITY</b>		<b><u>1,369,604,926.39</u></b>	<b><u>1,321,327,191.79</u></b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b><u>2,214,523,709.43</u></b>	<b><u>1,870,968,386.41</u></b>

The financial statements were approved by the Board of Directors of the Company on 29th March 2012.

Legal representative of the Company:  
Wang Xing

The person in charge of accounting affairs:  
Li Shunzhen

The head of the accounting department:  
Zhao Qiongfeng

(Seal of the Company)

Notes to the financial statements set out on pages 72 to 165 form part of these financial statements.

# CONSOLIDATED INCOME STATEMENT

For the year 2011

Unit: RMB

Items	Notes	2011	2010
<b>1. Operating income</b>	V. 34	<b>1,804,857,564.29</b>	<b>1,597,705,267.19</b>
<b>2. Less: Operating costs</b>	V. 34	<b>1,368,376,106.28</b>	<b>1,162,557,001.55</b>
Business tax and surcharges	V. 35	8,024,321.64	1,558,286.19
Selling and distribution expenses	V. 36	134,188,688.09	108,183,773.43
General and administrative expenses	V. 37	169,652,944.38	140,968,801.21
Financial expenses	V. 38	3,409,201.42	3,992,791.80
Impairment loss	V. 40	62,921,703.56	1,356,465.78
Add: Investment income ("—"for loss)	V. 39	7,334,821.80	9,859,063.47
Including: Income from investments in associates and jointly controlled enterprises		<u>7,334,821.80</u>	<u>9,859,063.47</u>
<b>3. Operating profit ("—"for losses)</b>		<b>65,619,420.72</b>	<b>188,947,210.70</b>
Add: Non-operating income	V. 41	5,090,585.51	14,068,307.88
Less: Non-operating expenses	V. 42	1,925,909.70	2,155,073.16
Including: losses from disposal of non-current assets		<u>499,354.16</u>	<u>625,490.12</u>
<b>4. Profit before income tax ("—" for losses)</b>		<b>68,784,096.53</b>	<b>200,860,445.42</b>
Less: Income tax expenses	V. 43	<u>16,568,488.10</u>	<u>27,397,123.94</u>
<b>5. Net profit for the year ("—"for net losses)</b>		<b>52,215,608.43</b>	<b>173,463,321.48</b>
Attributed to: Shareholders of the Company		54,567,125.16	178,324,801.52
Minority interests		<u>(2,351,516.73)</u>	<u>(4,861,480.04)</u>
<b>6. Earnings per share:</b>			
(1) Basic earnings per share	V. 44	0.10	0.34
(2) Diluted earnings per share	V. 44	0.10	0.34
<b>7. Other comprehensive income</b>		—	—
<b>8. Total comprehensive income</b>		<b>52,215,608.43</b>	<b>173,463,321.48</b>
Attributed to: Shareholders of the Company		54,567,125.16	178,324,801.52
Minority interest		<u>(2,351,516.73)</u>	<u>(4,861,480.04)</u>

The financial statements were approved by the Board of Directors of the Company on 29th March 2012.

Legal representative of the Company:  
Wang Xing

The person in charge of accounting affairs:  
Li Shunzhen

The head of the accounting department:  
Zhao Qiongfeng

(Seal of the Company)

Notes to the financial statements set out on pages 72 to 165 form part of these financial statements.

# INCOME STATEMENT

For the year 2011

Unit: RMB

Items	Notes	2011	2010
<b>1. Operating income</b>	<i>XI. 4</i>	<b>1,543,019,054.78</b>	<b>1,394,948,280.91</b>
Less: Operating costs	<i>XI. 4</i>	1,142,044,017.59	975,122,087.66
Business tax and surcharges		6,935,948.23	81,212.46
Selling and distribution expenses		124,945,870.63	100,412,256.15
General and administrative expenses		150,841,028.04	117,446,027.64
Financial expenses		1,899,375.54	3,070,139.06
Impairment loss		61,489,436.88	394,749.38
Add: Investment income	<i>XI. 5</i>	37,115,911.24	9,859,063.47
Including: Income from investments in associates and jointly controlled enterprises		7,334,821.80	9,859,063.47
<b>2. Operating profit ("–" for losses)</b>		<b>91,979,289.11</b>	<b>208,280,872.03</b>
Add: Non-operating income		5,090,528.20	10,711,329.75
Less: Non-operating expenses		1,528,527.77	1,807,557.04
Including: losses from disposal of non-current assets		449,985.37	(624,889.14)
<b>3. Profit before income tax ("–" for total losses)</b>		<b>95,541,289.54</b>	<b>217,184,644.74</b>
Less: Income tax expenses		20,709,499.78	29,446,394.02
<b>4. Net profit for the year ("–" for net losses)</b>		<b>74,831,789.76</b>	<b>187,738,250.72</b>
<b>5. Other comprehensive income</b>		–	–
<b>6. Total comprehensive income</b>		<b>74,831,789.76</b>	<b>187,738,250.72</b>

The financial statements were approved by the Board of Directors of the Company on 29th March 2012.

Legal representative of the Company:  
Wang Xing

The person in charge of accounting affairs:  
Li Shunzhen

The head of the accounting department:  
Zhao Qiongfeng

(the Seal of the Company)

Notes to the financial statements set out on pages 72 to 165 form part of these financial statements.

# CONSOLIDATED CASH FLOW STATEMENT

For the year 2011

Unit: RMB

Item	Notes	2011	2010
<b>1. Cash flows from operating activities:</b>			
Cash received from sale of goods and rendering of services		1,964,949,740.05	2,017,681,599.79
Refund of taxes		66,264.68	1,240,180.70
Cash received relating to other operating activities	V. 46(1)	10,226,078.00	24,122,610.13
Sub-total of cash inflows		1,975,242,082.73	2,043,044,390.62
Cash paid for goods and services		1,498,622,290.51	1,450,105,945.55
Cash paid to and for employees		302,276,499.68	235,138,343.49
Cash paid for all types of taxes		112,120,349.48	127,771,856.59
Cash paid relating to other operating activities	V. 46(2)	61,568,186.36	100,755,461.65
Sub-total of cash outflows		1,974,587,326.03	1,913,771,607.28
Net cash inflow from operating activities	V. 47(1)	654,756.70	129,272,783.34
<b>2. Cash flows from investing activities:</b>			
Cash received from return on investment		6,000,000.00	5,289,191.40
Net cash received from disposal of fixed assets, intangible assets and other long-term assets		1,102,590.00	365,498.47
Sub-total of cash inflows		7,102,590.00	5,654,689.87
Cash paid for acquisition of fixed assets, intangible assets and other long-term assets		165,856,206.78	69,989,452.71
Cash paid for guarantees		5,980,175.84	5,247,135.19
Sub-total of cash outflows		171,836,382.62	75,236,587.90
Net cash outflow from investing activities		(164,733,792.62)	(69,581,898.03)
<b>3. Cash flows from financing activities:</b>			
Cash received from borrowings		100,000,000.00	46,000,000.00
Cash received relating to other financing activities	V. 46(3)	31,167,565.87	–
Sub-total of cash inflows		131,167,565.87	46,000,000.00
Cash repayments of borrowings		46,000,000.00	70,000,000.00
Cash paid for of dividends, profit distributions or interest		29,972,771.22	24,136,523.76
Sub-total of cash outflows		75,972,771.22	94,136,523.76
Net cash inflow/(outflows) from financing activities		55,194,794.65	(48,136,523.76)
<b>4. Effect of foreign exchange rate changes on cash and cash equivalents</b>		<b>(1,190,013.48)</b>	<b>(609,646.31)</b>
<b>5. Net increase in cash and cash equivalents</b> ("–" for decreases)	V. 47(1)	(110,074,254.75)	10,944,715.24
Add: Cash and cash equivalents at the beginning of the year		285,882,274.37	274,937,559.13
<b>6. Cash and cash equivalents at the end of the year</b>	V. 47(2)	<b>175,808,019.62</b>	<b>285,882,274.37</b>

The financial statements were approved by the Board of Directors of the Company on 29th March 2012.

Legal representative of the Company:  
Wang Xing

The person in charge of accounting affairs:  
Li Shunzhen

The head of the accounting department:  
Zhao Qiongfeng

(Seal of the Company)

Notes to the financial statements set out on pages 72 to 165 form part of these financial statements.

# CASH FLOW STATEMENT

For the year 2011

Unit: RMB  
2010

Item	Notes	2011	2010
<b>1. Cash flows from operating activities:</b>			
Cash received from sale of goods and rendering of services		1,718,455,799.13	1,648,030,993.03
Refund of taxes		–	1,089,237.53
Cash received relating to other operating activities		9,251,024.91	23,121,367.95
Sub-total of cash inflows		1,727,706,824.04	1,672,241,598.51
Cash paid for goods and services		1,314,457,567.69	1,129,373,117.76
Cash paid to and for employees		272,568,425.03	213,289,347.27
Cash paid for all types of taxes		97,443,678.81	113,415,766.36
Cash paid relating to other operating activities		49,594,617.93	90,991,755.10
Sub-total of cash outflows		1,734,064,289.46	1,547,069,986.49
Net cash (outflow)/inflow from operating activities	XI. 6 (1)	(6,357,465.42)	125,171,612.02
<b>2. Cash flows from investing activities:</b>			
Cash received from disposal of investments		1,150,286.89	–
Cash received from return on investments		6,000,000.00	5,289,191.40
Net cash received from disposal of fixed assets, intangible assets and other long-term assets		1,101,220.00	335,667.00
Sub-total of cash inflows		8,251,506.89	5,624,858.40
Cash paid for guarantee		4,000,000.00	–
Cash paid for acquisition of fixed assets, intangible assets and other long-term assets		164,525,214.61	67,775,153.71
Sub-total of cash outflows		168,525,214.61	67,775,153.71
Net cash outflow from investing activities		(160,273,707.72)	(62,150,295.31)
<b>3. Cash flows from financing activities:</b>			
Cash received from borrowings		80,000,000.00	–
Cash received relating to other financing activities		31,167,565.87	21,000,000.00
Sub-total of cash inflows		111,167,565.87	21,000,000.00
Cash repayments of borrowings		21,000,000.00	50,000,000.00
Cash paid for dividends, profit distribution or interest		27,563,772.78	22,951,359.59
Sub-total of cash outflows		48,563,772.78	72,951,359.59
Net cash inflow/(outflow) from financing activities		62,603,793.09	(51,951,359.59)
<b>4. Effect of foreign exchange rate changes on cash and cash equivalents</b>		<b>(1,190,013.48)</b>	<b>(609,646.31)</b>
<b>5. Net increase in cash and cash equivalents</b>			
("–" for net decrease)	XI. 6 (1)	(105,217,393.53)	10,460,310.81
Add: Cash and cash equivalents at the beginning of the year		248,304,966.05	237,844,655.24
<b>6. Cash and cash equivalents at the end of the year</b>	XI. 6 (2)	<b>143,087,572.52</b>	<b>248,304,966.05</b>

The financial statements were approved by the Board of Directors of the Company on 29th March 2012.

Legal representative of the Company:  
Wang Xing

The person in charge of accounting affairs:  
Li Shunzhen

The head of the accounting department:  
Zhao Qionghen

(Seal of the Company)

Notes to the financial statements set out on pages 72 to 165 form part of these financial statements.

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Unit: RMB

Item	Notes	2011						2010					
		Attributable to the equity holders of the Company					Total	Attributable to the equity holders of the Company					Total
		Share capital	Capital reserve	Surplus reserve	Retained earnings	Minority interest		Share capital	Capital reserve	Surplus reserve	Retained earnings	Minority interest	
1. Balance at the beginning of the year		531,081,103.00	27,303,321.72	109,024,823.62	706,716,031.08	56,897,965.43	1,431,023,244.85	424,864,883.00	133,519,541.72	90,250,998.55	568,378,612.85	61,759,445.47	1,278,773,481.59
2. Changes in equity for the year ("—" for decrease)													
(1) Net profit for the year		-	-	-	54,567,125.16	(2,351,516.73)	52,215,608.43	-	-	-	178,324,801.52	(4,861,480.04)	173,463,321.48
(2) Other comprehensive income		-	-	-	-	-	-	-	-	-	-	-	-
Sub-total of (1) and (2)		-	-	-	54,567,125.16	(2,351,516.73)	52,215,608.43	-	-	-	178,324,801.52	(4,861,480.04)	173,463,321.48
(3) Appropriation of profits	V. 33												
1. Appropriation of surplus reserve		-	-	7,483,178.98	(7,483,178.98)	-	-	-	-	18,773,825.07	(18,773,825.07)	-	-
2. Distribution to shareholders		-	-	-	(26,554,055.16)	-	(26,554,055.16)	-	-	-	(21,213,558.22)	-	(21,213,558.22)
(4) Transfer within equity													
1. Share capital increased by capital reserve transfer		-	-	-	-	-	-	106,216,220.00	(106,216,220.00)	-	-	-	-
3. Closing balance of current year		531,081,103.00	27,303,321.72	116,508,002.60	727,245,922.10	54,546,448.70	1,456,684,798.12	531,081,103.00	27,303,321.72	109,024,823.62	706,716,031.08	56,897,965.43	1,431,023,244.85

The financial statements were approved by the Board of Directors of the Company on 29th March 2012.

Legal representative of the Company:  
Wang Xing

The person in charge of accounting affairs:  
Li Shunzhen

The head of the accounting department:  
Zhao Qiongfeng

(Seal of the Company)

Notes to the financial statements set out on pages 72 to 165 form part of these financial statements.

# STATEMENT OF CHANGES IN EQUITY

Unit: RMB

Item	Notes	2011					2010				
		Share capital	Capital reserve	Surplus reserve	Retained earnings	Total	Share capital	Capital reserve	Surplus reserve	Retained earnings	Total
1. Balance at the beginning of the year		531,081,103.00	27,303,321.72	109,024,823.62	653,917,943.45	1,321,327,191.79	424,864,883.00	133,519,541.72	90,250,998.55	506,167,076.02	1,154,802,499.29
2. Changes in equity for the year (“-” for decrease)											
(1) Net profit for the year		-	-	-	74,831,789.76	74,831,789.76	-	-	-	187,738,250.72	187,738,250.72
(2) Other comprehensive income		-	-	-	-	-	-	-	-	-	-
Sub-total of (1) and (2)		-	-	-	74,831,789.76	74,831,789.76	-	-	-	187,738,250.72	187,738,250.72
(3) Appropriation of profits	V. 33										
1. Appropriation of surplus reserve		-	-	7,483,178.98	(7,483,178.98)	-	-	-	18,773,825.07	(18,773,825.07)	-
2. Distribution to shareholders		-	-	-	(26,554,055.16)	(26,554,055.16)	-	-	-	(21,213,558.22)	(21,213,558.22)
(4) Transfer with in equity											
1. Share capital increased by capital reserve transfer		-	-	-	-	-	106,216,220.00	(106,216,220.00)	-	-	-
3. Closing balance of current year		531,081,103.00	27,303,321.72	116,508,002.60	694,712,499.07	1,369,604,926.39	531,081,103.00	27,303,321.72	109,024,823.62	653,917,943.45	1,321,327,191.79

The financial statements were approved by the Board of Directors of the Company on 29th March 2012.

Legal representative of the Company:  
Wang Xing

The person in charge of accounting affairs:  
Li Shunzhen

The head of the accounting department:  
Zhao Qiongfeng

(Seal of the Company)

Notes to the financial statements set out on pages 72 to 165 form part of these financial statements.



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (I). CORPORATE INFORMATION

Shenji Group Kunming Machine Tool Company Limited (the “Company”) was established in the People’s Republic of China (“the PRC”) with limited liability on 19th October 1993. The place of registration of the Company is 23 Ciba Road, Kunming City, Yunnan Province, the PRC.

The Company is a stock company limited by restructuring from Kunming Machine Tool Plant approved by [1993] no. 173 Ti Gai Sheng issued by the State Economic Reform Commission. The name at establishment was Kunming Machine Tool Company Limited (“Kunji”). Kunming Machine Tool Plant used its assets and liabilities at 30 June 1993 to invest in the Company. The above assets and liabilities were assessed by Shanghai Accounting Firm. The assessed net assets were RMB179,258,700. The assessment was approved by [1993] no. 420 Guo Zi Ping issued by the National State-owned assets Administration Commission. According to [1993] no. 114 Guo Zi Qi Han Fa issued by the National State-owned assets Administration Commission, the assessed state-owned land use rights included in the above net assets should be reduced by RMB34,217,100, meanwhile, 82.74% of the adjusted net assets (assessment value was RMB145,041,600) was discounted to 120,007,400 shares with par value RMB1.00 per share. The original investors of Kunming Machine Tool Plant, Yunnan Provincial People’s Government and Kunming Jinghua Company Ltd., held 102,397,700 and 17,609,700 shares respectively.

Approved by [1993] no. 50 Zheng Wei Fa issued by the Security Commission of the State Council, Kunji issued and listed 65,000,000 H shares with par value RMB1.00 per share in the Stock Exchange of Hong Kong Limited in December 1993. Then, it issued and listed 60,000,000 A shares with par value RMB1.00 per share in Shanghai Stock Exchange in January 1994.

On 25th December 2000, Xi’an Jiaotong University Industrial (Group) Incorporation (“Jiaotong Group”) entered into Shares Transfer Agreement of Jiaoda Kunji High-Tech Company Limited with the People’s Government of Yunnan Province (“Yunnan Government”) whereby Yunnan Government would transfer 71,052,146 state-owned shares of the Company to Jiaotong Group. The transaction was approved by [2001] no. 283 Cai Qi – the Approval of State-owned Shares Transfer of Jiaoda Kunji High-tech Company Limited issued by the Ministry of Finance of the PRC. Upon completion of share transfer procedure on 5th June 2001, Jiaotong Group became the largest shareholder of the Company.

With effective from 29th March 2002, the Company used the name “Jiaoda Kunji High Tech Company Limited” (“Jiaoda Kunji”) jointly approved by the State Administration for Industry and Commerce of the PRC and the Ministry of Foreign Trade and Economic Cooperation of the PRC after completing the business registration for change of company name in Yunnan Commercial and Industrial Administration Bureau.

On 15th September 2005, Jiaotong Group and Shenyang Machine Tool (Group) Co., Ltd. (“Shenji Group”) entered into a Share Transfer Agreement. Shenji Group agreed to purchase 71,052,146 shares of Jiaoda Kunji held by Jiaotong Group. The share transfer was approved pursuant to the “Written Reply Regarding the Transfer of State-owned Shares of Jiaoda Kunji High-tech Co., Ltd.” (Guo Zi Chan Quan [2006] No. 628) issued by State-owned Assets Supervision and Administration Committee of the State Council and the Opinion on Information Disclosure of the Acquisition of Jiaoda Kunji High-tech Co., Ltd. by Shenyang Machine Tool (Group) Co., Ltd. (Zheng Jian Gong Si [2006] No. 255) by China Securities Regulation Committee. On 1st December 2006, the register of equity transfer was completed and Shenji Group became the largest shareholder of the Company.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (I). CORPORATE INFORMATION *(Continued)*

On 4th April 2006, pursuant to the “Written Reply of the People’s Government of Yunnan Province Regarding the Transfer of Title of Jiaoda Kunji High-Tech Co., Ltd.” issued by the People’s Government of Yunnan Province and the “Written Reply of Yunnan State-owned Assets Supervision and Administration Committee regarding the Grant of Authorization to Yunnan State-owned Assets Operation Co., Ltd. to Exercise the Shareholders’ Right of Jiaoda Kunji High-tech Co., Ltd.” issued by Yunnan State-owned Assets Supervision and Administration Committee, 31,345,554 state-owned shares held by the People’s Government of Yunnan were transferred to Yunnan State-owned Assets Operation Co., Ltd. (“Yunnan State-owned Assets Operation Co., Ltd.”) at nil consideration on 31st December 2005. The share transfer was approved by the State-owned Assets Supervision and Administration Committee of the State Council pursuant to the “Written Reply regarding the Transfer of Part of the State-owned Shares of Jiaoda Kunji High-Tech Co., Ltd.” (Guo Zi Chan Quan [2006] No. 1412). The transfer was completed on 19th January 2007.

On 25th January 2007, the “Written Reply regarding the Transfer of Shares and Increase in Share of Jiaoda Kunji High-Tech Co., Ltd.” (Shang Zi Pi [2007] No. 133) was issued by the Ministry of Commerce of the PRC to approve the share reform proposal of the Company, pursuant to which a total of 38,235,855 shares (as to 28,091,955 A Shares and 10,143,900 H Shares respectively) were transferred from the capital reserve to all the shareholders whose names appeared on the Company’s register of members on 26th February 2007 on the basis of 1.5606 shares for every 10 shares held. On 5th March 2007, the holders of non-circulating shares of the Company made the payment with a total of 18,728,355 shares held as consideration to the holders of circulating A Shares on the basis of 2.7 shares for every 10 shares held. The new A Shares were listed on 7th March 2007. Of 18,728,355 shares, Shenji Group, Yunnan State-owned Assets Operation Co., Ltd. and Jinghua Company contributed as to 11,088,398 shares, 4,891,787 shares and 2,748,170 shares respectively. After implementation of the consideration arrangement, non-circulating shares held by the holders of non-circulating shares of the Company became tradable and listed.

On 23rd March 2007, approved by the shareholders’ meeting of Jiaoda Kunji, Jiaoda Kunji High-Tech Company changed its name to Shenji Group Kunming Machine Tool Company Limited.

Approved by the annual general meeting of the Company held on 29th June 2007, based on total share capital of 283,243,255 shares of the Company, increased shares on the basis of 5 shares for every 10 shares held to all the shareholders by capitalization of capital reserve, totally increased 141,621,628 shares. After share increase, total issued shares of the Company was 424,864,883 shares, and total registered capital of the Company was RMB424,864,883. The resolution was approved by the “Written Reply Regarding the Change of Name and Increase in Share Capital of Jiaoda Kunji High-Tech Co., Ltd.” (Shang Zi Pi [2007] No. 1390) issued by the Ministry of Commerce of the PRC.

Pursuant to the “Written Reply on the Change in Shareholders of the Six Listed Companies including Yunnan Salt & Chemical Industry Co., Ltd.” (Guo Zi Chan Quan [2009] No. 1182) issued by the State-owned Assets Supervision and Administration Commission of the State Council on 22nd October 2009, 47,018,331 shares of the Company held by Yunnan State Owned Assets Operation Co. Ltd. were transferred to Yunnan Industrial Investment Holding Group Co., Ltd. (“Yunnan Industrial Investment”) to perform the obligations as the contributor of state-owned assets.

Approved by the shareholders’ meetings held on 23rd June 2010, based on total share capital of 424,864,883 shares of the Company, increased shares on the basis of 2.5 shares for every 10 shares held to all the shareholders by capitalization of capital reserve, totally increased 106,216,220 shares. After share increase, total issued shares of the Company would be 531,081,103 shares, and total registered capital of the Company would be RMB531,081,103. The resolution was approved by the “Written Reply from the Department of Commerce of Yunnan Province Concerning its Consent to the Increase in Share Capital by Capitalization of the Capital Reserve by Shenji Group Kunming Machine Tool Company Limited” (Yun Shang Zi [2010] No. 130).

The Company and its subsidiaries (collectively the “Group”) mainly engage in development, design, production and sales of machine tool series products and accessories, sensor and turbo tables and computerized embroidery machines and accessories, and turbo machine series products and accessories.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES

### 1. Basis of preparation of financial statements

The financial statements of the Company have been prepared on a going concern basis.

### 2. Statement of compliance with the corporate accounting standards

The financial statements have been prepared in accordance with the requirements of "Accounting Standards for Business Enterprises – Basic Standard" and 38 Specific Standards issued by the Ministry of Finance on 15th February 2006, and application guidelines, explanations to corporate accounting standards and other relevant regulations issued subsequently (collectively referred to as "corporate accounting standards"). These financial statements provide a true and complete presentation of the consolidated financial position and financial position as at 31st December 2011, the consolidated results of operations and results of operations and the consolidated cash flows and cash flows of the Company for the year 2011.

These financial statements also comply with the disclosure requirements of "Regulation on the Preparation of Information Disclosures of Companies Issuing Public Shares, No. 15: General Requirements for Financial Reports" as revised by the CSRC in 2010 in relation to the disclosure requirements of the financial statements and their accompanying notes.

### 3. Accounting period

The accounting period commences on 1st January and ends on 31st December each year.

### 4. Functional currency

The functional currency of the Company is Renminbi ("RMB"). The Company presents the financial statements in RMB. The functional currency is determined by the Company and its subsidiaries on the basis of the currency in which major income and costs are denominated and settled.

### 5. Accounting treatment for business combination under common control and not under common control

#### (1) *Business combination under common control*

A business combination under common control is a business combination in which all of the combining entities are ultimately controlled by the same party or parties both before and after the combination, and that control is not transitory. Assets and liabilities that are obtained by the acquirer in a business combination shall be measured at their carrying amounts at the combination date as recorded by the party being acquired. The difference between the carrying amount of the net assets obtained and the carrying amount of the consideration paid for the combination (or the aggregate face value of shares issued as consideration) shall be adjusted to share premium under capital reserve (or capital premium). If the share premium under capital reserve (or capital premium) is not sufficient to absorb the difference, any excess shall be adjusted against retained earnings. Expenses that are directly attributable to business combination are expense in the profit and loss at the period incurred. The combination date is the date on which the acquiring party effectively obtains control of the party being acquired.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 5. Accounting treatment for business combination under common control and not under common control *(Continued)*

#### (2) *Business combinations not under common control*

A business combination not under common control is a business combination in which all of the combining entities are not ultimately controlled by the same party or parties both before and after the combination. The sum of the assets paid (including the equity interest of acquiree held before the date of acquisition) and liabilities incurred or committed and the equity securities issued by the Group who as an acquirer for obtaining the controlling interests of the acquiree measured at fair value on the date of acquisition minus the fair value of the acquiree's identifiable net assets in the combination, if the difference is positive, it should be recognized as goodwill (please refer to note II. 17), or if the difference is negative, it shall be included in the profit or loss for the period. The transaction expenses of issuing equity securities or liability securities as consideration for combination are included as the initial measurement amount of equity securities or liability securities. The direct expenses incurred in business combination shall be included in the profit or loss for the period. The difference between the fair value of assets paid and its book value should be included in the profit or loss for the period. The Group shall recognize acquiree's identifiable assets, liabilities and contingent liabilities acquired in the business combination at their fair values on the acquisition date that meet the criteria for recognition. Acquisition date is the date on which the acquirer effectively obtains control of the acquiree.

### 6. Preparation of consolidated financial statements

The consolidated financial statements are based on control for the scope of consolidation, and comprise the Company and its subsidiaries. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its operating activities. The financial position, financial performance and cash flow of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Where a subsidiary was acquired during the reporting period, through a business combination involving entities under common control, the financial statements of the subsidiary are included in the consolidated financial statements as if the combination had occurred at the date that common control was established. Therefore, the opening balances and the comparative figures of the consolidated financial statements are restated. In the preparation of the consolidated financial statements, the subsidiary's assets, liabilities and results of operations are included in the consolidated balance sheet and the consolidated income statement, respectively, based on their carrying amounts, from the date that common control was established.

Where a subsidiary was acquired during the reporting period, through a business combination involving entities not under common control, the acquired subsidiaries are included in the consolidated financial statements from the acquisition date, and based on the fair value of those identifiable assets and liabilities at the acquisition date.

For a business combination not involving enterprises under common control and achieved in stages, the Group remeasured its previously-held equity interest in the acquiree to its fair value at the acquisition date. The difference between the fair value and the carrying amount is recognized as investment income for the current period; the amount recognized in other comprehensive income relating to the previously-held equity interest in the acquiree is reclassified as investment income for the current period.

Where the Company acquires a minority interest from a subsidiary's minority shareholders or disposes of a portion of an interest in a subsidiary without a change in control, the difference between the amount by which the minority interests are adjusted and the amount of the consideration paid or received is adjusted to the capital reserve (share premium) in the consolidated balance sheet. If the credit balance of capital reserve (share premium) is insufficient, any excess is adjusted to retained earnings.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 6. Preparation of consolidated financial statements *(Continued)*

When the Group loses control of a subsidiary due to the disposal of a portion of an equity investment, the Group ceases to recognize the assets, liabilities, minority interests and other related items of the interests related to the subsidiary. The remaining equity investment is remeasured at its fair value at the date when control is lost. Any profit or loss incurred is recognized as investment income for the current period when control is lost.

Minority interest is presented separately in the consolidated balance sheet within shareholders' equity. Net profit or loss attributable to minority shareholders is presented separately in the consolidated income statement below the net profit line item.

When the amount of loss for the current period attributable to the minority shareholders of a subsidiary exceeds the minority shareholders' portion of the opening balance of shareholders' equity of the subsidiary, the excess is allocated against the minority interests.

When the accounting period or accounting policies of a subsidiary are different from those of the Company, the Company makes necessary adjustments to the financial statements of the subsidiary based on the Company's own accounting period or accounting policies. Intra-group balances and transactions, and any unrealized profit or loss arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealized losses resulting from intra-group transactions are eliminated in the same way as unrealized gains but only to the extent that there is evidence of impairment.

### 7. Determination of cash and cash equivalents

Cash and cash equivalents comprise cash on hand, demand deposits, and short-term, highly liquid investments, which are readily convertible into known amounts of cash and are subject to an insignificant risk of change in value.

### 8. Foreign currency transactions

When the Group receives capital in foreign currencies from investors, the capital is translated to Renminbi at the spot exchange rate at the date of the receipt. Other foreign currency transactions are, on initial recognition, translated to Renminbi at the spot exchange rates on the dates of the transactions.

A spot exchange rate is an exchange rate quoted by the People's Bank of China or a cross rate determined based on quoted exchange rates.

Monetary items denominated in foreign currencies are translated to Renminbi at the spot exchange rate at the balance sheet date. The resulting exchange differences are recognized in profit or loss, except those arising from the principals and interests on foreign currency borrowings specifically for the purpose of acquisition, construction of qualifying assets for capitalization (see Note II. 15). Non-monetary items denominated in foreign currencies that are measured at historical cost are to remain their amounts in their accounting currencies. Non-monetary items denominated in foreign currencies that are measured at fair value are translated using the foreign exchange rate at the date the fair value is determined; the resulting exchange differences are recognized in profit or loss.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 9. Financial instruments

Financial instruments of the Group comprise cash at bank and on hand, receivables, payables, loans, and share capital, etc.

#### (1) *Recognition and measurement of financial assets and financial liabilities*

A financial asset or financial liability is recognized in the balance sheet when the Group becomes a party to the contractual provisions of a financial instrument.

The Group classifies financial assets and liabilities into different categories at initial recognition, based on the purpose of acquiring assets or assuming liabilities: loans and receivables and other financial liabilities.

Financial assets and financial liabilities are measured initially at fair value and any attributable transaction costs are included in their initial costs. Subsequent to initial recognition financial assets and liabilities are measured as follows:

#### – Receivables

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

Subsequent to initial recognition, receivables are subsequently stated at amortized cost using the effective interest method.

#### – Other financial liabilities

Financial liabilities other than the financial liabilities at fair value through profit or loss are classified as other financial liabilities.

Subsequent to initial recognition, other financial liabilities are subsequently stated at amortized cost using the effective interest method.

#### (2) *Presentation of financial assets and financial liabilities*

Financial assets and financial liabilities are presented separately in the balance sheet and shall not be offset. However, a financial asset and a financial liability shall be offset and the net amount presented in the balance sheet when both of the following conditions are satisfied:

- the Group has a legal right to offset the recognized amounts and the legal right is currently enforceable; and
- the Group intends either to settle on a net basis, or to realize the financial asset and settle the financial liability simultaneously.

#### (3) *Determination of fair values*

If there is an active market for a financial asset or financial liability, the quoted price in the active market is used to establish the fair value.

If no active market exists for a financial instrument, a valuation technique is used to establish the fair value. Valuation techniques include using recent arm's length market transactions between knowledgeable, willing parties; reference to the current fair value of another instrument that is substantially the same and discounted cash flow analysis. The Group calibrates the valuation technique and tests it for validity periodically.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 9. Financial instruments *(Continued)*

#### (4) *Derecognition of financial assets and financial liabilities*

A financial asset is derecognized if the Group's contractual rights to the cash flows from the financial asset expire or if the Group transfers substantially all the risks and rewards of ownership of the financial asset to another party.

Where a transfer of a financial asset in its entirety meets the criteria of the derecognition, the difference between the two amounts below is recognized in profit or loss:

- carrying amount of the financial asset transferred;
- the sum of the consideration received from the transfer and any cumulative gains or loss that has been recognized directly in equity.

The Group derecognizes a financial liability (or part of it) only when the underlying present obligation (or part of it) is discharged.

#### (5) *Impairment of financial assets*

The carrying amounts of financial assets are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, impairment loss is provided.

Objective evidence that a financial asset is impaired includes, but is not limited to the following:

- (a) significant financial difficulty of the issuer or borrower;
- (b) a breach of contract by the borrower, such as a default or delinquency in interest or principal payments;
- (c) strong probability that the borrower will enter bankruptcy or go through another type of financial reorganisation;
- (d) the disappearance of an active market for the financial asset due to serious financial difficulties on the part of the issuer;
- (e) significant adverse changes in the technological, market, economic or legal environment in which the issuer operates, indicating that the cost of the investment in the equity instrument may not be recovered by the investor;
- (f) a significant or prolonged decline in the fair value of an equity instrument investment to below cost.

For the measurement of impairment of receivables, refer to Note II. 10.

#### (6) *Equity instruments*

An equity instrument is a contract that proves the residual interest of the assets after deducting all liabilities in the Company.

The consideration received from the issuance of equity instruments net of transaction costs is recognized in shareholders' equity.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 10. Impairment of receivables

Receivables are assessed for impairment both on an individual basis and on a collective group basis.

Where impairment is assessed on an individual basis, an impairment loss in respect of a receivable is calculated as the excess of its carrying amount over the present value of the estimated future cash flows (exclusive of future credit losses that have not been incurred) discounted at the original effective interest rate. The Group discounts the carrying amount of the receivables to its present value and the discounted amount is recognized as impairment loss of asset, all impairment losses are recognized in profit or loss.

The assessment is made collectively where receivables share similar credit risk characteristics (including those having not been individually assessed as impaired), based on their historical loss experiences, and adjusted by the observable figures reflecting present economic conditions.

If, after an impairment loss has been recognized on receivables, there is objective evidence of a recovery in value of the financial asset which can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss. A reversal of an impairment loss will not result in the asset's carrying amount exceeding that which would have been determined had no impairment loss been recognized in prior years.

#### (a) *Significant single accounts receivable which being made single bad debt provision*

Judgment basis or criteria for receivables that are individually significant	1 type of trade receivable (trade receivables): criteria: RMB7,000,000 for single accounts receivable;
	2 type of other receivable (other receivables): criteria: RMB3,500,000 for single accounts receivable;
	3 type of personal accounts receivable (other receivables): criteria: RMB100,000 for single accounts receivable.

Method of provision for bad and doubtful debts for receivables that are individually significant and assessed individually

The bad debt provision made for individually significant accounts receivable adopted both on individual basis and on collective combination basis. First by individual impairment test, if the present value of estimated future cash flows (exclusive of future credit losses that have not been incurred) discounted at the original effective interest rate is less than its carrying value, the difference should be recognized as impairment loss and should make provision. If the impairment not being incurred after the individual test, the accounts receivable should combine with other receivables to provide bad debt provision by credit risk characteristic combination (see (b) below).



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 10. Impairment of receivables *(Continued)*

(b) *Bad debt provision for accounts receivable by combination:*

For accounts receivable not impaired after individual test which stated in (a) above, the Group will include it in the accounts receivable combination with credit risk characters to do the test again.

Basis for determining groups	Divide the accounts receivable into two groups based on companies' nature
Group 1	Receivables from third parties
Group 2	Receivables from related parties
Methods for providing bad debt provision by different groups	
Group 1	Ageing analysis
Group 2	Individual assessment

In group 1, provision for bad debts made by ageing analysis:

	Percentage of provision for trade receivable (%)	Percentage of provision for other receivables
Ageing		
Within 1 year (including 1 year)	5%	5%
1-2 years (including 2 years)	30%	50%
2-3 years (including 3 years)	60%	100%
Over 3 years	95%	100%

In group 2, individual impairment test will be conducted to accounts receivable of related parties at the end of the year. Should objective evidence shows that it incurred impairment, according to the difference between the present value of future estimated cash flow and the book value, assets impairment should be recognized. Should no objective evidence show that it has impairment, no bad debt provision should be made.

### 11. Inventories

(1) *Classification*

Inventories include raw material, work in process, semi-finished goods, finished goods and reusable materials. Reusable materials include low-value consumables, packaging materials and other materials, which can be used repeatedly but do not meet the definition of fixed assets.

(2) *Determination of cost of inventories*

The actual cost of inventories is calculated using the weighted average method.

(3) *The underlying factors in the determination of net realizable value of inventories and the basis of provision for diminution in value of inventories*

Inventories are initially measured at cost. Cost of inventories comprises all costs of purchase, costs of conversion and other expenses that to help deliver the inventories to the current location and situation. In addition to the purchasing cost of raw materials, work in progress and finished goods include direct labour costs and an appropriate allocation of production overheads.

Inventories are measured at the lower of cost and net realizable value at the balance sheet date.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 11. Inventories *(Continued)*

- (3) *The underlying factors in the determination of net realizable value of inventories and the basis of provision for diminution in value of inventories (Continued)*

Net realizable value is the estimated selling price in the normal course of business less the estimated costs to completion and the estimated expenses and the related taxes necessary to make the sale. The net realizable value of materials held for use in the production of inventories is measured based on the net realizable value of the finished goods in which they will be incorporated. The net realizable value of the quantity of inventory held to satisfy sales or service contracts is based on the contract price. If the quantities of inventories specified in sales contracts are less than the quantities held by the Group, the net realizable value of the excess portion of inventories shall be based on general selling prices.

Any excess of the cost over the net realizable value of each item of inventories is recognized as a provision for diminution in the value of inventories and charged to profit or loss.

- (4) *Inventory system*

The Group maintains a perpetual inventory system.

- (5) *Amortization of consumables including low-value consumables and packaging material*

Consumables including low-value consumables and packaging materials are amortized in full when received for use. The amounts of the amortization are included in the cost of the related assets or profit or loss.

### 12. Long-term equity investments

- (1) *Initial investment cost*

- (a) Long-term equity investments acquired through a business combination

- The initial investment cost of a long-term equity investment obtained through a business combination involving entities under common control is the Company's share of the subsidiary's equity at the combination date. The difference between the initial investment cost and the carrying amounts of the consideration given is adjusted to share premium in capital reserve. If the balance of the share premium is insufficient, any excess is adjusted to retained earnings.
- For long-term equity investments obtained through business combinations involving enterprises not under common control, the initial investment cost represents the aggregate of the fair values of assets transferred, liabilities assumed, and equity securities issued by the Company, in exchange for control of the acquiree. For a long-term equity investment obtained through a business combination not involving enterprises under common control and achieved in stages, the initial cost comprises the carrying value of previously-held equity investment in the acquiree immediately before the acquisition date, and the additional investment cost at the acquisition date.

- (b) Long-term equity investments acquired otherwise than through a business combination

- An investment in a subsidiary acquired otherwise than through a business combination is initially recognized at actual payment cost if the Group acquires the investment by cash, or at the value stipulated in the investment contract or agreement if an investment is contributed by shareholders.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 12. Long-term equity investments *(Continued)*

#### (2) *Subsequent measurement and recognition of profit and loss*

##### (a) Investments in subsidiaries

In the Company's financial statements, long-term equity investments in subsidiaries are measured subsequently by using the cost method. Cash dividends or profit distributions declared by subsidiaries and attributed to the Company shall be recognized as investment income (not identifying whether it is the net profit realized by investee before or after investment), except those that have been declared but unpaid at the time of acquisition and therefore included in the price paid or consideration. The investments are stated at cost less provision for impairment in the balance sheet.

In the Group's consolidated financial statements, long-term equity investments in subsidiaries are accounted for in accordance with the principles described in Note II. 6.

##### (b) Investment in jointly controlled enterprises and associates

A jointly controlled enterprise is an enterprise which operates under joint control (see Note II. 12(3)) in accordance with a contractual agreement between the Group and other parties.

An associate is an enterprise over which the Group has significant influence (see Note II. 12(3)).

An investment in a jointly controlled enterprise or an associate is accounted for using the equity method when subsequent measurement is made, unless the investment meets the requirements as held-for-sale (see Note II. 26).

The Group makes the following accounting treatments when using the equity method:

- Where the initial investment cost of a long-term equity investment exceeds the Group's interest in the fair value of the investee's identifiable net assets at the date of acquisition, the investment is initially recognized at the initial investment cost. Where the initial investment cost is less than the Group's interest in the fair value of the investee's identifiable net assets, the investment is initially recognized at the initial investment cost at the date of acquisition, the investment is initially recognized at the investor's share of the fair value of the investee's identifiable net assets, and the difference is charged to profit or loss.
- After the acquisition of the investment, the Group recognizes its share of the investee's net profit or loss, and the difference is charged to profit or loss are not quoted in an active market recognized by the Group before the first-time adoption of CAS, as investment income or losses, and adjusts the carrying amount of investment accordingly. The debit balance of the equity investment difference is amortized using the straight-line method over the period which is determined in accordance with previous accounting standards. Once the investee declares any cash dividends or profits distributions, the carrying amount of the investment is reduced by that attributable to the Group.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 12. Long-term equity investments *(Continued)*

#### (2) *Subsequent measurement and recognition of profit and loss (Continued)*

##### (b) Investment in jointly controlled enterprises and associates *(Continued)*

The Group recognizes its share of the investee's net profits or losses after making appropriate adjustments to align the accounting policies or accounting periods with those of the Group based on the fair values of the investee's identifiable net assets at the date of acquisition. Unrealized profits and losses resulting from transactions between the Group and its associates or jointly controlled enterprises are eliminated to the extent of the Group's interest in the associates or jointly controlled enterprises. Unrealized losses resulting from transactions between the Group and its associates or jointly controlled enterprises are eliminated in the same way as unrealized gains but only to the extent that there is evidence of impairment.

- The Group discontinues recognizing its share of net losses of the investee after the carrying amount of the long-term equity investment and any long-term interest that in substance forms part of the Group's net investment in the associate or the jointly controlled enterprises is reduced to zero, except to the extent that the Group has an obligation to assume additional losses. Where net profits are subsequently made by the associate or jointly controlled enterprises, the Group resumes recognizing its share of those profits only after its share of the profits equals the share of losses not recognized.
- For other changes of shareholders' equity other than net profits or losses of jointly controlled enterprises or associates, the Group adjusts the carrying amount of the long-term equity investment and recognizes it in shareholder's equity.

##### (c) Other long-term equity investments

Other long-term equity investments refer to investments where the Group does not have control, joint control or significant influence over the investees, and the investments are not quoted in an active market and their fair value cannot be reliably measured.

Other long-term equity investments are accounted for subsequently using the cost method. Cash dividends or profit distributions declared by subsidiaries and attributed to the Group shall be recognized as investment income (regardless of whether it is the net profit realized by investee before or after investment), except those that have been declared but unpaid at the time of acquisition and therefore included in the price paid or consideration.

#### (3) *Basis for determining the existence of joint control or significant influence over an investee*

Joint control is the contractual agreed sharing of control over an investee's economic activity, and exists only when the strategic financial and operating decisions relating to the activity require the unanimous consent of the parties sharing the control. The following evidences shall be considered when determining whether the Group can exercise joint control over an investee:

- no single investor is in a position to control the operating activities unilaterally;
- operating decisions relating to the investee's economic activity require the unanimous consent of the parties sharing the control;
- if the parties sharing the control appoint one investor as the operator or manager of the jointly controlled enterprises through the contractual arrangement, the operator must act within the financial and operating policies that have been agreed by the investors in accordance with the contractual arrangement.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 12. Long-term equity investments *(Continued)*

(3) *Basis for determining the existence of joint control or significant influence over an investee (Continued)*

Significant influence is the power to participate in the financial and operating policy decisions of an investee but is not control or joint control over those policies. The following one or more evidences shall be considered when determining whether the Group can exercise significant influence over an investee:

- representation on the board of directors or equivalent governing body of the investee;
- participation in policy-making processes;
- material transactions between the investor and the investee;
- interchange of managerial personnel;
- provision of essential technical information.

(4) *Method of impairment testing and measuring*

For the method of impairment testing and measuring for subsidiaries, jointly controlled enterprises and associates, refer to Note II. 19.

For other long-term equity investments, the carrying amount is required to be tested for Impairment at the balance sheet date. If there is objective evidence that the investments may be impaired, the impairment shall be assessed on an individual basis. The impairment loss is measured as the amount by which the carrying amount of the investment exceeds the present value of estimated future cash flows discounted at the current market rate on return for a similar financial asset. Such impairment loss is not reversed. The other long-term equity investments are stated at cost less impairment losses in the balance sheet at the end of the period.

### 13. Fixed assets

(1) *Recognition criteria for fixed assets*

Fixed assets represent the tangible assets held by the Group for use in the production of goods or for operation and administrative purposes with useful lives over one accounting year.

The cost of a purchased fixed asset comprises the purchase price, related taxes, and any directly attributable expenditure for bringing the asset to working condition for its intended use. The cost of self-constructed assets is measured in accordance with the policy set out in Note II. 14.

Where parts of an item of fixed asset have different useful lives or provide benefits to the Group in different patterns thus necessitating use of different depreciation rates or methods, each part is recognized as a separate fixed asset.

The subsequent costs including the cost of replacing part of an item of fixed assets are recognized in the carrying amount of the item if the recognition criteria are satisfied, and the carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing of fixed assets are recognized in profit or loss as incurred.

Fixed assets are stated in the balance sheet at cost less accumulated depreciation and impairment losses.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 13. Fixed assets *(Continued)*

#### (2) *Depreciation method for fixed assets*

Fixed assets are depreciated using the straight-line method over their estimated useful lives, except for those which meet the requirement as held-for-sale (refer to Note II. 26).

The depreciation period, residual value rate and annual depreciation rate of each type of fixed assets are as follows:

Type	Useful life (year)	Residual value rate (%)	Annual depreciation rate (%)
Buildings and structures	40 years	5%	2.38%
Machinery equipment	5 – 20 years	5%	4.75% – 19%
Transportation equipment	5 – 14 years	5%	6.78% – 19%
Electronic equipment	5 – 14 years	5%	6.78% – 19%

Useful lives, estimated residual values and depreciation methods are reviewed at least each year-end.

#### (3) *For the method of impairment testing and provision for impairment, refer to Note II.19.*

#### (4) *Recognition and measurement of fixed assets acquired under finance leases.*

For the recognition and measurement of fixed assets acquired under finance leases, refer to the accounting policy set out in Note II. 25 (2).

#### (5) *Disposal of fixed assets*

The carrying amount of a fixed asset shall be derecognized:

- on disposal; or
- when no future economic benefits are expected to be generated from its use or disposal.

Gains or losses arising from the retirement or disposal of an item of fixed asset are determined as the difference between the net disposal proceeds and the carrying amount of the item, and are recognized in profit or loss on the date of retirement or disposal.

### 14. Construction in progress

The cost of self-constructed fixed assets includes the cost of materials, direct labour, borrowing costs that meet the criteria for capitalization (see Note II.15), and any other costs directly attributable to bringing the asset to working condition for its intended use.

A self-constructed fixed asset is included in construction in progress before it is transferred to fixed assets when it is ready for its intended use. No depreciation is provided against construction in progress. Construction in progress is stated in the balance sheet at cost less provision for impairment (see Note II.19).

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 15. Borrowing costs

Borrowing costs incurred directly attributable to the acquisition, construction of a qualifying asset are capitalized as part of the cost of the asset.

Except for the above, other borrowing costs are recognized as financial expenses in the income statement when incurred.

During the capitalization period, the amount of interest (including amortization of any discount or premium on borrowing) to be capitalized in each accounting period is determined as follows:

- Where funds are borrowed specifically for the acquisition, construction of a qualifying asset, the amount of interest to be capitalized is the interest expense calculated using effective interest rates during the period less any interest income earned from depositing the borrowed funds or any investment income on the temporary investment of those funds before being used on the asset.
- Where funds are borrowed generally and used for the acquisition, construction of a qualifying asset, the amount of interest to be capitalized on such borrowings is determined by applying a capitalization rate to the weighted average of the excess amounts of cumulative expenditures on the asset over the above amounts of specific borrowings. The capitalization rate is the weighted average of the interest rates applicable to the general-purpose borrowings.

The effective interest rate is determined as the rate that exactly discounts estimated future cash flow through the expected life of the borrowing or, when appropriate, a shorter period to the initially recognized amount of the borrowings.

During the capitalization period, exchange differences related to the principal and interest on a specific-purpose borrowing denominated in foreign currency are capitalized as part of the cost of the qualifying asset. The exchange differences related to the principal and interest on foreign currency borrowings other than a specific-purpose borrowing are recognized as a financial expense in profit and loss in the period they are incurred.

The capitalization period is the period from the date of commencement of capitalization of borrowing costs to the date of cessation of capitalization, excluding any period over which capitalization is suspended. Capitalization of borrowing costs commences when expenditure for the asset is being incurred, borrowing costs are being incurred and activities of acquisition that are necessary to prepare the asset for its intended use are in progress, and ceases when the assets become ready for their intended use. Capitalization of borrowing costs is suspended when the acquisition, construction activities are interrupted abnormally and the interruption lasts for over three months.

### 16. Intangible assets

Intangible assets are stated in the balance sheet at cost less accumulated amortization and impairment losses (see Note II.19). Intangible asset's cost less residual value and impairment loss is amortized on the straight-line method over its estimated useful life, except that the intangible asset match the conditions of held for sale (refer to Note II.26). The respective amortization periods for such intangible assets are as follows:

Items	Amortization period
Land use rights	50 years
Various software	3 – 10 years
Others	5 – 10 years

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 16. Intangible assets *(Continued)*

Expenditures on an internal research and development project are classified into expenditures on the research phase and expenditures on the development phase. Expenditures on research phase are recognized in profit or loss when incurred. Expenditures on development phase are capitalized if development costs can be measured reliably, the product or process is technically and commercially feasible, and the Group intends to and has sufficient resources to complete development. Capitalized development costs are stated at cost less impairment losses (see Note II.19). Other development expenditures are recognized as expenses in the period in which they are incurred.

### 17. Goodwill

The initial cost of Goodwill caused by business combination not under common control is the excess of combination cost and the fair value of obtained identifiable net assets obtained from the acquiree.

Goodwill is not amortized. Goodwill is stated at cost less accumulated impairment losses in the balance sheet at the end of the period (see Note II.19). Goodwill is transferred when its related assets or assets group is disposed, and recognized in profit or loss for the period.

### 18. Long-term deferred expenses

Long-term deferred expenses are amortized in equal installments over the period that it enjoys benefits. Amortization periods for expenditures are:

Item	Amortization period
Decoration	5 years

### 19. Impairment of assets other than inventories, financial assets and other long-term equity investments

The carrying amounts of the following assets are reviewed at each balance sheet date based on the internal and external sources of information to determine whether there is any indication of impairment:

- Fixed assets
- Construction in progress
- Assets acquired under finance lease
- Intangible assets
- Long-term equity investments in subsidiaries, jointly controlled enterprises and associates
- Goodwill
- Long-term deferred expenses
- Other non-current assets etc.



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 19. Impairment of assets other than inventories, financial assets and other long-term equity investments *(Continued)*

If any indication exists that an asset may be impaired, the recoverable amount of the asset is estimated. In addition, whether impairment evidence exists, the Group assesses the recoverable amount of goodwill at the end of each year. The Group amortizes the book value of goodwill based on benefit from the synergies of the business combination on its related asset or combination of assets, and on this basis conducts impairment test for goodwill annually.

The recoverable amount of an asset, asset group or set of asset groups is the higher of its fair value less costs to sell and its present value of expected future cash flows.

An asset group is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or asset groups. An asset group is composed of assets directly relating to cash-generation. Identification of an asset group is based on whether major cash inflows generated by the asset group are largely independent of the cash inflows from other assets or asset groups. In identifying an asset group, the Group also considers how management monitors the Group's operations and how management makes decisions about using or disposing of the company's assets.

An asset's fair value less costs to sell is the amount determined by the price of a sale agreement in an arm's length transaction, less the costs that are directly attributable to the disposal of the asset. The present value of expected future cash flows of an asset is determined by discounting the future cash flows, estimated to be derived from continuing use of the asset and from its ultimate disposal, to their present value using a pre-tax discount rate.

If the result of the recoverable amount estimation indicates the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. That reduction is recognized as an impairment loss and charged to profit or loss for the current period. A provision for impairment loss of the asset is recognized accordingly. For impairment losses related to an asset group or a set of asset groups, first reduce the carrying amount of any goodwill allocated to the asset group or set of asset groups, and then reduce the carrying amount of the other assets in the asset group or set of asset groups on a pro rata basis. However, the carrying amount of an impaired asset will not be reduced below the highest of its individual fair value less costs to sell (if determinable), the present value of expected future cash flows (if determinable) and zero.

Once an impairment loss is recognized, it is not reversed in a subsequent period.

### 20. Provisions

A provision is recognized for an obligation related to a contingency if the Group has a present obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Where the effect of time value of money is material, provisions are determined by discounting the expected future cash flows.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 21. Revenue

Revenue is the gross inflow of economic benefit arising in the course of the Group's ordinary activities when the inflows result in increase in shareholder's equity, other than increase relating to contributions from shareholders. Revenue is recognized in profit or loss when it is probable that the economic benefits will flow to the Group, the revenue and costs can be measured reliably and the following respective conditions are met.

#### (1) *Sale of goods*

Revenue from sale of goods is recognized when all of the general conditions stated above and the following conditions are satisfied:

- The significant risks and rewards of ownership of goods have been transferred to the buyers;
- The Group retains neither continuing managerial involvements to the degree usually associated with ownership nor effective control over the goods sold.

Revenue from the sale of goods is measured at the fair value of the considerations received or receivable under the sales contract or agreement.

#### (2) *Rendering of services*

Revenue from rendering of services is measured at the fair value of the considerations received or receivable under the contract or agreement.

At the balance sheet date, where the outcome of a transaction involving the rendering of services can be estimated reliably, revenue from the rendering of services is recognized in the income statement by reference to the stage of completion of the transaction based on the progress of work performed or the ratio of cost happened to the proportion of total estimated cost.

Where the outcome of rendering of services cannot be estimated reliably, if the costs incurred are expected to be recoverable, revenues are recognized to the extent that the costs incurred that are expected to be recoverable, and an equivalent amount is charged to profit or loss as service cost; if the costs incurred are not expected to be recoverable, the costs incurred are recognized in profit or loss and no service revenue is recognized.

#### (3) *Interest income*

Interest income is recognized on a time proportion basis with reference to the principle and the applicable effective interest rate.

#### (4) *Royalty income of intangible assets*

Royalty income of intangible assets is calculated based on the agreed charging time and method in the relevant contract or agreement.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 22. Employee benefits

Employee benefits are all forms of considerations given and other relevant expenditures incurred in exchange for services rendered by employees. Except for termination benefits, employee benefits are recognized as a liability in the period in which the associated services are rendered by employees, with a corresponding increase in cost of relevant assets or expenses in the current period.

#### (a) *Social insurance benefit and housing fund*

Pursuant to relevant regulations of PRC, the Group has joined a social insurance system established and managed by the government organization. At the applicable rates based on the amounts stipulated by national government, the Group has joined housing fund and made contributions to the basic pension insurance, basic medical insurance, unemployment insurance, injury insurance and maternity insurance. The contributions to social insurance and housing fund mentioned above are recognized as cost of assets or charged to profit or loss on an accrual basis. The Group will have no further payment obligations after periodic contributions mentioned above pursuant to national regulations.

#### (b) *Termination benefits*

When the Group terminates the employment relationship with employees before the employment contracts have expired, or provides compensation as an offer to encourage employees to accept voluntary redundancy, a provision for the termination benefits provided, is recognized in profit or loss when both of the following conditions have been satisfied:

- The Group has a formal plan for the termination of employment or has made an offer to employees for voluntary redundancy, which will be implemented shortly.
- The Group is not allowed to withdraw from termination plan or redundancy offer unilaterally.

#### (c) *Early retirement benefits*

The early retirement is recognized only when the Group has clear commitment to provide benefits to the staff who initially retire early and the commitment cannot be withdrawn unilaterally. If the related payment is over one year and the amount is significant, the amounts should be measured at discounted value.

### 23. Government grants

Government grants are transfers of monetary assets or non-monetary assets from the government to the Group at no consideration except for the capital contribution from the government as an investor in the Group. Special funds such as investment grants allocated by the government, if clearly defined in official documents as part of “capital reserve” are dealt with as capital contributions, and not regarded as government grants.

A government grant is recognized when there is reasonable assurance that the grant will be received and that the Group will comply with the conditions attaching to the grant.

If a government grant is in the form of a transfer of a monetary asset, it is measured at the amount that is received or receivable. If a government grant is in the form of a transfer of a non-monetary asset, it is measured at its fair value.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 23. Government grants *(Continued)*

A government grant related to an asset is recognized initially as deferred income and amortized to profit or loss on a straight-line basis over the useful life of the asset. A grant that compensates the Group for expenses or losses to be incurred in the subsequent periods is recognized initially as deferred income and recognized in profit or loss in the same periods in which the expenses are recognized. A grant that compensates the Group for expenses or losses incurred is recognized in profit or loss immediately.

### 24. Deferred tax assets and liabilities

Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities and their tax bases, which include the deductible losses and tax credits carried forward to subsequent years. Deferred tax assets are recognized to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilized.

Deferred tax is not recognized for the temporary differences arising from the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting profit nor taxable profit (or deductible loss). Deferred tax is not recognised for taxable temporary differences arising from the initial recognition of goodwill.

At the balance sheet date, the carrying amount of deferred tax assets and liabilities are measured based on the expected manner of recovery or settlement of the carrying amount of the assets and liabilities, using tax rates that are expected to be applied in the period when the asset is recovered or the liability is settled in accordance with tax laws.

The carrying amount of a deferred tax asset is reviewed at each balance sheet date. The carrying amount of a deferred tax asset is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow the benefit of the deferred tax asset to be utilized. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profits will be available.

At the balance sheet date, deferred tax assets and liabilities are offset if all the following conditions are met:

- the taxable entity has the legal rights to settle the income tax assets and income tax liabilities for the current period by net amount;
- they relate to income taxes levied by the same tax authority on either the taxable entity has a legally enforceable right or set off current income tax assets against current income tax liabilities, and different taxable entities which either intend to settle the current income tax liabilities and assets on a net basis, or to realize the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred income tax liabilities or assets are expected to be settled or recovered.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 25. Operating and finance leases

A lease is classified as either a finance lease or an operating lease. A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of a leased asset to the lessee, irrespective of whether the legal title to the asset is eventually transferred or not. An operating lease is a lease other than a finance lease.

#### (1) *Operating lease charges*

Rental payments under operating leases are recognized as costs or expenses on a straight-line basis over the lease term.

#### (2) *Assets acquired under finance leases*

When the Group acquires an asset under a finance lease, the asset is measured at an amount equal to the lower of its fair values and the present value of the minimum lease payments, each determined at the inception of the lease. The minimum lease payments are recorded as long-term payables. The difference between the value of the leased assets and the minimum lease payments is recognized as unrecognized finance charges. Initial direct costs that are attributable to a finance lease incurred by the Group are added to the amounts recognized for the leased asset. Depreciation and impairment losses are accounted for in accordance with the accounting policies described in Notes II.13 (2) and II.19, respectively.

If there is a reasonable certainty that the Group will obtain ownership of a leased asset at the end of the lease term, the leased asset is depreciated over its estimated useful life. Otherwise, the leased asset is depreciated over the shorter of the lease term and its estimated useful life.

Unrecognized finance charge under finance lease is amortized using an effective Interest method over the lease term. The amortization is accounted for in accordance with policies of borrowing costs (see Note II.15).

At the balance sheet date, long-term payables arising from finance leases, net of the unrecognized finance charges, are presented into long-term liabilities and long-term liabilities due within one year.

### 26. Assets held for sale

The Group has resolved and signed a non-cancellable agreement on the transfer of the assets classified as held for sale with the transferee, and the transfer is expected to be completed within one year. Such non-current assets included fixed assets, intangible assets, investment property subsequently measured using the cost model, long-term equity investment (excluding financial assets and deferred income tax assets). Non-current assets held for sale are stated at the lower of carrying amount and net realisable value. Any excess of the carrying amount over the net realisable value is recognised as impairment loss. At the balance sheet date, non-current assets held for sale are presented into each asset item by category.

### 27. Profit distributions to shareholders

Dividends or distributions of profits proposed in the profit appropriation plan which will be considered and approved after the balance sheet date, are not recognized as a liability at the balance sheet date but disclosed in the notes separately.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 28. Related parties

If a party has the power to control, jointly control or exercise significant influence over another party, or where two or more parties are subject to common control, joint control or significant influence from another party, they are considered to be related parties. Related parties may be individuals or enterprises. Enterprises which is under common control only from the State and that have no other related party relationships are not regarded as related parties of the Group. Related parties of the Group and Company include, but are not limited to:

- (a) the Company's parent;
- (b) the Company's subsidiaries;
- (c) enterprises that are controlled by the Company's parent;
- (d) investors that have joint control or exercise significant influence over the Group;
- (e) enterprises or individuals under control, joint control or significant influence over with the Group;
- (f) jointly controlled enterprises of the Group, including subsidiaries of jointly controlled enterprises;
- (g) associates of the Group, including subsidiaries of associates;
- (h) principal individual investors and close family members of the Group;
- (i) key management personnel of the Group and close family members of such individuals;
- (j) key management personnel of the Company's parent;
- (k) close family members of key management personnel of the Company's parent; and
- (l) other enterprises that are controlled or jointly controlled by principal individual investors, key management personnel of the Group, and close family members of such individuals.

Besides the related parties stated above, determined in accordance with the requirements of CAS, the following enterprises and individuals are considered as (but not restricted to) relate parties of the Group or Company based on the requirements of Administrative Procedures on the Information Disclosures of Listed Companies issued by the CSRC:

- (m) enterprises or persons that act in concert that hold 5% or more of the Company's shares;
- (n) individuals and close family members of such individuals who directly or indirectly hold 5% or more of the Company's shares, supervisors for listed companies and their close family members;
- (o) enterprises that satisfy any of the aforesaid conditions in (a), (c) and (m) during the past 12 months or will satisfy them within the next 12 months pursuant to a relevant agreement;
- (p) individuals who satisfy any of the aforesaid conditions in (i), (j) and (n) during the past 12 months or will satisfy them within the next 12 months pursuant to a relevant agreement; and
- (q) enterprises, other than the Company and subsidiaries controlled by the Company, which are controlled directly or indirectly by an individual defined in (i), (j), (n) or (p), or in which such an individual assumes the position of a director or senior executive.

### 29. Segment reporting

The Group determines the operating segments on the basis of internal structure, management requirements and internal reporting system, and determines reporting segments based on the operating segments. An operating segment is a component of the Group that meets the following criteria:

- that may earn revenue and incur expenses in daily business activities;
- whose operating results are regularly reviewed by the Group's management to allocate its resources and assess its performance;
- for which discrete financial information on financial positions, operating results and cash flow is available to the Group;

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 29. Segment reporting *(Continued)*

Two or more operating segments can be aggregated into one operating segment if the segments have similar economic characteristics and the segments are similar in each of the following respects:

- the nature of each product and service;
- the nature of production process;
- the type or class of customers for their products and services;
- the methods used to distribute their products or provide their services;
- the influence brought by law, administrative regulations on production of products and provision of services.

Inter-segment revenues are measured on the basis of actual transaction price for such transactions for segment reporting, and segment accounting policies are consistent with those used for the preparation of financial statements of the Group.

### 30. Significant accounting estimates and judgments

The preparation of financial statements requires management to make estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Key assumptions and judgments on uncertainties related to estimates are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised and in any future periods affected.

Aparting the information of risk factors and fair value assumption of the impairment of goodwill, termination benefits and financial instruments contained in Notes V. 11, 21 and Note X. 3, other key sources of estimation uncertainty are as follows:

#### (a) *Impairment of receivables*

As described in Note II.10, receivables that are measured at amortization cost are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, impairment loss is provided. Objective evidence of impairment includes observable data that comes to the attention of the Group about loss events such as a significant decline in the estimated future cash flow of an individual debtor or the portfolio of debtors, and significant changes in the financial condition that have an adverse effect on the debtor. If there is an indication that the receivables has recovered to its value and is related to the events occurred after the recognition of the loss, the impairment loss recognized in prior years is reversed.

#### (b) *Provision for diminution of inventory cost*

As stated in Note II. 11, the Group estimates the net realisable value of inventories periodically and recognize the excess of inventory cost over its net realizable value as diminution of inventory cost. When making estimation of the realizable value of inventories, the Group considers the purpose of holding the inventory based on available information including its market price and previous operation costs of the Group. The actual selling price, production costs and sales expenses and taxes may vary with sales status, production technologies or the actual usage of the inventories and the provision for diminution of inventory cost may change accordingly. The adjustments to the provision for diminution of inventory cost will have effects upon the profit and loss for the period of change in estimation.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (II). SIGNIFICANT ACCOUNTING POLICIES OF THE COMPANY AND ACCOUNTING ESTIMATES *(Continued)*

### 30. Significant accounting estimates and judgments *(Continued)*

- (c) *Impairment of other assets excluding inventories, financial assets and other long-term equity investments*

As described in Note II.19, other assets excluding inventories, financial assets and other long-term equity investments are reviewed at each balance sheet date to determine whether the carrying amount exceeds the recoverable amount of the assets. If there are indications that the carrying amount of the long-term asset cannot be recovered, the asset is impaired and impairment loss is provided.

The recoverable amount of an asset (asset group) is the greater of its fair value net of selling price and its present value of expected future cash flows. Since the market price of the asset (the asset group) cannot be obtained reliably, the fair value of the asset cannot be estimated reliably. In assessing the present value of expected future cash flows, significant judgments are exercised over the asset's production volume, selling price, related operating expenses and discounting rate to calculate the present value. All relevant materials which can be obtained are used for estimation of the recoverable amount, including the estimation of the production volume, selling price and related operating expenses based on reasonable and supportable assumption.

- (d) *Depreciation and amortization of fixed assets and intangible assets*

As described in Notes II.13 and 16, fixed assets and intangible assets are depreciated and amortized using the straight-line method over their useful lives after taking into account residual value. The estimated useful lives are regularly reviewed to determine the depreciation and amortization costs charged in each reporting period. The useful lives are determined based on historical experience of similar assets and estimated technical changes. If there is an indication that there has been a change in the factors used to determine the depreciation or amortization, the amount of depreciation or amortization is revised.

- (e) *Product quality warranty*

As described in Note V. 25, according to recent maintenance experience, the Group has made provisions for providing after-sales quality maintenance to its customers on the sales of machine tool products. Since the recent maintenance experience might not reflect the maintenance information for sold products in the future, the management needs to apply more judgments to estimate the provisions. The increase or decrease of the provisions will affect the profit or loss in the future year.



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (III). TAXATION

### 1. Major types of tax and tax rates

Types	Tax basis	Tax rate
VAT	In accordance with Tax Law, tax on sales of goods or taxable service income for the period after deducting the current allowed deduction of tax, the balance should be the taxable VAT in accordance with the policies	17%
Business tax	In accordance with taxable operating income	3%-5%
City construction tax	In accordance with actual business tax paid and VAT payable	1%-7%
Education fee surcharges	In accordance with actual business tax paid and VAT payable	3%
Local education surcharges	In accordance with actual business tax paid and VAT payable	2%
Enterprise income tax	In accordance with Income tax payable	Note

*Note:* The applicable rate of income tax for 2011 of the Company and the Company's subsidiary Xi'an Ser Turbo Machinery Manufacturing Co., Ltd (Xi'an Ser) and Changsha Ser Turbo Equipment Co., Ltd. (Changsha Ser) is 15% (2010: 15%) and the applicable rate of income tax of other subsidiaries for 2011 is 25% (2010: 25%).

### 2. Preferential tax policies and approvals

Based on Notice [2007] No.183 dated 25th December 2007 issued by the Kunming State Tax Bureau, CNC machine tool production the Company engaged in is an encouraged industry. Therefore, during the period from 2004 to 2010, if the Company's annual sales income of CNC machine tool products is over 70% of total sales income, the Company was entitled to a applicable corporate income tax rate of 15% under the Preferential Tax Policies for the Extensive Development of the Western Region. In 2010, as the sales of CNC machine tool products exceeded the above limit, the preferential tax rate of 15% is applicable for the Company.

As at 27th July 2011, Ministry of Finance, China Custom and State Administration of Taxation jointly issued the Notice Issues on Tax Policies for the Implementation of the Strategy Further Exploration and Development of the Western Region (Cai Shui [2011] No. 58), according to which, from 1st January 2011 to 31st December 2020, the enterprises of encouraged industries established in the Western regions are subject to an income tax rate of 15%. The enterprises of encouraged industries are the enterprises whose major businesses are those listed in the Encouraged Industries Catalog in the Western Region and whose major operation income are over 70% of its total income. The Company is an enterprise of encouraged industries and applied to Kunming State Taxation bureau for an income tax of 15% commencing from 2011. In March 2012, the application was approved by Kunming State Taxation Bureau and the applicable tax rate for 2011 is 15%.

The subsidiaries of the Company, Xi'an Ser and Changsha Ser are certified as Advanced and New Technology Enterprise and the expiry dates of the certification are 9th October 2014 and 31st December 2011 respectively. Pursuant to relevant laws and regulations of China, the preferential enterprise income tax rate for 2011 is 15% (2010: 15%).

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (IV). BUSINESS COMBINATION AND CONSOLIDATED FINANCIAL STATEMENTS

### 1. Background of major subsidiaries

(1) *Subsidiaries acquired through establishment or investment*

Full name	Type of subsidiaries	Type of enterprise	Place of registration	Business nature and scope of business	Organization code	Registered capital	Actual capital contribution at the end of the year	Proportion of shareholding (%)	Proportion of voting rights (%)	Consolidated statements	Minority interests at the end of the year (RMB)	Reversal of minority loss interest from minority interest (RMB)
Fujian Kunji Conventional Machine Tool Co., Ltd. ("Fujian Kunji") (note 1)	Non-controlling subsidiaries	Company with limited liabilities	China	Development, design, production and sales of machine tool series products and accessories	67190471-3	RMB5,000,000	RMB5,000,000	50%	60%	Yes	-398,670.20	615,965.13
Kunming Kunji General Machine Co., Ltd. ("General Machine") (note 2)	Wholly-owned subsidiaries	Company with limited liabilities	China	Development, design, production and sales of machine tool series products and accessories	665546112	RMB3,000,000	RMB3,000,000	100%	100%	Yes	-	-

Note 1: The percentage of voting rights of the Group in Fujian Kunji is determined by the percentage of total voting rights of the Group in the board of directors of Fujian Kunji. Fujian Kunji was consolidated due to the fact that the Group has gained control over its financial and operational decision making.

The resolution regarding the disposal of Fujian Kunji was passed at the board meeting held on 19th November 2010. On 21st March 2012, the Group entered into an equity transfer agreement with Fujian Chenggong Machine Tool Co., Ltd. to transfer its share interest in Fujian Kunji at a consideration of RMB1,000,000.

Note 2: The resolution regarding the dissolution of General Machine was passed at the board meeting held on 19th October 2010. As at the date of this financial statement, according to the requirements under relevant laws and regulations, the liquidation is still processing.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (IV). BUSINESS COMBINATION AND CONSOLIDATED FINANCIAL STATEMENTS

(Continued)

### 1. Background of major subsidiaries (Continued)

(2) Subsidiaries acquired from business combination not under common control

Full name	Type of subsidiaries	Type of enterprise	Place of registration	Business nature and scope of business	Organization code	Registered capital	Actual capital contribution at the end of the year	Proportion of shareholding (%)	Proportion of voting rights (%)	Consolidated statements	Reversal of minority interest	
											Minority interests at the end of the year (RMB)	loss interest from minority interest (RMB)
Xi'an Ser (note)	Non-controlling subsidiaries	Company with limited liabilities	China	Development, design, production and sales of compressor series products and accessories	22063182-4	RMB 50,000,000	RMB 50,000,000	45%	60%	Yes	53,844,091.02	2,076,855.87
Changsha Ser	Non-controlling subsidiaries	Company with limited liabilities	China	Development, design, production and sales of compressor series products and accessories	75801180-3	RMB 10,000,000	RMB 10,000,000	100%	100%	Yes	-	-
Hangzhou Ser Gas Engineering Co., Ltd. ("Hangzhou Ser")	Non-controlling subsidiaries	Company with limited liabilities	China	Development, design, production and sales of compressor series products and accessories	759548450	RMB 1,200,000	RMB 1,200,000	51%	51%	Yes	1,101,027.88	(341,304.27)

Note: The percentage of voting rights of the Group in Xi'an Ser is determined by the percentage of voting rights of the Group in the board of directors of Xi'an Ser. Xi'an Ser was consolidated due to the fact that the Group has gained control over its financial and operational decision making.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (IV). BUSINESS COMBINATION AND CONSOLIDATED FINANCIAL STATEMENTS

(Continued)

### 2. Explanation to the change of scope of consolidation of the Company

Winko Machines Co., Ltd. ("Winko") convened an extraordinary general meeting of 2008 on 30th June 2008, at which a resolution regarding the dissolution of Winko was considered and passed, and a liquidation team comprising all shareholders was established. As at 28th February 2011, the liquidation team has completed the cancellation procedures. The operating results of Winko from 1st January 2011 to the date of cancellation have been consolidated into the Group's consolidated income statement.

A board meeting of Kunji Transportation Company Limited ("Kunji Transportation") was held on 24th March 2010, at which a resolution regarding the dissolution of Kunji Transportation was passed, and a liquidation team comprising all shareholders of Kunji Transportation was established to liquidate the company. As at 10th June 2011, the liquidation team has completed the cancellation procedures. The operating results of Kunji Transportation from 1st January 2011 to the date of cancellation have been consolidated into the Group's consolidated income statement.

### 3. Entities no longer consolidated in the Company during the reporting period

(1) *Subsidiaries no longer consolidated in the Company during the year*

*Unit: RMB*

Name	Note	At 31st December 2010			From 1st January 2011 to the date of cancellation		
		Total assets	Total liabilities	Total shareholders' equity	Operating income	Operating cost and expenses	Net profit
Winko	(IV).2	2,913,631.67	12,773,440.27	(9,859,808.60)	-	(9,859,808.60)	9,859,808.60
Kunji Transportation	(IV).2	1,132,398.09	(28,415.55)	1,160,813.64	-	10,526.75	(10,526.75)

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

### 1. Cash at bank and on hand

Item	Original currency	2011		Original currency	2010	
		Exchange rate	RMB/RMB equivalents		Exchange rate	RMB/RMB equivalents
Cash on hand:	-	-	503,574.06	-	-	1,107,200.04
RMB	-	-	461,601.60	-	-	1,062,540.52
HKD	5,137.07	0.8107	4,161.03	5,132.64	0.8509	4,367.36
USD	2,866.46	6.3009	18,059.32	2,866.15	6.6227	18,981.66
EUR	2,420.30	8.1625	19,752.11	2,419.86	8.8065	21,310.50
Cash at bank:	-	-	175,304,445.56	-	-	284,775,074.33
RMB	-	-	159,138,846.02	-	-	263,142,585.74
HKD	8,916,284.47	0.8107	7,228,431.82	8,908,215.67	0.8509	7,580,000.71
USD	1,405,490.18	6.3009	8,855,851.43	2,118,260.00	6.6227	14,028,600.51
EUR	9,962.71	8.1625	81,316.29	2,712.47	8.8065	23,887.37
Deposits with banks	-	-	16,392,311.03	-	-	10,412,135.19
RMB	-	-	16,392,311.03	-	-	10,412,135.19
<b>Total</b>	<b>-</b>	<b>-</b>	<b>192,200,330.65</b>	<b>-</b>	<b>-</b>	<b>296,294,409.56</b>

Unit: RMB

As at 31st December 2011, security deposit of RMB16,392,311.03 (at 31st December 2010: RMB10,412,135.19) is pledged for the Group's bank guarantee and bank acceptance note.

### 2. Bills receivable

(1) Classification of bills receivable

Type	2011	2010
Bank acceptance notes	104,034,946.22	115,906,620.42
Total	104,034,946.22	115,906,620.42

Unit: RMB

The above bills receivable are due within one year.

None of the above bills receivable was due from shareholders holding over 5% (or 5%) shares of the Company entitling voting rights.

(2) At as the end of the year, no bills receivable was pledged.

(3) At as the end of the year, no bills receivable was transferred to accounts receivable due to non-performance of the issuers.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 3. Accounts receivable

(1) Analysis of accounts receivable by the type of customers:

Type of customers	2011	Unit: RMB
		2010
Third party	461,679,432.22	370,560,565.08
Related party	6,094,433.84	6,641,213.38
Subtotal	467,773,866.06	377,201,778.46
Less: provision for bad and doubtful debts	182,828,343.15	127,372,966.78
Total	<u>284,945,522.91</u>	<u>249,828,811.68</u>

(2) Ageing analysis of accounts receivable:

Ageing	2011	Unit: RMB
		2010
Within one year (including one year)	160,235,520.22	157,919,643.52
1-2 years (including two years)	131,994,960.49	94,062,730.36
2-3 years (including three years)	73,342,118.82	58,560,347.76
Over three years	102,201,266.53	66,659,056.82
Subtotal	467,773,866.06	377,201,778.46
Less: provision for bad and doubtful debts	182,828,343.15	127,372,966.78
Total	<u>284,945,522.91</u>	<u>249,828,811.68</u>

The ageing of accounts receivable is calculated starting from the date of recognition.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 3. Accounts receivable (Continued)

(3) Analysis of accounts receivable by category

Unit: RMB

Type	Note	2011		2010		2011		2010	
		Carrying amount	Provision for bad and doubtful debts	Carrying amount	Provision for bad and doubtful debts	Carrying amount	Provision for bad and doubtful debts	Carrying amount	Provision for bad and doubtful debts
		Amount	Amount	Amount	Amount	Amount	Amount	Amount	Amount
			(%)		(%)		(%)		(%)
Individually significant and assessed individually for impairment	(4)	89,372,562.83	19.11	12,612,691.31	14.11	24,260,424.16	6.43	3,587,513.37	14.79
Collectively assessed for impairment*									
Group 1	(5)	372,306,869.39	79.59	170,215,651.84	45.72	346,300,140.92	91.81	123,785,453.41	35.75
Group 2	(10)	6,094,433.84	1.30	-	-	6,641,213.38	1.76	-	-
Sub-total		<u>378,401,303.23</u>	<u>80.89</u>	<u>170,215,651.84</u>	<u>44.98</u>	<u>352,941,354.30</u>	<u>93.57</u>	<u>123,785,453.41</u>	<u>35.07</u>
Total		<u>467,773,866.06</u>	<u>100</u>	<u>182,828,343.15</u>	<u>-</u>	<u>377,201,778.46</u>	<u>100.00</u>	<u>127,372,966.78</u>	<u>-</u>

Note\*: This category included accounts receivable having been individually assessed but not impaired.

The Group did not receive any collateral for the above accounts receivable with provision for bad and doubtful debt.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 3. Accounts receivable (Continued)

(4) Individually significant accounts receivable with individual bad debt provision as at the end of the year:

Unit: RMB

Type	Carrying amount	Provision for bad and doubtful debts	Proportion	Reasons for making provision
Accounts receivable	89,372,562.83	12,612,691.31	14.11%	Impairment occurred under individual assessment method

(5) Provisions for accounts receivable in groups using ageing analysis method:

Unit: RMB

Ageing	2011		Provision for bad and doubtful debts	2010		Provision for bad and doubtful debts
	Carrying amount			Carrying amount		
	Amount	Proportion (%)		Amount	Proportion (%)	
Within one year	108,521,429.37	29.15	5,624,619.36	136,515,974.61	39.42	6,634,274.66
1-2 years	97,708,010.38	26.24	29,312,403.11	84,564,761.73	24.42	25,280,595.90
2-3 years	63,876,163.11	17.16	38,282,426.17	58,560,347.76	16.91	30,146,178.87
Over 3 years	102,201,266.53	27.45	96,996,203.20	66,659,056.82	19.25	61,724,403.98
Total	<u>372,306,869.39</u>	<u>100.00</u>	<u>170,215,651.84</u>	<u>346,300,140.92</u>	<u>100.00</u>	<u>123,785,453.41</u>

(6) During the year, no significant bad debt provision for the accounts receivable was reversed or collected.

(7) During the year, there was no significant writing-off for the accounts receivable.



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 3. Accounts receivable (Continued)

(8) Amount of top five accounts receivable:

Debtor	Relationship with the Company	Amount	Ageing	Unit: RMB Percentage of total accounts receivable (%)
1st	Third party	27,227,757.01	Within one year	5.82
2nd	Third party	22,516,000.00	Over one year	4.81
3rd	Third party	14,224,317.81	Over one year	3.04
4th	Third party	9,936,000.00	Within one year	2.12
5th	Third party	8,177,400.00	Within one year	1.75
Total		<u>82,081,474.82</u>		<u>17.54</u>

As names of customers are confidential commercial information of the Group, we did not disclose the specific names of the top five customers. None of the above accounts receivables was due from shareholders holding over 5% (or 5%) shares of the Company entitling voting rights.

(9) Accounts receivables due from related parties

Debtor	Notes	Relationship with the Company	Amount	Unit: RMB Percentage of total accounts receivable (%)
Kunming TOS Machine Tool Company Limited ("Kunming TOS")	6	Jointly controlled enterprise	6,085,433.84	1.30
Yunnan CY Group Co., Ltd., Products Trading Center ("Trading Center")	6	Subsidiary of the largest shareholder of the Company	9,000.00	0.00
Total			<u>6,094,433.84</u>	<u>1.30</u>

(10) Credit policy

The account receivables of the Group were mainly in the form of deposit for warranty, which generally would due after one year of installation of the products according to the sales contracts entered into with customers. Except for deposit for warranty, all payments are payable by the end of the negotiated credit term. The Group would grant credit term of one to three months in general to customers according to their payment records and transaction performance.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 4. Other receivables

(1) Analysis of other receivables by the type of customers:

Type of customers	Unit: RMB	
	2011	2010
Third party	17,520,895.29	18,715,559.32
Related party	930,594.93	233,675.62
Sub-total	18,451,490.22	18,949,234.94
Less: provision for bad debt	4,221,633.89	2,330,005.85
Total	<u>14,229,856.33</u>	<u>16,619,229.09</u>

(2) Ageing analysis of other receivables:

Ageing	Unit: RMB	
	2011	2010
Within one year (including one year)	13,181,557.63	13,345,690.13
1-2 years (including two years)	2,870,339.98	3,568,072.43
2-3 years (including three years)	765,174.94	1,010,308.30
Over three years	1,634,417.67	1,025,164.08
Sub-total	18,451,490.22	18,949,234.94
Less: provision for bad debt	4,221,633.89	2,330,005.85
Total	<u>14,229,856.33</u>	<u>16,619,229.09</u>

The ageing of other receivables is calculated starting from the date of recognition.

(3) Analysis of other receivables by category:

Type	Note	2011				2010			
		Carrying amount		Provision for bad and doubtful debts		Carrying amount		Provision for bad and doubtful debts	
		Amount	Proportion (%)	Amount	Proportion (%)	Amount	Proportion (%)	Amount	Proportion (%)
Individually significant and assessed individually for impairment	(4)	1,014,793.03	5.50	664,785.54	65.51	14,860,741.53	78.42	1,075,379.21	7.24
Collectively assessed for impairment*									
Group 1	(5)	16,506,102.26	89.46	3,556,848.35	21.55	3,854,817.79	20.35	1,254,626.64	32.55
Group 2	(10)	930,594.93	5.04	-	-	233,675.62	1.23	-	-
Sub-total		17,436,697.19	94.50	3,556,848.35	20.40	4,088,493.41	21.58	1,254,626.64	30.69
Total		<u>18,451,490.22</u>	<u>100.00</u>	<u>4,221,633.89</u>	<u>-</u>	<u>18,949,234.94</u>	<u>100.00</u>	<u>2,330,005.85</u>	<u>-</u>

Note\*: This category included other receivables having been individually assessed but not impaired.

The Group did not received any collateral for the above other receivables with provision for bad and doubtful debt.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 4. Other receivables (Continued)

(4) Individually significant other receivables with individual bad debt provision as at the end of the year,:

Unit: RMB

Type	Carrying amount	Provision for bad and doubtful debts	Proportion	Reasons for making provision
1. Borrowings of staff	1,014,793.03	664,785.54	65.51	Impairment occurred under individual assessment method

(5) Other receivables in groups with provision for bad and doubtful debts using ageing analysis method:

Unit: RMB

Ageing	2011			2010		
	Carrying amount	Proportion (%)	Provision for bad and doubtful debts	Carrying amount	Proportion (%)	Provision for bad and doubtful debts
Within one year	11,935,165.34	72.31	591,571.89	2,732,355.77	70.88	235,284.19
1-2 years	2,770,339.98	16.78	1,164,679.52	206,239.15	5.35	103,119.58
2-3 years	765,174.94	4.64	765,174.94	44,808.79	1.16	44,808.79
Over 3 years	1,035,422.00	6.27	1,035,422.00	871,414.08	22.61	871,414.08
Total	16,506,102.26	100.00	3,556,848.35	3,854,817.79	100.00	1,254,626.64

(6) During the year, no significant bad debt provision for the other receivables was reversed or collected.

(7) During the year, there was no significant writing-off for the other receivables.

(8) Amount of top five other receivables

Unit: RMB

Debtor	Relationship with the Company	Amount	Ageing	Percentage of total receivable (%)
Sany Heavy Industry Co., Ltd.	Third party	1,752,000.00	Over one year	9.50
Shenyang Fantian Brand Management Co., Ltd.,	Third party	1,200,400.00	Over one year	6.51
Kunming TOS	Jointly controlled enterprise	930,594.93	Within one year	5.04
Henan Runlong Commercial Trading Co., Ltd.	Third party	580,000.00	Within one year	3.14
China National Technical Import and Export Corporation	Third party	571,000.00	Within one year	3.09
Total	-	5,033,994.93	-	27.28

(9) None of the above other receivables was due from shareholders holding over 5% (or 5%) shares of the Company entitling voting rights.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 4. Other receivables (Continued)

(10) Other receivables due from related parties

Debtor	Notes	Relationship with the Company	Amount	Unit: RMB
				Percentage of total other receivable (%)
Kunming TOS	VI. 6	Jointly controlled enterprise	930,594.93	5.04

As at 31st December 2011, the Group conducted individual assessment on other receivables due from related parties and considered that there was no need to make provisions for doubtful and bad debts.

### 5. Prepayments

(1) Prepayments by category

Item	Unit: RMB	
	2011	2010
Prepayment for materials	79,699,344.86	53,337,722.23

(2) Ageing analysis of prepayments

Ageing	Unit: RMB			
	Amount	2011 Proportion (%)	Amount	2010 Proportion (%)
Within one year (including one year)	74,758,304.84	93.80	23,767,550.55	44.56
1-2 years (including 2 years)	1,188,237.42	1.49	14,229,912.34	26.68
2-3 years (including 3 years)	639,125.00	0.80	12,464,467.74	23.37
Over 3 years	3,113,677.60	3.91	2,875,791.60	5.39
Total	<u>79,699,344.86</u>	<u>100.00</u>	<u>53,337,722.23</u>	<u>100.00</u>

The ageing of prepayments is calculated starting from the date of recognition.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 5. Prepayments (Continued)

(3) Amount of top five prepayments

Unit: RMB

Debtor	Relationship with the Company	Amount	Percentage of total prepayments (%)	Prepayment time	Reasons for non-settlement
Hangzhou Chinen Steam Turbine Power Co., Ltd	The third party	23,208,956.35	29.12	Within one year	Prepayment for materials undue
Siemens International Trading (Shanghai) Co. Ltd. 德國瓦格納技術製造有限公司	The third party	18,201,722.10	22.84	Within one year	Prepayment for materials undue
	The third party	3,416,378.60	4.29	Within one year	Prepayment for materials undue
Yunnan Jet Get International Logistics Co., Ltd.	The third party	2,898,944.26	3.64	Within one year	Prepaid transportation expenses
East Fuhui Machine Equipment (Beijing) Co., Ltd.	The third party	2,619,000.00	3.29	Within one year	Prepayment for materials undue
Total		50,345,001.31	63.18		

(4) None of the above prepayments was made to shareholders holding over 5% (or 5%) shares of the Company entitling voting rights.

### 6. Inventories

(1) Inventories by category

Unit: RMB

Item	Book value	2011 Provision for diminution in value of inventories	Carrying amount	Book Value	2010 Provision for diminution in value of inventories	Carrying amount
Raw materials	136,500,099.11	3,065,619.64	133,434,479.47	117,321,473.22	3,065,619.64	114,255,853.58
Turnover materials	6,096,567.83	82,781.00	6,013,786.83	5,358,146.97	82,781.00	5,275,365.97
Work in progress	506,056,400.92	10,435,282.97	495,621,117.95	435,732,995.40	5,898,283.82	429,834,711.58
Inventory of goods	334,943,612.36	2,684,150.37	332,259,461.99	200,248,281.45	2,684,150.37	197,564,131.08
Commissioned processing materials	16,350,544.28	–	16,350,544.28	5,845,948.61	–	5,845,948.61
Total	999,947,224.50	16,267,833.98	983,679,390.52	764,506,845.65	11,730,834.83	752,776,010.82

As at 31st December 2011, no inventory was pledged (2010: nil) by the Group.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 6. Inventories (Continued)

(2) An analysis of the movements of inventories for the year is as follows:

Item	Unit: RMB			
	Opening balance	Increase during the year	Decrease during the year	Closing balance
Raw materials	117,321,473.22	1,257,469,742.82	1,238,291,116.93	136,500,099.11
Consumables	5,358,146.97	19,678,543.06	18,940,122.20	6,096,567.83
Work in progress	435,732,995.40	1,560,784,156.15	1,490,460,750.63	506,056,400.92
Finished goods	200,248,281.45	1,496,086,203.25	1,361,390,872.34	334,943,612.36
Goods in transit	-	2,030,852.27	2,030,852.27	-
Commissioned processing of materials	5,845,948.61	87,054,241.40	76,549,645.73	16,350,544.28
Sub-total	764,506,845.65	4,423,103,738.95	4,187,663,360.10	999,947,224.50
Less: Provision for diminution in value of inventories	11,730,834.83	4,536,999.15	-	16,267,833.98
Total	<u>752,776,010.82</u>	<u>4,418,566,739.80</u>	<u>4,187,663,360.10</u>	<u>983,679,390.52</u>

(3) Provision for diminution in value of inventories

Item	Unit: RMB			Closing balance
	Opening balance	Provision made for the year	Written back during the year	
Raw materials	3,065,619.64	-	-	3,065,619.64
Consumables	82,781.00	-	-	82,781.00
Work in progress	5,898,283.82	4,536,999.15	-	10,435,282.97
Finished goods	2,684,150.37	-	-	2,684,150.37
Total	<u>11,730,834.83</u>	<u>4,536,999.15</u>	<u>-</u>	<u>16,267,833.98</u>

### 7. Long-term equity investments

(1) Long-term equity investment by category:

Item	Unit: RMB	
	2011	2010
Investments in jointly controlled enterprises	47,500,223.66	45,965,425.09
Investments in associates	14,424,357.29	14,624,334.06
Other long-term equity investments	2,000,000.00	2,000,000.00
Sub-total	63,924,580.95	62,589,759.15
Less: impairment provision	2,000,000.00	2,000,000.00
Total	<u>61,924,580.95</u>	<u>60,589,759.15</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 7. Long-term equity investments (Continued)

(2) Movements of long-term equity investment during the year:

Unit: RMB

Invested company	Investment cost	Opening balance	Increase/Decrease	Closing balance	Shareholding in the invested company (%) (A)	Percentage (%) of voting rights in the invested company (B)	Explanation for discrepancy between (A) and (B)	Impairment provision	Impairment provision made during the year	Cash dividend for the year
Under equity method:										
jointly controlled enterprise										
Kunming TOS	24,739,533.99	45,965,425.09	1,534,798.57	47,500,223.66	50.00	50.00	N/A	-	-	6,000,000.00
Under equity method:										
associate										
Xi'an Ruite Laser Prototyping Manufacturing & Engineering Research Co., Ltd. ("Xi'an Ruite")										
	14,000,000.00	14,624,334.06	-199,976.77	14,424,357.29	23.34	23.34	N/A	-	-	-
Under cost method:										
other long-term equity investment										
Yunnan Cheng Jiang Copper Products Plant (note)										
	2,000,000.00	2,000,000.00	-	2,000,000.00	40.00	40.00	N/A	2,000,000.00	-	-
<b>Total</b>	<b>40,739,533.99</b>	<b>62,589,759.15</b>	<b>1,334,821.80</b>	<b>63,924,580.95</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>2,000,000.00</b>	<b>-</b>	<b>6,000,000.00</b>

Note: Full provision for impairment loss on long-term investment of Yunnan Cheng Jiang Copper Products Plant was made in 1999 because the plant has lost the ability of sustainable operation. In 2009, as approved at the 7th meeting of the six session of the Board of the Company, the Company began to dispose of such investment. As at the date of the financial statement, the process of disposal is still in progress.

(3) Information of major jointly controlled enterprises and associates:

Unit: RMB

Invested companies	Total assets at the end of the year	Total liabilities at the end of the year	Total net assets at the end of the year	Total operating income for the year	Net profit/loss for the year
1. Jointly controlled enterprise Kunming TOS	185,521,782.26	90,543,380.98	94,978,401.28	110,051,567.63	15,069,597.14
2. Associate Xi'an Ruite	131,077,102.67	68,960,051.82	62,117,050.85	36,402,278.08	(857,043.29)

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 8. Fixed assets

(1) Details of fixed assets

Item					Unit: RMB
	Building and structures	Machinery and equipment	Transportation equipment	Electronic equipment	Total
Cost					
Opening balance	317,747,337.11	395,778,475.89	39,318,399.86	39,702,335.94	792,546,548.80
Re-classification and adjustment	4,218,470.99	33,617,232.02	(12,260,017.50)	(25,575,685.51)	-
Addition during the year	225,006.00	30,290,872.01	4,747,697.80	1,977,119.08	37,240,694.89
Transfer from construction in progress	9,750,417.07	54,571,384.10	778,290.60	-	65,100,091.77
Disposal during the year	(17,458.00)	(4,091,449.41)	(24,300.00)	(1,179,118.50)	(5,312,325.91)
Closing balance	331,923,773.17	510,166,514.61	32,560,070.76	14,924,651.01	889,575,009.55
Accumulated depreciation					
Opening balance	70,316,522.35	192,650,072.26	16,057,516.20	22,965,468.97	301,989,579.78
Re-classification and adjustment	265,032.88	16,746,676.22	(2,980,679.00)	(14,031,030.10)	-
Charge for the year	8,534,106.07	26,304,135.54	2,781,256.78	1,938,310.44	39,557,808.83
Written off during the year	(16,759.68)	(3,303,141.15)	(23,327.99)	(1,118,879.24)	(4,462,108.06)
Closing balance	79,098,901.62	232,397,742.87	15,834,765.99	9,753,870.07	337,085,280.55
Impairment provision					
Opening balance	-	3,581,706.76	-	127,337.28	3,709,044.04
Re-classification and adjustment	-	24,987.20	-	(24,987.20)	-
Written off on disposal	-	(664.28)	-	-	(664.28)
Closing balance	-	3,606,029.68	-	102,350.08	3,708,379.76
Carrying amounts					
At the end of the year	<u>252,824,871.55</u>	<u>274,162,742.06</u>	<u>16,725,304.77</u>	<u>5,068,430.86</u>	<u>548,781,349.24</u>
At the beginning of the year	<u>247,430,814.76</u>	<u>199,546,696.87</u>	<u>23,260,883.66</u>	<u>16,609,529.69</u>	<u>486,847,924.98</u>

During the year, the depreciation of fixed assets amounted to RMB39,557,808.83.

The transfer from construction-in-progress to fixed assets at cost during the year amounted to RMB65,100,091.77.

As at 31st December 2011, certain fixed assets (buildings and structures) with net book value of RMB10,458,326.16 were pledged to banks for short-term loans (2010: RMB15,839,591.02).



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 8. Fixed assets (Continued)

#### (2) Temporarily idle fixed assets

					<i>Unit: RMB</i>
Item	Cost	Accumulated depreciation	Impairment provision	Carrying amount	Remark
Machinery and equipment	2,323,655.38	1,968,957.25	-	354,698.13	Temporarily sealed and stored

#### (3) Fixed assets acquired under finance leases

				<i>Unit: RMB</i>
Items	Cost	Accumulated depreciation	Carrying Amount	
As at 31st December 2011				
Buildings and structures	2,592,597.82	2,488,893.91	103,703.91	
As at 31st December 2010				
Buildings and structures	2,610,055.82	2,505,653.59	104,402.23	

As at the end of 2011 and 2010, fixed assets acquired under finance leases were fully depreciated.

#### (4) Fixed assets with pending certificates of ownership

As at 31st December 2011 and at the date of approval of this statement, the Group is applying for property certificates for some buildings and structures. The time of obtaining property certificates is depending upon the consideration and approval procedures of the relevant government authorities. The carrying amount of the above mentioned fixed assets was RMB42,506,860.24 (2010: RMB43,637,000).

Directors of the Company are of the opinion that pending the grant of property certificates will not affect the usage and operation of the buildings and structures.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 9. Construction in progress

(1) Information of construction in progress

Unit: RMB

Project	2011			2010		
	Book value	Impairment provision	Carrying amount	Book value	Impairment provision	Carrying amount
Okamoto gantry precision CNC surface guideway grinder	-	-	-	19,880,285.05	-	19,880,285.05
Duyun Guihang 14m gantry planer	-	-	-	4,700,061.28	-	4,700,061.28
Heavy casting base	90,650,165.27	-	90,650,165.27	66,696,541.29	-	66,696,541.29
CNC vertical lathe	-	-	-	4,100,000.00	-	4,100,000.00
New-built 24-m span workshop	-	-	-	2,589,780.00	-	2,589,780.00
CNC cylindrical grinder and grinder imported from Switzerland for small parts workshop	10,247,728.44	-	10,247,728.44	3,755,700.00	-	3,755,700.00
Other items	20,305,830.76	2,056,931.37	18,248,899.39	22,639,469.34	2,056,931.37	20,582,537.97
Total	121,203,724.47	2,056,931.37	119,146,793.10	124,361,836.96	2,056,931.37	122,304,905.59

The carrying amount of construction in progress of the Group did not include the capitalization of borrowings. (2010: RMB0)

(2) Movements of major construction projects in progress during the year:

Unit: RMB

Project	Budget	Opening balance	Additions during the year	Transfer to fixed assets during the year	Other decreases	Investment percentage to total budget (%)	Project progress	Source of the fund	Closing balance
Okamoto gantry precision CNC surface guideway grinder	7,000,000.00	19,880,285.05	1,280,471.85	21,160,756.90	-	302.30%	100%	Self-financing	-
Duyun Guihang 14m gantry planer	4,280,000.00	4,700,061.28	-	4,700,061.28	-	109.81%	100%	Self-financing	-
Heavy casting base	729,560,000.00	66,696,541.29	23,953,623.98	-	-	12.43%	35%	Self-financing and budgetary investment of central government	90,650,165.27
CNC vertical lathe	3,880,000.00	4,100,000.00	-	4,100,000.00	-	105.67%	100%	Self-financing	-
New-built 24-m span workshop	5,000,000.00	2,589,780.00	2,607,773.22	5,197,553.22	-	103.95%	100%	Self-financing	-
CNC cylindrical grinder and grinder imported from Switzerland for small parts workshop	12,000,000.00	3,755,700.00	6,492,028.44	-	-	85.40%	100%	Self-financing	10,247,728.44
Other items	-	20,582,537.97	30,686,123.00	29,941,720.37	3,078,041.21	-	-	-	18,248,899.39
Total	-	122,304,905.59	65,020,020.49	65,100,091.77	3,078,041.21	-	-	-	119,146,793.10

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 9. Construction-in-progress (Continued)

(2) Progress of major construction project during the year

Project	Work progress	Remark
Heavy casting base	35%	Major structure for the base under construction

### 10. Intangible assets

Item	Land use rights	Various software	Others	Unit: RMB	
				Total	
Cost					
Opening balance	25,925,562.02	16,430,886.75	3,736,089.93	46,092,538.70	
Addition during the year	–	3,231,033.66	–	3,231,033.66	
Closing balance	25,925,562.02	19,661,920.41	3,736,089.93	49,323,572.36	
Accumulated amortization					
Opening balance	3,052,573.45	7,421,572.17	423,239.69	10,897,385.31	
Charge for the year	599,235.84	2,319,039.86	129,272.18	3,047,547.88	
Closing balance	3,651,809.29	9,740,612.03	552,511.87	13,944,933.19	
Carrying amounts					
At the end of the year	22,273,752.73	9,921,308.38	3,183,578.06	35,378,639.17	
At the beginning of the year	22,872,988.57	9,009,314.58	3,312,850.24	35,195,153.39	

Amortization for intangible assets for the year was RMB3,047,547.88.

As at 31st December 2011, carrying amounts of intangible assets of the Group did not include the capitalization of borrowings (2010: Nil).

As at 31st December 2011, land use rights with the carrying amounts of RMB12,100,712.60 was pledged to banks for short-term loans (2010: RMB12,383,770.44).

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 11. Goodwill

Invested company	Opening balance	Increase during the year	Decrease during the year	Closing balance	Unit: RMB
					Impairment provision at the end of the year
Xi'an Ser	7,296,277.00	–	–	7,296,277.00	–

When the Group acquired Xi'an Ser in 2001, the cost of merger was higher than the fair value of the identifiable assets and liabilities of Xi'an Ser corresponding to the interests acquired, and the difference was recognized as goodwill related to Xi'an Ser.

The recoverable amount of Xi'an Ser is determined based on the present value of the estimated future cash flows. The Group prepared cash flow forecasts for this asset based on the recent 5 years financial budgets approved by the management and a 10% discount rate before tax. The cash flows after the 5 years forecast would remain stable. The forecast result imposed no impairment loss to the recoverable amounts. However, the key assumptions on which the discount estimated cash flows were based may vary. The management considered that if negative change occurred to the key assumptions, the book value of the Company may exceed its recoverable amount.

The key assumptions for the calculation of the present value of estimated future cash flows for Xi'an Ser were the gross profit margin and the growth rate of operating income of the turbo machine segment. The management determined these key assumptions based on the historical information prior to the estimated period.

### 12. Long-term deferred expenses

Item	Opening balance	Increase during the year	Amortization during the year	Unit: RMB	
				Closing balance	
Decoration	678,209.81	865,000.00	178,093.26	1,365,116.55	

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 13. Deferred tax assets

(1) Reconciliation of composition of deferred income tax assets and liabilities:

Unit: RMB

Item	2011		2010	
	Deductible temporary difference	Deferred tax assets	Deductible temporary difference	Deferred tax assets
<b>Deferred tax assets:</b>				
Bad debt provision	187,049,977.04	28,226,996.55	144,122,461.62	25,341,705.62
Provision for diminution in value of inventories	16,267,833.98	2,440,175.10	11,730,834.83	2,719,396.12
Provision for impairment of fixed assets	3,708,379.76	556,256.96	3,709,044.04	927,261.01
Provision for impairment of construction in progress	2,056,931.37	308,539.71	2,056,931.37	514,232.84
Provision for impairment of long-term equity investments	3,500,000.00	525,000.00	2,000,000.00	5,335,386.21
Provisions	17,390,990.97	2,608,648.64	22,469,390.59	3,370,408.59
Depreciation of fixed assets	5,432,865.15	814,929.77	6,230,202.52	934,530.38
Accrued expenses	4,140,100.00	621,015.00	–	–
Unrealized internal profits	6,527,481.51	979,122.23	4,345,811.40	651,871.71
Discounted value of retirement benefits for internal staff under early retirement	11,325,508.61	1,698,826.30	10,666,424.84	2,369,107.94
Issuance of VAT invoice in advance, revenue not yet recognized	–	–	19,429,740.37	2,914,461.05
Government subsidies	39,643,000.00	5,946,450.00	23,889,000.00	3,583,350.00
Payables overdue for two years	1,276,914.33	191,537.15	1,276,914.36	191,537.15
Deductible tax losses	9,980,608.03	1,327,591.21	8,013,861.90	1,202,079.29
Total	308,300,590.75	46,245,088.62	259,940,617.84	50,055,327.91

(2) Breakdown of unrecognized deferred tax assets

Unit: RMB

Item	2011	2010
Deductible tax losses	4,733,074.58	20,647,983.72

(3) Expiration of deductible tax losses for unrecognized deferred tax assets

Unit: RMB

Year	2011	2010
2012	–	–
2013	201,495.36	201,495.36
2014	730,877.95	16,495,942.20
2015	2,448,294.03	3,950,546.16
2016	1,352,407.24	–
Total	<u>4,733,074.58</u>	<u>20,647,983.72</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 14. Other non-current assets

Item	2011	Unit: RMB	
		2011	2010
Project prepayments	10,770,514.20		–
Prepayments for land use rights (Note)	50,720,000.00		–
Prepayments for contracted technology licensing fee (Note (VI). 5(1) note 3)	18,246,610.80		–
Total	<u>79,737,125.00</u>		–

Note: As at 31st December 2011, the prepayments for land use right was paid to the People's Government of Gaoming City of Yunnan Province for a piece of land in Yanglin Industrial Development Zone.

### 15. Breakdown of provision for impairment of assets

Item	Note	Opening balance	Increase during the year		Decrease during the year		Closing balance
			Charge for the year	Other	Reversal	Write-off	
Accounts receivable	(V)3	127,372,966.78	56,493,076.37	–	–	1,037,700.00	182,828,343.15
Other receivables	(V)4	2,330,005.85	1,891,628.04	–	–	–	4,221,633.89
Inventories	(V)6	11,730,834.83	4,536,999.15	–	–	–	16,267,833.98
Long-term equity investments	(V)7	2,000,000.00	–	–	–	–	2,000,000.00
Fixed assets	(V)8	3,709,044.04	–	–	–	664.28	3,708,379.76
Construction in progress	(V)9	2,056,931.37	–	–	–	–	2,056,931.37
Total		<u>149,199,782.87</u>	<u>62,921,703.56</u>	<u>–</u>	<u>–</u>	<u>1,038,364.28</u>	<u>211,083,122.15</u>

Please refer to notes to the relevant assets for reasons of impairment loss recognized for different assets during the year.

### 16. Restricted assets

As at 31st December 2011, the assets with restrictions placed on their ownership as follows:

Item	Note	Opening balance	Increase during the year	Decrease during the year	Unit: RMB	
					Closing balance	Closing balance
Assets pledged as collateral						
– Cash at bank and on hand	(V)1	10,412,135.19	5,980,175.84	–	–	16,392,311.03
– Fixed assets	(V)8	15,839,591.02	–	5,381,264.86	–	10,458,326.16
– Intangible assets	(V)10	12,383,770.44	–	283,057.84	–	12,100,712.60
Total		<u>38,635,496.65</u>	<u>5,980,175.84</u>	<u>5,664,322.70</u>	<u>–</u>	<u>38,951,349.79</u>

During the financial reporting period, restricted ownership security deposit is deposited with the bank as security for the letters of guarantee and bank acceptance notes issued by the bank for the Group.

Restricted ownership fixed assets and intangible assets were pledged for short-term loans. After repayment of the short-term loans, the term of restriction will be released.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 17. Short-term loans

(1) *Types of short-term loans:*

Item	2011	Unit: RMB
		2010
Secured loans	20,000,000.00	25,000,000.00
Guarantee loans	<u>80,000,000.00</u>	<u>21,000,000.00</u>
Total	<u>100,000,000.00</u>	<u>46,000,000.00</u>

(2) As at 31st December 2011, the Group had no short-term loans due but outstanding.

### 18. Bills payable

Item	2011	Unit: RMB
		2010
Bank acceptance bills	<u>46,596,910.09</u>	<u>20,426,973.00</u>

The above amount of bills payable will be due within one year.

### 19. Accounts payable

(1) *Types of accounts payable are as follows:*

Item	2011	Unit: RMB
		2010
Accounts payable to related company	45,553,713.06	22,769,396.37
Accounts payable to suppliers	<u>318,378,289.87</u>	<u>207,487,014.31</u>
Total	<u>363,932,002.93</u>	<u>230,256,410.68</u>

(2) There were no accounts payable to shareholders holding over 5% (or 5%) shares of the Company entitling voting rights.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 19. Accounts payable (Continued)

(3) Aging analysis of accounts payable:

Aging	2011		2010	
	Book value Amount	Proportion (%)	Book value Amount	Proportion (%)
Within one year (including one year)	345,694,705.24	94.99	218,286,870.11	94.80
1-2 years (including 2 years)	13,028,799.15	3.58	5,572,764.33	2.42
2-3 years (including 3 years)	2,547,823.45	0.70	1,895,752.42	0.82
Over 3 years	2,660,675.09	0.73	4,501,023.82	1.96
Total	<u>363,932,002.93</u>	<u>100.00</u>	<u>230,256,410.68</u>	<u>100.00</u>

Unit: RMB

The aging of accounts payable is calculated starting from the date of recognition.

### 20. Advances from customers

All advances from customers are payment for goods received in advance from the customers of the Company.

(1) Advances from customers by aging of accounts are as follows:

Aging	2011		2010	
	Book value Amount	Proportion (%)	Book value Amount	Proportion (%)
Within one year (including one year)	356,431,749.52	82.25	266,897,136.09	64.36
1-2 years (including 2 years)	49,972,174.63	11.53	137,236,489.83	33.09
2-3 years (including 3 years)	19,731,124.00	4.55	9,360,939.92	2.26
Over 3 years	7,218,723.20	1.67	1,230,557.38	0.29
Total	<u>433,353,771.35</u>	<u>100.00</u>	<u>414,725,123.22</u>	<u>100.00</u>

Unit: RMB

There were no advances due from shareholders holding over 5% (or 5%) shares of the Company entitling voting rights.



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 21. Employee benefits payable

Item	<i>Unit: RMB</i>			
	Opening balance	Accrued during the year	Paid during the year	Closing balance
1. Salary, bonus, subsidy and grants (note 1)	17,174,514.83	232,277,267.53	236,369,545.67	13,082,236.69
2. Staff welfare	–	5,879,133.84	5,842,468.40	36,665.44
3. Social insurance Including:	(1,252,945.35)	36,964,328.59	33,343,645.29	2,367,737.95
(i) Medical insurance	567,078.33	10,669,251.78	9,656,059.23	1,580,270.88
(ii) Basic retirement insurance	(1,234,022.79)	22,640,050.42	20,347,370.54	1,058,657.09
(iii) Unemployment insurance	(586,000.89)	2,076,971.69	1,897,448.36	(406,477.56)
(iv) Work injury insurance	–	929,731.89	798,118.99	131,612.90
(v) Maternity insurance	–	648,322.81	644,648.17	3,674.64
4. Housing fund	1,846,049.72	13,770,048.29	13,780,144.29	1,835,953.72
5. Termination benefits (including early retirement fee) (note 2)	10,601,889.84	6,114,156.55	5,390,537.78	11,325,508.61
6. Union expenses and employees education expenses	6,286,900.75	6,113,544.73	7,550,158.25	4,850,287.23
<b>Total</b>	<b>34,656,409.79</b>	<b>301,118,479.53</b>	<b>302,276,499.68</b>	<b>33,498,389.64</b>

Note 1: Except for accrued year-end bonuses, the Group paid the accrued salary, bonus, subsidy and grants in January 2012. As at 31st December 2011, the Group did not have any accrued salary in arrears.

Note 2: As at 31st December 2011, the above termination benefits did not include the compensation for termination of labour service contract.

Some employees of the Group retired from employment of the Group prior to their statutory retirement age. According to the requirements of the early retirement plan of the Group, from the date of ceasing service provision up to their respective statutory retirement dates, such employee salary as proposed salary and social insurance for early retirement employees were recognised at their discounted present value as provisions and were included in current administrative expenses ("early retirement expenses"). The discount rate selected by the Group represent the interest rate of national bonds having the same credit term with early retirement expenses of the Group.

### 22. Taxes payable

Item	<i>Unit: RMB</i>	
	2011	2010
Value added tax	3,199,549.74	(5,343,083.12)
Business tax	120,830.69	106,944.87
Corporate income tax	267,149.52	6,846,857.07
Others	3,722,772.91	3,259,924.75
<b>Total</b>	<b>7,310,302.86</b>	<b>4,870,643.57</b>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 23. Dividends payable

Item	Unit: RMB	
	2011	2010
Cash dividends declared but outstanding	135,898.49	135,898.49

### 24. Other payables

(1) Other payables are as follows:

Item	Unit: RMB	
	2011	2010
Secured deposits for projects	4,607,662.25	2,875,589.20
Leasing expenses	2,254,373.81	-
R&D expenditures	45,000.00	5,059,388.19
Auditor's fee	2,150,000.00	2,150,000.00
Commissions and business promotion fees	20,414,223.33	960,000.00
Others	11,194,377.60	9,617,069.76
Total	<u>40,665,636.99</u>	<u>20,662,047.15</u>

There were no other payables due to shareholders holding over 5% (or 5%) shares of the Company entitling voting rights.

(2) Other payables by aging of accounts are as follows:

Aging	Unit: RMB			
	2011		2010	
	Book value balance amount	Proportion (%)	Book value balance amount	Proportion (%)
Within one year (including one year)	35,435,519.62	87.14	9,970,962.39	48.27
1-2 years (including 2 years)	1,293,896.67	3.18	8,941,401.43	43.27
2-3 years (including 3 years)	2,263,850.30	5.57	1,207,539.67	5.84
Over 3 years	1,672,370.40	4.11	542,143.66	2.62
Total	<u>40,665,636.99</u>	<u>100.00</u>	<u>20,662,047.15</u>	<u>100.00</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 25. Provisions

Item	2011	Unit: RMB	
		2011	2010
Product quality warranty	<u>17,390,990.97</u>	<u>16,301,190.59</u>	

Generally, the Group provides after-sale quality service guarantee to its customers who buy machine tool products from the Group. If the products have malfunction caused by non-accident or quality problems within one year after sale, the Group will provide free maintenance. The above product quality warranty was made based on the Group's forecasted product quality warranty expenditures needed to be undertaken for products sold during the year and prior years.

### 26. Non-current liabilities due within one year

Information of non-current liabilities due within one year is as follows:

Item	Note	2011	Unit: RMB	
			2011	2010
Obligation under finance lease	V.27	213,209.00		–
Sales and lease back	V.29	<u>205,300.00</u>		–
Total		<u>418,509.00</u>		–

### 27. Long-term payables

Item	2011	Unit: RMB	
		2011	2010
Obligation under finance lease	<u>1,918,881.90</u>	<u>2,345,300.00</u>	

Obligation under finance lease reflected the present value of minimum lease payments caused by the Group's lease of some workshops and factory buildings after sale in 2001. The lease constituted finance lease and the term of lease was 20 years. In 2011, the Group presented the obligation under finance lease as long-term payables and non-current liabilities due within one year (note V. 26).

As at 31st December 2011, the balance of unrecognised finance expenses of the Group was RMB1,289,599.00 (2010: RMB1,418,558.80).

There were no long-term payables due to shareholders holding over 5% (or 5%) shares of the Company entitling voting rights.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 27. Long-term payables (Continued)

Interest analysis of the minimum financial lease payment of the Group payable after 31st December 2011 and calculated at the undiscounted contractual cash flow (including at contractual interest (in the case of floating interest, the prevailing interest on 31st December)) is as follows:

Minimum lease payments	2011	2010
Within one year (including one year)	342,168.88	342,168.88
1-2 years (including 2 years)	342,168.88	342,168.88
2-3 years (including 3 years)	342,168.88	342,168.88
Over 3 years	2,395,183.26	2,737,352.16
Sub-total	3,421,689.90	3,763,858.80
Less: unrecognised finance charges	1,289,599.00	1,418,558.80
Total	<u>2,132,090.90</u>	<u>2,345,300.00</u>

The amount of financial lease payment due within one year after deducting unrecognised financial expenses was disclosed in note V. 26.

### 28. Special payables

Item	Opening balance	Increase during the year	Decrease during the year	Unit: RMB Closing balance
Specific appropriation from Shaanxi Intellectual Property Office	100,000.00	-	-	100,000.00
Tax refund for import tariff and import VAT for key parts of machine tools (note)	-	15,167,565.87	-	15,167,565.87
Total	<u>100,000.00</u>	<u>15,167,565.87</u>	<u>-</u>	<u>15,267,565.87</u>

*Note* Pursuant to the stipulations of the "Notice from the Ministry of Finance, National Development Reform Commission, China Customs, State Administration of Taxation on Import Duties Policy Related to Several Opinions on the Acceleration of Revitalising the Equipment Manufacturing Industry" (Cai Guan Shui [2007] No. 11), the tax refund will be treated as state investment, and should convert into state capital within the specified time. If an enterprise cannot convert the tax refund into state capital within the specified time, it should return the refund to state treasury on time. According to the resolution passed at the 19th meeting of the sixth session of the Board of the Company held on 16th August 2010, the Company would directly issue shares to its state-owned substantial shareholders Shenji Group and Yunnan Industrial Investment within two years after receiving the tax refund and complete the procedure of converting tax refund into state capital. Before that time, the Company will treat it as specific payables according to accounting standards.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 29. Other non-current liabilities

Item	2011	Unit: RMB 2010
Deferred income		
– sales and lease back (note 1)	1,847,702.91	2,258,303.11
– government grants (note 2)	39,643,000.00	23,889,000.00
Total	<u>41,490,702.91</u>	<u>26,147,303.11</u>

Note 1 Deferred income-sales and lease back were caused by the Group's lease of some buildings and structures and land use rights after sale in 2001 and the lease constituted finance lease. Therefore, the difference between the income of selling premises and land use rights and the original book value formed deferred income and would be amortised by straight-line method within 20 years of leasing period. In 2011, the Group treated the deferred income which was forecasted to be transferred to income statement within one year as non-current liabilities due within one year (see Note V. 26).

Note 2 As at 31st December 2011, the government grants mainly included specific government grants for developing THM65160 series precision horizontal machine tool products and TGK46100 series high-tech boring and milling machines, and government grants for civil construction and equipment purchasing and installation for the heavy casting base (see Note V. 9).

### 30. Share capital

	Unit: RMB Opening and closing balance
Ordinary domestic A Shares	390,186,228.20
Overseas foreign H Shares listed in Hong Kong	140,894,874.80
Total	<u>531,081,103.00</u>

### 31. Capital reserve

Item	Unit: RMB Opening and closing balance
Share premium	19,206,777.12
Other capital reserves	8,096,544.60
Total	<u>27,303,321.72</u>

### 32. Surplus reserve

	Opening balance	Increase during the year	Decrease during the year	Unit: RMB Closing balance
Statutory surplus reserve	109,024,823.62	7,483,178.98	–	<u>116,508,002.60</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 33. Retained earnings

Item	Note	Unit: RMB Amount
Retained earnings at the beginning of the year		706,716,031.08
Add: net profits attributable to shareholders of the Company for the year		54,567,125.16
Less: Appropriation for statutory surplus reserve		7,483,178.98
Dividends payable on ordinary shares	(1)	<u>26,554,055.16</u>
Retained earnings at the end of the year	(2)	<u>727,245,922.10</u>

(1) *Distribution of dividends on ordinary shares*

At the general meeting held on 10th May 2011, the payment of a cash dividend of RMB0.05 per share (2010: RMB0.05 per share) or RMB26,554,055.16 in respect of the year 2010 was approved (2010: RMB21,213,558.22).

(2) *Retained earnings at the end of the year*

RMB228,079.02 of surplus reserve attributed to the Company was made by subsidiaries during the year (2010: RMB930,000.00).

As at 31st December 2011, the Group's retained earnings attributed to the Company included RMB6,750,282.16 of surplus reserve drawn by subsidiaries of the Company (2010: RMB6,720,984.42).

### 34. Operating income and operating costs

(1) *Operating income and operating costs*

Item	2011	2010
Operating income from principal activities	1,798,749,531.20	1,579,041,911.75
Including: income from sales of goods	1,778,371,514.54	1,563,249,614.53
income from services	20,378,016.66	15,792,297.22
Other operating income	6,108,033.09	18,663,355.44
Total of operating income	<u>1,804,857,564.29</u>	<u>1,597,705,267.19</u>
Operating costs	<u>1,368,376,106.28</u>	<u>1,162,557,001.55</u>

(2) *Principal activities (by industry)*

Industry	2011		2010	
	Operating income	Operating costs	Operating income	Operating costs
Machine tools	1,548,123,743.44	1,149,136,018.72	1,355,563,454.92	966,773,545.76
Turbo machines	256,733,820.85	219,240,087.56	200,791,359.45	179,117,429.97
Sensor and turbo tables and computerised embroidery machines	-	-	41,350,452.82	16,666,025.82
Total	<u>1,804,857,564.29</u>	<u>1,368,376,106.28</u>	<u>1,597,705,267.19</u>	<u>1,162,557,001.55</u>

(3) Please refer to note X. 2 (2) for information regarding income from external customers as set out by different areas by the Group.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 34. Operating income and operating costs (Continued)

(4) Operating income from top five customers in 2011

Name of customers	Operating income	Unit: RMB
		Proportion to total operating income (%)
1st	152,672,649.60	8.46
2nd	93,059,829.06	5.16
3rd	41,277,777.79	2.29
4th	39,203,418.85	2.17
5th	38,358,974.37	2.13
Total	<u>364,572,649.67</u>	<u>20.21</u>

As names of customers involve the commercial confidential information of the Group, we did not disclose the specific names of the top five customers in 2011.

### 35. Business taxes and surcharges

Item	2011	2010	Unit: RMB
			Taxation basis and rates
Business tax	22,931.25	59,243.00	3% – 5% of operating income
Urban maintenance and construction tax	4,727,000.36	972,277.65	1% – 7% of paid VAT and business tax
Education surcharges	2,132,201.57	526,765.54	3% of paid VAT and business tax
Local education surcharges	1,142,188.46	–	2% of paid VAT and business tax
Total	8,024,321.64	1,558,286.19	

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 36. Selling and distribution expenses

Item	2011	Unit: RMB
		2010
Staff cost	28,567,237.60	22,643,378.85
Sales commission and business promotion expenses	32,743,045.33	17,269,800.00
Depreciation expenses	1,077,046.01	905,932.75
Others	71,801,359.15	67,364,661.83
Total	<u>134,188,688.09</u>	<u>108,183,773.43</u>

### 37. General and administrative expenses

Item	2011	Unit: RMB
		2010
Staff cost	67,292,056.59	51,333,123.52
R&D expenses	42,960,137.36	31,571,572.27
Depreciation expenses	8,713,597.84	7,780,645.57
Others	50,687,152.59	50,283,459.85
Total	<u>169,652,944.38</u>	<u>140,968,801.21</u>

### 38. Finance expenses

Item	2011	Unit: RMB
		2010
Interest expenses	3,712,939.82	3,540,278.67
Interest income	(1,459,190.35)	(1,837,080.78)
Net exchange (gain)/losses	(76,054.68)	1,087,846.64
Other financial expenses	1,231,506.63	1,201,747.27
Total	<u>3,409,201.42</u>	<u>3,992,791.80</u>



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 39. Investment income

Item	Note	2011	Unit: RMB 2010
Income from long-term equity investments accounted for using the equity method	V.7	7,334,821.80	9,859,063.47

(1) Information on income from long-term equity investments accounted for using the equity method is as follows:

Invested companies	2011	2010
Kunming TOS	7,534,798.57	9,275,207.46
Xi'an Ruite	(199,976.77)	583,856.01
Total	<u>7,334,821.80</u>	<u>9,859,063.47</u>

### 40. Impairment losses

Item	2011	Unit: RMB 2010
Accounts receivable	56,493,076.37	8,489,406.67
Other receivables	1,891,628.04	769,253.94
Inventories	4,536,999.15	(7,844,614.41)
Fixed assets	-	(57,580.42)
Total	<u>62,921,703.56</u>	<u>1,356,465.78</u>

### 41. Non-operating income

(1) Non-operating income by item is as follows:

Item	Note	2011	Unit: RMB 2010
Gain on disposal of non-current assets		1,892,985.09	842,420.63
Government grants	(2)	2,552,408.50	6,700,335.00
Others		645,191.92	6,525,552.25
Total		<u>5,090,585.51</u>	<u>14,068,307.88</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 41. Non-operating income (Continued)

(2) Breakdown of government grants:

Item	2011	2010	Explanation
Grants for R&D of products	1,800,000.00	5,900,000.00	Government grants for the machine tool R&D of the Group
Other grants	752,408.50	800,335.00	–
Total	<u>2,552,408.50</u>	<u>6,700,335.00</u>	–

### 42. Non-operating expenses

Item	2011	2010	Unit: RMB Amount included in non-recurring gains or losses for the year 2011
Losses on disposal of fixed assets	499,354.16	175,900.51	499,354.16
Donations provided	8,000.00	6,000.00	8,000.00
Others	1,418,555.54	1,973,172.65	1,418,555.54
Total	<u>1,925,909.70</u>	<u>2,155,073.16</u>	<u>1,925,909.70</u>

### 43. Income tax expenses

Item	Note	2011	Unit: RMB 2010
Current tax expenses for the year based on tax law and regulations		12,758,248.81	30,676,813.47
Changes in deferred tax assets	(1)	<u>3,810,239.29</u>	<u>(3,279,689.53)</u>
Total		<u>16,568,488.10</u>	<u>27,397,123.94</u>

During the 12 months ended 31st December 2011 and 31st December 2010, the Group did not have assessable profits subject to Hong Kong Profits Tax. Therefore, no provision has been made for Hong Kong Profits Tax.

(1) The analysis of changes in deferred tax assets is set out below:

Item	2011	Unit: RMB 2010
Origination and reversal of the temporary differences	(8,832,491.81)	(2,825,574.82)
Effects of tax rate changes on deferred tax	17,957,297.13	(705,667.43)
Unrecognised deductible losses	338,101.81	604,428.29
Offsetting deferred income tax assets recognised in prior years	750,000.00	–
Using deductible losses unrecognised in prior years	<u>(6,402,667.84)</u>	<u>(352,875.57)</u>
Total	<u>3,810,239.29</u>	<u>(3,279,689.53)</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 43. Income tax expenses (Continued)

(2) The relationship between income tax expenses and accounting profit:

Item	2011	Unit: RMB
		2010
Profit before tax	68,784,096.53	200,860,445.42
Expected income tax under tax rate applicable to relevant region	17,196,024.13	50,215,111.36
Add: nondeductible expenses	1,503,757.07	2,212,229.09
non-taxable income	(1,833,705.45)	(2,464,765.88)
Unrecognised deductible losses	338,101.81	604,428.29
Offsetting deferred income tax assets recognised in prior years	750,000.00	–
Using deductible losses unrecognised in prior years	(6,402,667.84)	(352,875.57)
Effects of tax rate changes on deferred tax	17,957,297.13	(705,667.43)
Effects of items eligible for additional deduction	(4,604,571.13)	(1,022,220.45)
Effects on preferential income tax	(8,335,747.62)	(21,089,115.47)
Income tax expenses for the year	<u>16,568,488.10</u>	<u>27,397,123.94</u>

### 44. Calculation of basic earnings per share and diluted earnings per share

(1) Basic earnings per share

The basic earnings per share was calculated by dividing the consolidated net profit attributable to ordinary shareholders of the Company by the weighted average number of the outstanding ordinary shares of the Company:

	2011	2010
Consolidated net profit attributable to ordinary shareholders of the Company (RMB)	54,567,125.16	178,324,801.52
Weighted average number of the outstanding ordinary shares of the Company (share)	531,081,103.00	531,081,103.00
Basic earnings per share (RMB/share)	0.10	0.34

Calculation of the weighted average number of ordinary shares:

	2011	2010
Number of shares in issue at the beginning of the year	531,081,103	424,864,883
Converting reserves into share capital regards as the adjustment of the financial statements at the beginning of the year	–	106,216,220
Weighted average number of ordinary shares at the end of the year	531,081,103	531,081,103

(2) Diluted earnings per share

The diluted earnings per share was the same as the basic earnings per share, because the Company did not have any potentially dilutive ordinary shares during the year.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 45. Income statement supplementary information

Expenses in the income statement by nature:

<b>Item</b>	<b>2011</b>	<i>Unit: RMB</i> <b>2010</b>
Operating income	1,804,857,564.29	1,597,705,267.19
Less: changes in inventory of finished goods and work in process	(205,018,736.43)	(112,313,018.66)
Consumption of raw materials	885,222,323.15	701,273,874.34
Staff cost incurred	301,118,479.53	221,210,841.17
Processing expenses	329,551,893.44	286,171,232.25
Depreciation expenses	39,557,808.83	36,405,474.26
Amortization of intangible assets	3,047,547.88	2,743,298.11
Impairment of assets	62,921,703.56	1,356,465.78
Bank loans interests	3,712,939.82	3,540,278.67
R&D costs	42,960,137.36	31,571,572.27
Auditor's fee	2,700,000.00	3,014,000.00
Others	270,299,370.62	221,870,803.58
Total profits	<u>68,784,096.53</u>	<u>200,860,445.42</u>

### 46. Notes to cash flow statement

(1) Other cash received relating to operating activities during the year

<b>Item</b>	<i>Unit: RMB</i> <b>Amount</b>
Government grants for R&D of products	9,169,408.50
Others	1,056,669.50
Total	<u>10,226,078.00</u>

(2) Other cash paid relating to operating activities during the year

<b>Item</b>	<i>Unit: RMB</i> <b>Amount</b>
Commission fees	18,550,322.00
Product quality warranty expenses	16,920,223.68
Others	26,097,640.68
Total	<u>61,568,186.36</u>

(3) Cash received relating to other financing activities

<b>Item</b>	<i>Unit: RMB</i> <b>Amount</b>
Government grants for heavy casting base	16,000,000.00
Tax refund for import tariff and import VAT for key parts of machine tools (note V 28)	15,167,565.87
Total	<u>31,167,565.87</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 47. Related information of cash flow statement

(1) Relevant information on cash flow statement

Supplementary information	2011	Unit: RMB 2010
<b>1. Reconciliation of net profit to cash flows from operating activities:</b>		
Net profit	52,215,608.43	173,463,321.48
Add: Provision for impairment of assets	62,921,703.56	1,356,465.78
Depreciation of fixed assets	39,557,808.83	36,405,474.26
Amortization of intangible assets	3,047,547.88	2,743,298.11
Amortization of long-term deferred expenses	178,093.26	175,362.69
Amortization of deferred gain	(205,300.20)	(205,300.20)
Profit on disposal of fixed assets	(1,393,630.93)	(625,490.12)
Finance expense	4,116,520.60	4,497,041.44
Investment income	(7,334,821.80)	(9,859,063.47)
Decrease in deferred income tax assets ("-" for increase)	3,810,239.29	(3,279,689.53)
Increase in inventories	(235,440,378.85)	(142,487,528.76)
Increase in operating receivable	(190,586,600.85)	(82,477,863.29)
Increase in operating payable	269,767,967.48	149,566,754.95
Net cash flows from operating activities	<u>654,756.70</u>	<u>129,272,783.34</u>
<b>2. Net change in cash and cash equivalents:</b>		
Cash balance at the end of the year	175,808,019.62	285,882,274.37
Less: cash balance at the beginning of the year	285,882,274.37	274,937,559.13
Net increase in cash and cash equivalents ("-" for decrease)	(110,074,254.75)	10,944,715.24

(2) Composition of cash and cash equivalents

Item	2011	Unit: RMB 2010
1. Cash	175,808,019.62	285,882,274.37
Including: cash on hand	503,574.06	1,107,200.04
Bank deposits available on demand	175,304,445.56	284,775,074.33

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 48. Director's remuneration

Details of director's remuneration for the year ended 31st December 2011

Unit: RMB ten thousand

	Director's fee	Salaries allowances and benefits in kind	Retirement scheme contributions	Discretionary bonuses	Total
Executive directors:					
Wang Xing (Chairman) (i)	65	206	–	–	271
Zhang Xiaoyi	70	429	37	180	716
Ye Nong	51	359	59	180	649
Li Shunzhen (ii)	11	61	9	–	81
Pi Jianguo (iii)	40	346	73	50	509
Non-executive directors:					
Guan Xin	45	–	–	–	45
Gao Minghui (i)/(ii)	71	404	59	100	634
Zhang Tao (vi)	–	–	–	–	–
Li Zhenxiong (vi)	–	–	–	–	–
Independent directors:					
Wayne Yu (iv)	79	–	–	–	79
Chen Ying (iii)	95	–	–	–	95
Li Dongru	119	–	–	–	119
Chen Fusheng (v)	83	–	–	–	83
Xiao Jianming (ii)	24	–	–	–	24
Liu Minghui	119	–	–	–	119
Total	872	1,805	237	510	3,424

Note:

- (i) On 27th July 2011, Mr. Gao Minghui resigned the position of chairman and director Mr. Wang Xing was appointed Chairman of the Company.
- (ii) The Company held a general meeting on 31st October 2011 to review and approve Ms. Li Shunzhen as executive director of the Company with effect from 31st October 2011, Mr. Gao Minghui as non-executive director of the Company with effect from 31st October 2011 and Mr. Xiao Jianming as independent non-executive director of the Company with effect from 31st October 2011.
- (iii) Mr. Pi Jianguo and Mr. Chen Ying has resigned on 31st October 2011 because of the expiration of term of office.
- (iv) Mr. Wayne Yu has resigned on 15th June 2011 due to the expiration of term of office.
- (v) The Company held a general meeting on 18th July 2011 to review and approve Mr. Chen Fusheng as independent non-executive director of the Company with effect from 18th July 2011.
- (vi) The director had elected to waive any remuneration to him from the Group.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (V). NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 48. Director's remuneration (Continued)

Details of director's remuneration for the year ended 31st December 2010

Unit: RMB ten thousand

	Director's fee	Salaries allowances and benefits in kind	Retirement scheme contributions	Discretionary bonuses	Total
Executive directors:					
Gao Minghui (Chairman)	81	367	45	50	543
Zhang Xiaoyi	67	463	39	150	719
Pi Jianguo	49	381	70	30	530
Ye Nong (iii)	20	425	45	110	600
Non-executive directors:					
Guan Xin (iii)	23	–	–	–	23
Wang Xing	43	–	–	–	43
Sun Kai (ii)	16	–	–	–	16
Li Zhenxiong (i)	–	–	–	–	–
Zhang Tao (i)	–	–	–	–	–
Independent directors:					
Wayne Yu	171	–	–	–	171
Chen Ying	114	–	–	–	114
Li Dongru	114	–	–	–	114
Liu Minghui	115	–	–	–	115
<b>Total</b>	<b>813</b>	<b>1,636</b>	<b>199</b>	<b>340</b>	<b>2,988</b>

Note:

- (i) The director had elected to waive any remuneration to him from the Group.
- (ii) The Company held a general meeting on 11th May 2010 to review and approve the resignation of Mr. Sun Kai from his position as non-executive director of the company with effect from 11th May 2010.
- (iii) The Company held a general meeting on 23rd June 2010 to review and approve Mr. Ye Nong and Mr. Guan Xin as executive director and non-executive director of the company respectively with effect from 23rd June 2010.

### 49. Individuals With Highest Emoluments

Of the five individuals with the highest emoluments, four (2010: four) are directors whose emolument are disclosed in note V 48. The aggregate of the emoluments in respect of the remaining individuals are as follows:

Item	Unit: RMB ten thousand	
	2011	2010
Salaries and other emoluments	366	376
Discretionary bonuses	180	38
Retirement scheme contributions	37	100
<b>Total</b>	<b>583</b>	<b>514</b>

The emoluments of the one individual (2010: one) with the highest emoluments are within the following band:

Item	2011	2010
HKD Nil – HKD 1,000,000	1	1

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (VI). RELATED PARTIES AND TRANSACTIONS

### 1. Information on the largest shareholder of the Company

Unit: RMB

Name of the largest shareholder	Type	Place of registration	Legal representative	Business nature	Registered capital	Percentage of shareholding (%)	Percentage of voting rights (%)	Ultimate controlling shareholder of the Company	Organization code
Shenji Group	Limited liability company	China	Guan Xiyou	Production and sales of machine tools	1,556,480,000	25.09	25.09	Shenyang State-owned Assets Supervision and Administration Commission	243381258

### 2. Subsidiaries of the Company

Please see Note IV for information of subsidiaries of the Company.

### 3. Jointly controlled enterprises and associated companies of the Company

Name of investee	Type	Place of registration	Legal representative	Business nature	Registered capital	Percentage of shareholding (%)	Percentage of voting rights (%)	Organization code
1. Jointly controlled enterprise Kunming TOS	Limited company	China	Ing. JanRYDL	Production and sales of machine tools	EUR5,000,000	50	50	77266099-X
2. Associated company Xi'an Ruite	Limited company	China	Tian Huisheng	Production and sales of laser prototyping machine	RMB60,000,000	23.34	23.34	79166780-4

### 4. Information on other related parties

Name of other related parties	Related relationship	Organization code
Shenyang Machine Tool Import and Export Co., Ltd. ("Shenyang I & E Co.")	Subsidiary of the largest shareholder of the Company	746486385
Yunnan Yun Ji Group Import and Export Co., Ltd. ("Yun Ji I & E Co.")	Subsidiary of the largest shareholder of the Company	709781545
Yunnan CY Group Co., Ltd.	Subsidiary of the largest shareholder of the Company	919190831
Kunming Kunji Group Co., Ltd. ("Kunji Group Co.")	Subsidiary of the second largest shareholder of the Company	216547232
Yunnan State-owned Assets Property Management Co., Ltd. ("Yunnan State-owned Assets Property")	Subsidiary of the second largest shareholder of the Company	291887852
Yunnan CY (Group) Company Jinhui Spraying Factory ("Jinhui Spraying Factory")	Subsidiary of the largest shareholder of the Company	99211416-5
Trading Centre	Subsidiary of the largest shareholder of the Company	292147185
Shenyang Machine Tool Company Limited	Subsidiary of the largest shareholder of the Company	24340683-0
SCHIESS GmbH ("SchieSS")	Subsidiary of the largest shareholder of the Company	N/A



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (VI). RELATED PARTIES AND TRANSACTIONS (Continued)

### 5. Related party transactions

#### (1) Summary of related party transactions

The Group

Related party	Nature of connected transactions	Pricing method and decision-making procedures of connected transactions	2011		Unit: RMB 2010	
			Amount	Percentage of the same type of transactions (%)	Amount	Percentage of the same type of transactions (%)
Key management (Note 8)	service Remuneration	Based on relevant terms of agreement	6,517,384.69	2.37	5,655,766.28	2.26
Trading Centre	Sales of goods	Based on relevant terms of agreement	957,264.96	7.00	220,611.97	1.42
Kunming TOS (Note 4)	Sales of goods	Based on Normal commercial terms	10,225,251.69	0.66	8,547,017.27	0.55
Shenji I & E Co. (Note 1)	Sales of goods	Based on Normal commercial terms	-	-	1,076,923.08	0.07
Yunji I & E Co. (Note 1)	Sales of goods	Based on Normal commercial terms	1,794.87	-	1,837.61	0.00
Yunnan CY Group Co., Ltd.	Sales of goods	Based on Normal commercial terms	292,863.25	0.02	6,811.59	0.00
Kunming TOS (Note 4)	Purchase of goods	Based on Normal commercial terms	105,850,902.77	11.39	103,239,306.30	7.35
Yunnan CY Group Co., Ltd.	Purchase of goods	Based on Normal commercial terms	-	-	3,310,530.09	0.22
Jinhui Spraying Factory (Note 5)	Purchase of goods	Based on Normal commercial terms	3,644,430.73	0.39	-	-
Shenyang Machine Tool Company Limited	Purchase of goods	Based on Normal commercial terms	405,749.91	0.04	-	-
Shenyang Machine Tool Company Limited (Note 6)	Purchase of equipment	Based on Normal commercial terms	9,475,871.81	5.08	-	-
Yunnan CY Group Co., Ltd. (Note 7)	Purchase of equipment	Based on Normal commercial terms	1,640,601.71	0.88	-	-
Yunnan State-owned Assets Property (VI 5 (2))	Receipt of service and leasing	Based on relevant terms of agreement	1,693,728.82	22.45	628,861.12	1.10
Kunji Group Co. (Note 2, VI 5(2))	Receipt of service and leasing	Based on relevant terms of agreement	5,462,125.10	72.41	2,220,543.00	46.50
Schiess (Note 3)	Receipt of services	Based on relevant terms of agreement	3,483,152.00	100.00	-	-
Schiess (Note 3)	Payment of contract technology license fees	Based on relevant terms of agreement	18,246,610.80	100.00	-	-

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (VI). RELATED PARTIES AND TRANSACTIONS (Continued)

### 5. Related party transactions (Continued)

#### (1) Summary of related party transactions (Continued)

The Company

Related party	Nature of connected transactions	Pricing method and decision-making procedures of connected transactions	2011		Unit: RMB 2010	
			Amount	Percentage of the same type of transactions (%)	Amount	Percentage of the same type of transactions (%)
Key management (Note 8)	Service Remuneration	Based on relevant terms of agreement	6,517,384.69	2.59	5,655,766.28	2.49
Trading Centre	Sales of goods	Based on relevant terms of agreement	957,264.96	7.00	220,611.97	1.42
Fujian Kunji	Sales of goods	Based on relevant terms of agreement	204,679.50	0.01	4,070,116.00	0.30
Kunming TOS (Note 4)	Sales of goods	Based on Normal commercial terms	10,225,251.69	0.66	8,547,017.27	0.62
Shenji I & E Co. (Note 1)	Sales of goods	Based on Normal commercial terms	-	-	1,076,923.08	0.08
Yunji I & E Co. (Note 1)	Sales of goods	Based on Normal commercial terms	1,794.87	-	1,837.61	0.00
Yunnan CY Group Co., Ltd.	Sales of goods	Based on Normal commercial terms	292,863.25	0.02	6,811.59	0.00
Kunming TOS (Note 4)	Purchase of goods	Based on Normal commercial terms	105,850,902.77	13.28	103,239,306.30	8.78
Yunnan CY Group Co., Ltd.	Purchase of goods	Based on Normal commercial terms	-	-	3,310,530.09	0.28
Jinhui Spraying Factory (Note 5)	Purchase of goods	Based on Normal commercial terms	3,644,430.73	0.46	-	-
Shenyang Machine Tool Company Limited	Purchase of goods	Based on Normal commercial terms	405,749.91	0.05	-	-
General Machine	Purchase of goods	Based on Normal commercial terms	2,604,618.23	0.33	-	-
Xi'an Ser	Provision of services	Based on relevant terms of agreement	2,155,575.62	100.00	2,096,000.00	100.00
Shenyang Machine Tool Company Limited (Note 6)	Purchase of equipment	Based on Normal commercial terms	9,475,871.81	5.18	-	-
Yunnan CY Group Co., Ltd. (Note 7)	Purchase of equipment	Based on Normal commercial terms	1,640,601.71	0.90	-	-
Yunnan State-owned Assets Property (VI 5(2))	Receipt of service and leasing	Based on relevant terms of agreement	1,693,728.82	1.16	628,861.12	10.71
Kunji Group Co. (Note 2, VI 5(2))	Receipt of service and leasing	Based on relevant terms of agreement	5,462,125.10	3.73	2,220,543.00	46.50
Schiess (Note 3)	Receipt of services	Based on relevant terms of agreement	3,483,152.00	100.00	-	-
Schiess (Note 3)	Payment of contract technology license fees	Based on relevant terms of agreement	18,246,610.80	100.00	-	-

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (VI). RELATED PARTIES AND TRANSACTIONS *(Continued)*

### 5. Related party transactions *(Continued)*

#### (1) Summary of related party transactions *(Continued)*

*Note 1:* Transactions are about the Company's sale of machine tool products to Shenji I & E Co. and Yunji I & E Co. respectively. The Company entered into distribution agreements in respect of certain machine tool products with Shenji I & E Co. and Yunji I & E Co. respectively. Pursuant to the agreements, the Company agreed to grant the distribution rights of certain machine tool products to Shenji I & E Co. and Yunji I & E Co., authorizing Shenji I & E Co. and Yunji I & E Co. to distribute and export certain products of the Company from 1st April 2008 to 31st December 2010.

*Note 2:* According to the services agreement entered into between the Company and Kunji Group Company, the Company agreed to provide certain public utility services such as water and electricity to Kunji Group Company, while Kunji Group Company agreed to provide certain services to the Company including property management, employee's medical services, education and administration of retired staff. Service fee is reviewed by both parties on an annual basis.

*Note 3:* As reviewed and approved by the first extraordinary general meeting of 2011 of the Company held on 18th July 2011, the Company and Schiess entered into the Proprietary Technology and Patent Licensing Contract to introduce the proprietary technology for the design, manufacture and installation of double column 2000mm-crossrail machine ("contract products"), and obtain the exclusive and non-transferable license for the production in PRC and sale in Asia of these contract products.

According to the Proprietary Technology and Patent Licensing Contract, contractual expenses include:

- License Fee in one lump-sum: EUR6,600,000;
- Technical training fees: EUR700,000; and
- Technical service fees for the first two prototype machines of machine models VMG6 and VM8: EUR200,000;

The Company will enter into an agreement with Schiess separately to purchase assembly components of VMG6 and VM8 prototype machines from Schiess with an aggregate amount of EUR7,360,651.

In August 2011, the Company paid 30% of the contract technology license fee to Schiess, was amounted to EUR1,980,000 (equivalent to RMB18,246,610.80), and received part of the technical documents (including design drawing, process and content) of the first prototype machine. As at 31st December 2011, the amount was included in the balance sheet as other non-current liabilities (refer to note V 14).

The Company paid technical training fees of EUR400,000 (equivalent to RMB3,483,152.00) to Schiess in November 2011.

*Note 4:* The ordinary business framework agreement was entered between the Company and Tos Kunming Machine Tool Co., Ltd. regarding the purchase of goods, receipt of services, sales of goods and provision of services etc. in 2011 with effective from 31st October 2011 to 31st December 2013.

*Note 5:* The framework agreement was entered between the Company and Jinhui Spraying Factory regarding the purchase of machine tool's packing material in 2011 with effective from 21st September 2011 to 31st December 2013.

*Note 6:* The framework agreement was entered between the Company and Shenyang Machine Tool Co., Ltd. regarding the purchase of vertical lathe and radial drill in 2011 with effective from 21st September 2011 to 31st December 2013.

*Note 7:* The framework agreement was entered between the Company and Yunnan CY (Group) Company regarding the purchase of lathe in 2011 with effective from 21st September 2011 to 31st December 2013.

*Note 8:* The amount comprised remunerations paid to directors (see Note 48) and certain highest paid employees (see Note 49) of the Company.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (VI). RELATED PARTIES AND TRANSACTIONS *(Continued)*

### 5. Related party transactions *(Continued)*

(2) Leases:

Leasing information of the Group and the Company

*Unit: RMB*

Name of leaser	Name of lessee	Type of leased assets	Inception date of lease	Maturity date of lease	Basis for determining lease income	Lease income recognised in 2011
Yunnan State-owned Assets Property Management Co., Ltd.	The Company	Land and premises	1st January 2011	31st December 2013	Based on relevant terms of agreement <i>(Note 1)</i>	989,150.00
Kunji Group Co.	The Company	Land and premises	12th November 2001	11th November 2021	Based on relevant terms of agreement <i>(Note 2)</i>	5,250,000.00

*Note 1:* The transactions were about rental fees for land and premises paid to Yunnan State-owned Assets Property Management Co., Ltd.

The rental agreement for land and premises was entered between the Company and Yunnan State-owned Assets Property Management Co., Ltd. on 28th July 2011. The rental for the first, second and third year amounted to RMB989,150, RMB1,088,065 and RMB1,196,871, respectively. The agreement was effective from 1st January 2011 to 31st December 2013.

*Note 2:* The transactions were about rental fees for premises and land use rights paid to Kunji Group Co.. Kunji Group Co. was authorized by the People's Government of Yunnan Province to succeed the rights and obligations of the "The Premise Rental Agreement" and "The Land Use Rights Rental Agreement" signed between the People's Government of Yunnan Province and the Company on 12th November 2001.

On 12th August 2009, the Company entered into a supplementary agreement for rental adjustment with Kunji Group Co.. The annual rent of land use rights was adjusted from RMB1,320,000 to RMB4,245,086, and the annual rent of premises was adjusted from RMB832,228 to RMB754,914. The adjusted annual rent of land use rights and premises was effective from 12th November 2007 to 11th November 2010.

On 1st February 2011, the Company entered into an agreement for rental adjustment with Kunji Group Co.. The annual rent of land use rights was adjusted to RMB4,457,340, and the annual rent of premises was adjusted to RMB792,660. The adjusted annual rent was effective from 12th November 2010 to 11th November 2013.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (VI). RELATED PARTIES AND TRANSACTIONS (Continued)

### 6. Receivables and payables from/to related parties

The Group

Receivables from related parties

Item	Related parties	2011		2010	
		Carrying amount	Provision for bad and doubtful debt	Carrying amount	Provision for bad and doubtful debt
Accounts receivable	Kunming TOS	6,085,433.84	–	6,632,213.38	–
Other receivables	Kunming TOS	930,594.93	–	233,675.62	–
Accounts receivable	Trading Center	9,000.00	–	9,000.00	–
Other non-current assets	Schiess	18,246,610.80	–	–	–

Unit: RMB

The Group

Payables to related parties

Item	Related parties	2011		2010	
Accounts payable	Kunming TOS		43,510,497.07		22,635,320.30
Accounts payable	Jinhui Spraying Factory		2,043,215.99		134,076.07
Advances from customers	Shenji I & E Co.		–		4,000.00
Other payables	Kunji Group Company		2,625,000.00		–
Other payables	Yunnan CY Group Co., Ltd.		1,461,801.71		–
Other payables	Shenyang Machine Tool Co., Ltd.		1,875,871.81		–

Unit: RMB

The Company

Receivables from related parties

Item	Related parties	2011		2010	
		Carrying amount	Provision for bad and doubtful debt	Carrying amount	Provision for bad and doubtful debt
Accounts receivables	Kunming TOS	6,085,433.84	–	6,632,213.38	–
Accounts receivables	Changsha Ser	244,000.00	–	244,000.00	–
Accounts receivables	Fujian Kunji	4,992,195.83	1,130,000.00	4,972,259.03	–
Accounts receivables	Trading Center	9,000.00	–	9,000.00	–
Other receivables	Kunming TOS	930,594.93	–	233,675.62	–
Other receivables	Xi'an Ser	6,564,496.74	–	4,408,921.12	–
Other receivables	Kunji Transportation	–	–	18,024.57	–
Other receivables	Fujian Kunji	637,604.30	–	452,861.60	–
Other receivables	Winko	–	–	12,693,414.95	9,859,808.60
Other non-current assets	Schiess	18,246,610.80	–	–	–
Dividends receivables	Xi'an Ser	11,000,000.00	–	11,000,000.00	–
Dividends receivables	General Machine	29,130,802.55	–	–	–

Unit: RMB

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (VI). RELATED PARTIES AND TRANSACTIONS *(Continued)*

### 6. Receivables and payables from/to related parties *(Continued)*

The Company

Payables to related parties

Items	Related parties	2011	Unit: RMB	
			2011	2010
Accounts payable	Kunming TOS	43,510,497.07	22,635,320.30	
Accounts payable	Jinhui Spraying Factory	2,043,215.99	134,076.07	
Accounts payable	General Machine	–	11,453,601.95	
Accounts payable	Fujian Kunji	325,000.00	325,000.00	
Advances from customers	Shenji I & E Co.	–	4,000.00	
Advances from customers	Changsha Ser	9,120.67	–	
Other payables	General Machine	12,640,191.46	718,936.38	
Other payables	Kunji Transportation	–	300,000.00	
Other payables	Kunji Group Company	2,625,000.00	–	
Other payables	Yunnan CY Group Co., Ltd.	1,461,801.71	–	
Other payables	Shenyang Machine Tool Co., Ltd.	1,875,871.81	–	

## (VII). CONTINGENCIES

### Contingent liabilities arising from outstanding litigations and arbitration and related financial effect

- (1) The Company signed a sales contract with Yancheng Xinde Oil Machine Company (“Xinde Machine”) in June 2002 for sales of four machine tools with a contract amount of RMB11.9 million. The four related machine tools have been delivered to Xinde Machine before October 2003. In June 2009, Xinde Machine filed a lawsuit against the Company alleging that the goods delivered by the Company were unqualified and sought for return of goods, refund of advances paid of RMB10.7 million and payment of penalty and compensation of RMB0.3 million and RMB3.7 million respectively. In consultation with legal counsels, the Company has denied the claim and filed a counter claim against Xinde Machine alleging that it was unreasonable for Xinde Machine to claim for return of goods after use of the Company’s products for more than 6 years and requesting Xinde Machine to repay the unpaid amount of RMB1.3 million for the goods. In February 2010, the Company and Xinde Machine agreed to mediate the disputes through the court.

Up to the date of the financial statements, the above case is still under the mediation stage. Management considered it may be not quite probable that an outflow of economic benefits would arise from the outcome of the above mediation. Therefore no provision has been made in respect of the above pending case in the financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (VII). CONTINGENCIES (Continued)

### Contingent liabilities arising from outstanding litigations and arbitration and related financial effect (Continued)

- (2) A sales contract of sets of turbo machines amounted to RMB2.8 million was entered into between Xi'an Ser, a subsidiary of the Company, and Zhucheng Guanghua Acetylene Oxygen Making Co., Ltd. (hereinafter referred to as "Zhucheng Guanghua") in September 2004. In 2008, Zhucheng Guanghua filed a law suit against Xi'an Ser, alleging that the goods received did not meet the requirements stipulated in the contract and required Xi'an Ser to return the amount of RMB1.68 million paid and to be liable to breach of contract. Xi'an Ser denied the charge and countercharged Zhucheng Guanghua because of its breach of contract in advance for failing to pay in accordance with the contract. Xi'an Ser also required Zhucheng Guanghua to settle the balance. On 16th October 2009, Weifang Intermediate People's Court made the final judgment that Zhucheng Guanghua should pay a total of RMB1,319,518 for goods price, interest accrued and transpiration fee. On 3rd March 2010, Zhucheng Guanghua refused to accept the final verdict and appealed to the People's Procuratorate of Shandong Province. On 25th May 2010, the People's Procuratorate of Shandong Province filed a protest to the Higher People's Court of Shandong Province. On 4th June 2010, the People's Procuratorate of Shandong Province ordered a retrial by the Higher People's Court of Shandong Province and suspension of the execution of original court decision during the retrial. On 4th June 2010, Higher People's Court of Shandong Province made a judgment for retrial, that the case would be reopened by the Higher People's Court of Shandong Province, and the original judgment should be suspended during retrial period. On 16th February 2011, the Higher People's Court of Shandong Province opened court session for the case. Presently, the Company and Zhucheng Guanghua agreed to mediate the disputes through the court.

Up to the date of the financial statements, the above case is still under the mediation stage. Management considered that it is not probable to result in an outflow of economic benefits from the outcome of the above mediation. Therefore no provisions have been recognized in respect of such litigation in the financial statements.

## (VIII). COMMITMENTS

### 1. Significant commitments

(1) Capital commitments

Items	Unit: RMB	
	2011	2010
Construction contract signed but not implemented or not fully implemented	171,007,819.14	19,482,217.47
Construction contract authorized but not signed or not implemented or not fully implemented	422,571,073.06	241,278,837.62
Proprietary technology and patent licensing contract signed and implementing or proposed to implement	74,405,718.64	—
Total	<u>667,984,610.84</u>	<u>260,761,055.09</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (VIII). COMMITMENTS *(Continued)*

### 1. Significant commitments *(Continued)*

#### (2) Operating Lease commitments

According to the irrevocable lease agreement of premises, the minimum lease payments after the date of 31st December that the Group should pay are as follows:

Items	2011	Unit: RMB
		2010
Within 1 year (including 1 year)	7,194,685.00	5,067,284.00
1-2 years (including 2 years)	7,066,006.00	5,000,000.00
2-3 years (including 3 years)	5,691,200.00	5,000,000.00
Over 3 years	35,000,000.00	40,000,000.00
Total	<u>54,951,891.00</u>	<u>55,067,284.00</u>

## (IX). EVENTS AFTER BALANCE SHEET DATE

### 1. Profit appropriation after the balance sheet date

		Unit: RMB
Profit distribution or dividends to be appropriated	Note(1)	<u>10,621,622.06</u>

#### (1) Distribution of dividends of ordinary shares proposed after the balance sheet date

On 29th March 2012, the Board of directors proposed the Company to distribute cash dividends of RMB0.02 per share (2010: RMB0.05 per share) to ordinary shareholders amounting to RMB10,621,622.06 (2010: RMB26,554,055.16). This proposal is pending approval by the general meeting. The cash dividends proposed to distribute after balance sheet date have not been recognized as liabilities at balance sheet date.

## (X). OTHER SIGNIFICANT ITEMS

### 1. Leases

Please refer to note V.27 for information of amounts payable of the Group in respect of finance lease.

### 2. Segment Reporting

According to the internal organization structure, the requirements of management and internal reporting system, the Group defined its business into three reportable segments – boring machine, turbo machines and sensors and turbo tables, and computerised embroidery machines. Each reportable segment is a separate business unit and provides different goods and services. As each segment needs different technology and marketing strategy, it needs separate management. The management of the Group will review the financial information of different segment regularly for the purpose of resources allocation and assessment of segment performance.



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (X). OTHER SIGNIFICANT EVENTS *(Continued)*

### 2. Segment Reporting *(Continued)*

#### (1) Information of gain or loss, assets and liabilities for the reporting segments

In order to assess the performance of each segment and to allocate resources, the management of the Group will review assets, liabilities, income, expenses, and operating results which attribute to each segment. The basic preparation of these information is as follows:

Segment assets include current assets of all tangible assets, intangible assets, accounts receivable, prepayments, and inventories attributable to each segment, but not including deferred income tax assets caused by the unrealized gains and losses of the Group's internal transactions, long-term equity investment and other undistributed assets of headquarters. Segment liabilities include accounts payable, advance from customers, bank loans and expected liabilities attributable to each segment.

Segment operating results is about the income generated by each segment (including income from transactions with outside parties and income from transactions among segments), deducts expenses caused by each segment, depreciation, amortization and impairment for losses attributable to assets of each segment, and the net interest expense arising from between bank deposit and bank loans attributable to each segment. The pricing of transactions among segments is similar to that of transactions with outside parties. The Group did not allocate investment income and directors' remuneration to each segment.

The information of each reportable segment of the Group disclosed below is the data for the management of the Group to calculate the profit (loss), assets and liabilities of each segment or data not being used but provided to management regularly.

2011

*Unit: RMB*

Item	Business segment of boring machines	Business segment of turbo machines	Business segment of sensor, turbo tables and computerized embroidery machines	Elimination among segments	Undistributed items	Total
Revenue from external customers	1,548,123,743.44	256,733,820.85	-	-	-	1,804,857,564.29
Inter-segment revenue	-	-	-	-	-	-
Investment income from jointly controlled enterprises and associated companies	-	-	-	-	7,334,821.80	7,334,821.80
Impairment loss of assets for the period	55,532,688.41	7,389,015.15	-	-	-	62,921,703.56
Depreciation and amortization expenses	35,409,017.23	7,196,339.48	-	-	-	42,605,356.71
Interest income from bank deposits	1,083,161.36	376,028.99	-	-	-	1,459,190.35
Interest expense	1,370,128.27	2,342,811.55	-	-	-	3,712,939.82
Total profit ("(") for total loss)	67,294,713.05	(2,422,696.55)	-	-	3,912,080.03	68,784,096.53
Income tax expenses ("(") for income tax income)	15,883,637.86	1,012,100.76	-	-	(327,250.52)	16,568,488.10
Net profits ("(") for net loss)	51,411,075.19	(3,434,797.31)	-	-	4,239,330.55	52,215,608.43
Total assets	2,177,134,752.09	398,345,322.68	-	(79,719,416.83)	62,903,703.18	2,558,664,361.12
Total liabilities	882,353,032.33	299,345,947.50	-	(79,719,416.83)	-	1,101,979,563.00
Other significant non-cash items						
- other non-cash expenses other than depreciation and amortization	80,931,727.62	-	-	-	-	80,931,727.62
- long-term equity investment to jointly controlled enterprises and associated companies	-	-	-	-	61,924,580.95	61,924,580.95
- other increment of non-current assets other than long-term equity investment	186,254,866.80	3,674,765.03	-	-	-	189,929,631.83

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (X). OTHER SIGNIFICANT EVENTS (Continued)

### 2. Segment Reporting (Continued)

(1) Information of gain or loss, assets and liabilities for the reporting segments (Continued)

2010

Unit: RMB

Item	Business segment of boring machines	Business segment of turbo machines	Business segment of sensor, turbo tables and computerized embroidery machines	Elimination among segments	Undistributed items	Total
Revenue from external customers	1,396,913,907.74	200,791,359.45	-	-	-	1,597,705,267.19
Inter-segment revenue	-	-	777,800.71	(777,800.71)	-	-
Investment income from jointly controlled enterprises and associated companies	-	-	-	-	9,859,063.47	9,859,063.47
Impairment loss of assets for the period	3,617,940.19	(2,261,474.41)	-	-	-	1,356,465.78
Depreciation and amortization expenses	31,898,688.86	7,409,325.78	16,120.42	-	-	39,324,135.06
Interest income from bank deposits	1,451,901.76	376,344.34	8,834.68	-	-	1,837,080.78
Interest expense	1,771,014.50	1,769,264.17	-	-	-	3,540,278.67
Total profit ("(") for total loss)	200,905,549.14	(8,276,640.19)	1,360,120.26	-	6,871,416.21	200,860,445.42
Income tax expenses ("(") for income tax income)	28,361,472.41	(727,332.42)	-	-	(237,016.05)	27,397,123.94
Net profits ("(") for net loss)	172,544,076.73	(7,549,307.77)	1,360,120.26	-	7,108,432.26	173,463,321.48
Total assets	1,796,443,776.05	395,684,577.89	2,913,631.67	(7,486,527.47)	60,174,903.49	2,247,730,361.63
Total liabilities	518,169,798.59	293,250,405.39	12,773,440.27	(7,486,527.47)	-	816,707,116.78
Other significant non-cash items						
- other non-cash expenses other than depreciation and amortization	16,858,777.65	-	-	-	-	16,858,777.65
- long-term equity investment jointly controlled enterprises and associated companies	-	-	-	-	60,589,759.15	60,589,759.15
- other increment of non-current assets other than long-term equity investment	82,431,809.97	2,197,299.00	-	-	-	84,629,108.97

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (X). OTHER SIGNIFICANT EVENTS *(Continued)*

### 2. Segment Reporting *(Continued)*

#### (2) Geographic Information

The following table sets out information about the geographical location of the Group's revenue from external customers. The geographical location of customers is based on the location at which the goods delivered or the services were provided.

Items	2011	2010
China	1,783,015,467.75	1,593,468,033.51
International	21,842,096.54	4,237,233.68
Total	<u>1,804,857,564.29</u>	<u>1,597,705,267.19</u>

The non-current assets of the Group are located in the mainland of China.

#### (3) Major Customers

All revenues of the Group from individual customers are lower than 10% of total revenues of the Group for the year 2011 and 2010.

### 3. Risk and sensitivity analysis and fair value of financial instruments

The Group is exposed to the following risks from financial instruments during its ordinary activities:

- Credit risk
- Liquidity risk
- Interest rate risk
- Foreign exchange risk

This note presents information about the Group's exposure to each of the above risks and their sources, the Group's objectives, policies and processes for measuring and managing risks, etc.

The goal of the Group's involvement in risk management is to balance the risk and revenue and minimize the adverse effects on financial results of the Group brought by the financial risks. The Group's risk management policies are established to identify and analyze the risks confronted by the Group, to set appropriate risk limits and control program, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The internal audit department of the Group also examines whether the exercise of internal control system meets the requirements of risk management policies on periodical and random basis.

#### (1) Credit Risk

Credit risk refers to the risk of financial loss incurred to one party of the financial instrument due to the other party's failure of performing its duty. The Group's credit risk is primarily attributable to monetary capital and accounts receivables, etc.. Exposure to these credit risks are monitored by management on an ongoing basis.

As the Group principally puts monetary funds excluding cash to the financial institutions with good credit standing, the management considers that there is no significant credit risk and the Group will not incur loss from the counterparty's default.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (X). OTHER SIGNIFICANT EVENTS *(Continued)*

### 3. Risk analysis and sensibility analysis for financial instrument and fair value *(Continued)*

#### (1) Credit Risk *(Continued)*

In respect of receivables, the sales department of the Group has established a credit policy under which individual credit evaluations are performed on all customers to determine the amount and term of credit. Credit grading is depending on the financial condition, external grading and bank credit record (if any). Generally, except for deposit for warranty, all payments have to be paid by the end of the negotiated credit term. The group authorized credit term to customers according to their payment records and transaction performance, generally, the credit term will be one to three months. Normally, the Group does not require collateral from customers.

In monitoring customer credit risk, customers are grouped according to some factors, such as ageing and maturity date.

The accounts receivable of the Group and the Company as at 31st December 2010 and 31st December 2011 that are overdue but not impaired assessed via individual and collective basis are not significant.

The credit risk of the Group is principally impacted by self-characteristics of each customer other than their industries or countries and areas where their businesses operate. Therefore, significant concentration of credit risk is principally attributable to individual customers' significant accounts receivable. 16.86% (2010: 13.54%) of the total accounts receivable and other receivables was due from the Group's top five buyers.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet. The Group does not provide any other guarantees resulted in credit risk exposure.

#### (2) Liquidity risk

Liquidity refers to the risk of short of funds when an enterprise performs its duty related to financial liabilities. The Group and its subsidiaries are responsible for their own cash management, including short-term investment for surplus cash and the raising of loans to satisfy expected cash demands (if the amount of borrowings exceeds the preset limits, the approval from the board of directors is required). The Group's policy is to regularly monitor its short-term and long-term liquidity requirements and its compliance with lending covenants, to ensure that it maintains sufficient reserves of cash, readily realizable marketable securities and adequate committed lines of funding from major financial institutions to meet its liquidity requirements in the short and longer term.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (X). OTHER SIGNIFICANT EVENTS (Continued)

### 3. Risk analysis and sensibility analysis for financial instrument and fair value (Continued)

#### (2) Liquidity risk (Continued)

As at the balance sheet date, the residual contractual term of the financial assets and liabilities of the Group calculated at the undiscounted contractual cash flow (including at contractual interest (in the case of floating rate, at the prevailing interest as at 31st December) and their earliest date required to be repaid are as follows:

Unit: RMB

Items	2011 Undiscounted contractual cash flow				Total	Carrying amount at balance sheet
	Within one year or on demand	1-2 years	2-5 years	Over 5 years		
<b>Financial assets</b>						
- Cash at bank and on hand	192,200,330.65	-	-	-	192,200,330.65	192,200,330.65
- Accounts receivable and other receivables	299,175,379.24	-	-	-	299,175,379.24	299,175,379.24
- Bills receivable	104,034,946.22	-	-	-	104,034,946.22	104,034,946.22
Sub-total	595,410,656.11	-	-	-	595,410,656.11	595,410,656.11
<b>Financial liabilities</b>						
- Short term loans	(104,649,545.78)	-	-	-	(104,649,545.78)	(100,000,000.00)
- Accounts payable and other payables	(404,597,639.92)	-	-	-	(404,597,639.92)	(404,597,639.92)
- Employee benefits payable	(26,050,999.69)	(3,124,236.31)	(4,585,874.65)	(1,155,605.19)	(34,916,715.84)	(33,498,389.64)
- Bills payable	(46,596,910.09)	-	-	-	(46,596,910.09)	(46,596,910.09)
- Taxes payable	(7,310,302.86)	-	-	-	(7,310,302.86)	(7,310,302.86)
- Financial lease amount payable	(342,168.88)	(342,168.88)	(1,026,506.64)	(1,710,844.60)	(3,421,689.00)	(2,132,090.90)
Sub-total	(589,547,567.22)	(3,466,405.19)	(5,612,381.29)	(2,866,449.79)	(601,492,803.49)	(594,135,333.41)
Net amount	5,863,088.89	(3,466,405.19)	(5,612,381.29)	(2,866,449.79)	(6,082,147.38)	1,275,322.70

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (X). OTHER SIGNIFICANT EVENTS *(Continued)*

### 3. Risk analysis and sensibility analysis for financial instrument and fair value *(Continued)*

#### (2) Liquidity risk *(Continued)*

Unit: RMB

Items	2010 Undiscounted contractual cash flow				Total	Carrying amount at balance sheet
	Within one year or on demand	1-2 years	2-5 years	Over 5 years		
<b>Financial assets</b>						
- Cash at bank and on hand	296,294,409.56	-	-	-	296,294,409.56	296,294,409.56
- Accounts receivable and other receivables	266,448,040.77	-	-	-	266,448,040.77	266,448,040.77
- Bills receivable	115,906,620.42	-	-	-	115,906,620.42	115,906,620.42
Sub-total	<u>678,649,070.75</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>678,649,070.75</u>	<u>678,649,070.75</u>
<b>Financial liabilities</b>						
- Short term loans	(47,221,008.64)	-	-	-	(47,221,008.64)	(46,000,000.00)
- Accounts payable and other payables	(250,918,457.83)	-	-	-	(250,918,457.83)	(250,918,457.83)
- Employee benefits payable	(27,119,846.65)	(2,866,395.26)	(4,154,083.76)	(2,285,744.91)	(36,426,070.58)	(34,656,409.79)
- Bills payable	(20,426,973.00)	-	-	-	(20,426,973.00)	(20,426,973.00)
- Taxes payable	(4,870,643.57)	-	-	-	(4,870,643.57)	(4,870,643.57)
- Financial lease amount payable	(342,168.88)	(342,168.88)	(1,026,506.64)	(2,053,014.40)	(3,763,858.80)	(2,345,300.00)
Sub-total	<u>(350,899,098.57)</u>	<u>(3,208,564.14)</u>	<u>(5,180,590.40)</u>	<u>(4,338,759.31)</u>	<u>(363,627,012.42)</u>	<u>(359,217,784.19)</u>
Net amount	<u>327,749,972.18</u>	<u>(3,208,564.14)</u>	<u>(5,180,590.40)</u>	<u>(4,338,759.31)</u>	<u>315,022,058.33</u>	<u>319,431,286.56</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (X). OTHER SIGNIFICANT EVENTS *(Continued)*

### 3. Risk analysis and sensibility analysis for financial instrument and fair value *(Continued)*

#### (3) Interest Rate Risk

The Group's exposure to fair value interest rate risk and cash flow interest rate risk mainly arise from interest-bearing financial instruments with fixed rate and floating rate. The Group determined the proportion of fixed interest rate and floating interest rate risk based on the market conditions and maintained an appropriate mix of fixed interest rate and floating interest rate through regular review and supervision. The Company did not hedge interest rate risk with derivative financial instruments.

(a) The interest-bearing financial instruments held by the Group as at 31st December are as follows:

<b>Items</b>	<b>2011 Amount</b>	<i>Unit: RMB</i> <b>2010 Amount</b>
Fixed interest rate financial instruments		
Financial assets		
– monetary fund	1,500,000.00	1,500,000.00
Financial liabilities		
– short-term borrowings	–	(46,000,000.00)
<b>Total</b>	<u><u>1,500,000.00</u></u>	<u><u>(44,500,000.00)</u></u>
Floating interest rate financial instruments		
Financial assets		
– monetary fund	190,700,330.65	294,794,409.56
Financial liabilities		
– short-term borrowings	(100,000,000.00)	–
<b>Total</b>	<u><u>90,700,330.65</u></u>	<u><u>294,794,409.56</u></u>

#### (b) Sensitivity Analysis

As at 31st December 2011, if the interest rates had been 1 basis point higher/lower and all other variables held constant, the net profit and shareholder equity of the Group would increase/decrease RMB7,709.53 (2010: RMB25,458.48).

The sensitivity analysis above indicates the instantaneous change in the net profit and equity that would arise assuming that the change in interest rates had occurred at the balance sheet date and had been applied to re-measure those financial instruments held by the Group which expose the Group to fair value interest rate risk at the balance sheet date. In respect of the exposure to cash flow interest rate risk arising from floating rate non-derivative instruments held by the Group at the balance sheet date, the impact on the net profit and equity is estimated as an annualised impact on interest expense or income of such a change in interest rates. The analysis is performed on the same basis for the prior year.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (X). OTHER SIGNIFICANT EVENTS *(Continued)*

### 3. Risk analysis and sensibility analysis for financial instrument and fair value *(Continued)*

#### (4) Foreign Exchange Risk

In respect of accounts receivables and payables denominated in foreign currencies other than the functional currency, the Group ensures that its net exposure is kept to an acceptable level by buying or selling foreign currencies at spot rates when necessary to address short-term imbalances.

- (a) The Group's exposure as at 31st December to currency risk arising from recognised major assets or liabilities denominated in foreign currencies is as follows. For presentation purposes, the amounts of the exposure are shown in Renminbi, translated using the spot rate at the balance sheet date.

*Unit: RMB*

	2011				2010			
	EUR	USD	Japanese YEN	HKD	EUR	USD	Japanese YEN	HKD
Cash at bank and on hand	101,068.40	8,873,910.75	-	7,232,592.85	45,197.87	14,047,582.17	-	7,584,368.07
Bills receivable	-	-	-	-	-	495,000.00	-	-
Accounts receivable	-	6,060,997.01	-	-	-	-	-	-
Other receivables	-	-	-	11,994.11	15,359.11	443,950.76	-	-
Accounts payable	-	-	-	-	(11,062,090.82)	(3,497,996.89)	(312,363.44)	-
Advance from customers	(14,389.82)	(10,066,056.00)	-	-	-	(4,272,148.09)	-	-
Total balance sheet exposure	86,678.58	4,868,851.76	-	7,244,586.96	(11,001,533.84)	7,216,387.95	(312,363.44)	7,584,368.07

- (b) The exchange rates of RMB to foreign currency applicable by the Group are as follows:

*Unit: RMB*

Items	Average rate		Reporting date mid-spot rate	
	2011	2010	2011	2010
USD	6.4618	6.7255	6.3009	6.6227
Japanese YEN	0.0812	0.0775	0.0811	0.0813
HKD	0.8308	0.8657	0.8107	0.8509
EUR	8.4845	9.3018	8.1625	8.8065



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (X). OTHER SIGNIFICANT EVENTS *(Continued)*

### 3. Risk analysis and sensibility analysis for financial instrument and fair value *(Continued)*

#### (4) Foreign Exchange Risk *(Continued)*

##### (c) Sensitivity analysis

Assuming all other risk variables other than exchange rate remained constant, a 1% appreciation of the RMB against the USD, Japanese yen, Euro and HKD at 31st December would have increased (decreased) equity and net profit by the amount shown below, whose effect is in RMB and translated using the spot rate at the balance sheet date.

Items	Equity	Unit: RMB
		Net profit
As at 31st December 2011		
USD	(41,385.24)	(41,385.24)
Japanese YEN	–	–
HKD	(61,578.99)	(61,578.99)
EUR	(736.77)	(736.77)
Total	<u>(103,701.00)</u>	<u>(103,701.00)</u>
As at 31st December 2010		
USD	(65,498.69)	(65,498.69)
Japanese YEN	2,697.57	2,697.57
HKD	(62,320.81)	(62,320.81)
EUR	95,009.38	95,009.38
Total	<u>(30,112.55)</u>	<u>(30,112.55)</u>

A 1% depreciation of the RMB against the USD, Japanese yen, Euro and HKD at 31st December would have had the equal but opposite effect on them to the amounts shown above, on the basis that all other variables remain constant.

The above sensitivity analysis has been ascertained assuming that the change in foreign exchange rates had occurred at the balance sheet date and had re-measured the exposure to foreign exchange risk for financial instruments held by the Group at that date. The analysis was performed on the same assumption and method of the previous year.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (X). OTHER SIGNIFICANT EVENTS *(Continued)*

### 3. Risk analysis and sensibility analysis for financial instrument and fair value *(Continued)*

#### (5) Fair value

The carrying amounts of the Group's financial assets and financial liabilities as reflected in the consolidated statement of financial position approximate their respective fair values at 31st December.

#### (6) Determination of Fair value

The main methods and assumptions applied by the Group to estimate the fair value of financial instruments are as follows.

##### (a) Accounts receivable

The fair value is based on present value of future cash flow forecast, and the discount rate is market rate at balance sheet date.

##### (b) Borrowings and other non-derivative financial liabilities

The fair value of borrowings and other non-derivative financial liabilities is based on present value of future cash flow forecast, and the discount rate is market rate at balance sheet date.

##### (c) Interest rates used for determining fair value

The Group uses the interest rate of RMB loan as of the balance sheet date plus an adequate constant credit spread to discount financial instruments. The interest rates used are as follows:

<b>Item</b>	<b>2011</b>	<b>2010</b>
Accounts receivable	6.56%	5.81%
Borrowings and other non-derivative financial liabilities	6.56%	5.81%

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

### 1. Accounts receivable

(1) Analysis of the accounts receivable in accordance with the type of customers:

Type of customers	2011	Unit: RMB
		2010
Third parties	340,328,421.27	278,506,467.41
Related parties	11,330,629.67	11,857,472.41
Sub-total	351,659,050.94	290,363,939.82
Less: provision for bad debt	153,990,342.37	96,896,813.68
Total	<u>197,668,708.57</u>	<u>193,467,126.14</u>

(2) Ageing analysis of the accounts receivable:

Ageing	2011	Unit: RMB
		2010
Within one year (including one year)	104,681,157.63	116,956,045.38
1-2 years (including two years)	95,827,346.73	76,296,967.60
2-3 years (including three years)	62,773,342.74	44,990,483.51
Over three years	88,377,203.84	52,120,443.33
Sub-total	351,659,050.94	290,363,939.82
Less: provision for bad debt	153,990,342.37	96,896,813.68
Total	<u>197,668,708.57</u>	<u>193,467,126.14</u>

The ageing is calculated from the date accounts receivable is recognized.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

(Continued)

### 1. Accounts Receivable (Continued)

(3) Analysis of the accounts receivable by category:

Unit: RMB

Type	Note	2011				2010			
		Carrying amount		Provision for bad and doubtful debts		Carrying amount		Provision for bad and doubtful debts	
		Amount	Proportion (%)	Amount	Proportion (%)	Amount	Proportion (%)	Amount	Proportion (%)
Individually significant and assessed individually for impairment	(4)	39,628,805.82	11.27	10,125,503.46	25.55	24,260,424.16	8.36	3,587,513.37	14.79
Collectively assessed for impairment*									
Group 1	(5)	300,699,615.45	85.51	142,734,838.91	47.47	254,246,043.25	87.56	93,309,300.31	36.70
Group 2	(10)	11,330,629.67	3.22	1,130,000.00	9.97	11,857,472.41	4.08	-	-
Sub-total of groups		<u>312,030,245.12</u>	<u>88.73</u>	<u>143,864,838.91</u>	<u>46.11</u>	<u>266,103,515.66</u>	<u>91.64</u>	<u>93,309,300.31</u>	<u>35.06</u>
Totall		<u>351,659,050.94</u>	<u>100.00</u>	<u>153,990,342.37</u>	<u>-</u>	<u>290,363,939.82</u>	<u>100.00</u>	<u>96,896,813.68</u>	<u>-</u>

Note\*: This category included accounts receivable having been individually assessed but not impaired.

The Company did not have any collateral for the above accounts receivable with provision for bad and doubtful debt.

(4) As at the end of the year, individually significant accounts receivable with individual bad debt provision:

Unit: RMB

Type	Carrying amount	Provision for bad and doubtful debts	Percentage of provision	Reasons for provision
Accounts receivable	39,628,805.82	10,125,503.46	25.55%	Having impairment by using individual assessment method

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

(Continued)

### 1. Accounts Receivable (Continued)

(5) Accounts receivables provided for bad debt using ageing analysis method:

Unit: RMB

Ageing	2011			2010		
	Book balance Amount	Proportion (%)	Bad debt provision	Book balance Amount	Proportion (%)	Bad debt provision
Within one year	80,194,823.79	26.67	4,261,530.10	93,090,813.27	36.61	4,247,731.80
1-2 years	80,536,396.62	26.78	24,160,918.99	65,760,498.97	25.86	19,586,827.03
2-3 years	53,307,387.03	17.73	31,984,432.22	43,274,287.68	17.03	21,600,970.32
Over 3 years	86,661,008.01	28.82	82,327,957.60	52,120,443.33	20.50	47,873,771.16
Total	<u>300,699,615.45</u>	<u>100.00</u>	<u>142,734,838.91</u>	<u>254,246,043.25</u>	<u>100.00</u>	<u>93,309,300.31</u>

(6) There was no significant bad debt provision to be reversed or collected for the accounts receivable for the year.

(7) There was no significant writing-off for the accounts receivable for the year.

(8) Amounts of top five accounts receivable

Unit: RMB

Ranking	Relationship with the Company	Amount	Age	Percentage to total accounts receivable (%)
1st	Third party	14,224,317.81	Over one year	4.04
2nd	Third party	9,936,000.00	Within one year	2.83
3rd	Third party	8,177,400.00	Within one year	2.33
4th	Third party	7,291,088.01	Over one year	2.07
Kunming TOS	Jointly controlled enterprise	<u>6,085,433.84</u>	Within one year	<u>1.73</u>
Total		<u>45,714,239.66</u>		<u>13.00</u>

As names of customers involve the business secret of the Company, we did not disclose the specific names of the top five customers in 2011. In the above balances, there were no accounts receivable due from shareholders holding over 5% (or 5%) shares of the Company entitling voting rights.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

(Continued)

### 1. Accounts Receivable (Continued)

(9) Accounts receivable from related parties

Name of the related party	Note	Relationship with the Company	Amount	Unit: RMB
				Percentage to total accounts receivable (%)
Kunming TOS	VI. 6	Jointly controlled enterprise	6,085,433.84	1.73
Changsha Ser	VI. 6	Subsidiary	244,000.00	0.07
Fujian Kunji	VI. 6	Subsidiary	4,992,195.83	1.42
Trading Center	VI. 6	The subsidiary of the biggest shareholder Company	9,000.00	0.00
Total			<u>11,330,629.67</u>	<u>3.22</u>

As at 31st December 2011, the Company conducted individual assessment on accounts receivable from related parties and made a provision for bad and doubtful debt for Fujian Kunji of RMB1,130,000.00.

### 2. Other Receivables

(1) Analysis of other receivables by the type of customers:

Type	2011	Unit: RMB
		2010
Third parties	15,439,858.98	16,287,576.49
Related parties	8,132,695.97	17,806,897.86
Sub-total	23,572,554.95	34,094,474.35
Less: provision for bad and doubtful debt	<u>3,595,344.13</u>	<u>11,596,944.54</u>
Total	<u>19,977,210.82</u>	<u>22,497,529.81</u>

(2) Ageing analysis of other receivables:

Type	2011	Unit: RMB
		2010
Within one year (including one year)	14,508,931.01	14,814,236.06
1-2 years (including two years)	4,598,950.71	3,576,410.08
2-3 years (including three years)	3,015,855.68	1,010,308.30
Over three years	1,448,817.55	14,693,519.91
Sub-total	23,572,554.95	34,094,474.35
Less: provision for bad and doubtful debt	<u>3,595,344.13</u>	<u>11,596,944.54</u>
Total	<u>19,977,210.82</u>	<u>22,497,529.81</u>

The ageing is calculated from the date other receivables are recognized.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

(Continued)

### 2. Other receivables (Continued)

(3) Analysis of other receivables in accordance with the type below:

Unit: RMB

Type	Note	2011				2010			
		Carrying amount		Provision for bad and doubtful debts		Carrying amount		Provision for bad and doubtful debts	
		Amount	Proportion (%)	Amount	Proportion (%)	Amount	Proportion (%)	Amount	Proportion (%)
Individually significant and assessed individually for impairment	(4)	6,910,074.10	29.31	196,722.87	2.85	29,513,906.14	86.57	10,935,182.64	37.05
Collectively assessed for impairment*									
Group 1	(5)	15,094,281.62	64.03	3,398,621.26	22.52	3,876,006.42	11.37	661,761.90	17.07
Group 2	(10)	1,568,199.23	6.66	-	-	704,561.79	2.06	-	-
Sub-total of groups		<u>16,662,480.85</u>	<u>70.69</u>	<u>3,398,621.26</u>	<u>20.40</u>	<u>4,580,568.21</u>	<u>13.43</u>	<u>661,761.90</u>	<u>14.45</u>
Total		<u>23,572,554.95</u>	<u>100.00</u>	<u>3,595,344.13</u>	<u>-</u>	<u>34,094,474.35</u>	<u>100.00</u>	<u>11,596,944.54</u>	<u>-</u>

Note\*: The type included other receivables not having impairment on single test.

The Company did not have any collateral for the above other receivables with provision for bad and doubtful debt.

(4) As at the end of the year, individually significant other receivables with individual bad debt provision:

Unit: RMB

Type	Carrying amount	Provision for bad and doubtful debts	Percentage of provision	Reasons for provision
1. Staff advances	345,577.36	196,722.87	56.93%	Having impairment by using individual assessment method
2. Xi'an Ser	6,564,496.74	-	-	Related party, no impairment

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

(Continued)

### 2. Other receivables (Continued)

(5) Other receivables provided for bad debt using ageing analysis method:

Unit: RMB

Ageing	2011			2010		
	Carrying amount		Provision for bad and doubtful debts	Carrying amount		Provision for bad and doubtful debts
	Amount	Proportion (%)		Amount	Proportion (%)	
Within one year	11,156,731.22	73.92	554,819.09	3,362,739.99	86.76	190,780.08
1-2 years	2,187,496.46	14.49	1,093,748.23	84,569.23	2.18	42,284.62
2-3 years	744,681.94	4.93	744,681.94	44,808.79	1.16	44,808.79
Over 3 years	1,005,372.00	6.66	1,005,372.00	383,888.41	9.90	383,888.41
Total	<u>15,094,281.62</u>	<u>100.00</u>	<u>3,398,621.26</u>	<u>3,876,006.42</u>	<u>100.00</u>	<u>661,761.90</u>

(6) There was no significant provision for bad and doubtful debt to be reversed or collected for the other receivables for the year.

(7) Write off for the other receivables for the year.

Unit: RMB

Name	Nature of other receivables	Amount of written off	Reason for write off	Whether the amount was caused by connected transaction
Winko	Receivable from subsidiary	9,859,808.60	Note	Yes

Note: Winko was cancelled in February 2011. The above amount was confirmed to be uncollected and was written-off.

(8) Amount of top five other receivables

Unit: RMB

Name	Relationship with the Company	Amount	Ageing	Percentage of total amount of other receivables (%)
Xi'an Ser	Subsidiary	6,564,496.74	Over one year	27.85
Sany Heavy Industry Co., Ltd.	Third party	1,752,000.00	Over one year	7.43
SHENYANG FANTIAN Brand Management Co., Ltd.,	Third party	1,200,400.00	Within one year	5.09
Kunming TOS	Jointly controlled enterprise	930,594.93	Within one year	3.95
Fujian Kunji	Subsidiary	<u>637,604.30</u>	Over one year	<u>2.70</u>
Total		<u>11,085,095.97</u>		

In the above amount, there were no other receivables due from shareholders holding over 5% (or 5%) shares of the Company entitling voting rights.



# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

(Continued)

### 2. Other Receivables (Continued)

(9) Other receivables from related parties

Name	Note	Relationship with the Company	Amount	Unit: RMB
				Percentage of total amount of other receivables (%)
Kunming TOS	VI. 6	Jointly controlled enterprise	930,594.93	3.95
Fujian Kunji	VI. 6	Subsidiary	637,604.30	2.70
Xi'an Ser	VI. 6	Subsidiary	6,564,496.74	27.85
Total			<u>8,132,695.97</u>	<u>34.50</u>

As at 31st December 2011, the Group conducted individual assessment on other receivables due from related parties and considered that there was no need to make provisions for doubtful and bad debts.

### 3. Long-term equity investments

(1) Long-term equity investments by type:

Items	Unit: RMB	
	2011	2010
Investment in subsidiaries	27,193,265.85	47,034,810.70
Investment in jointly controlled enterprises	47,500,223.66	45,965,425.09
Investment in associated companies	14,424,357.29	14,624,334.06
Other long-term equity investments	2,000,000.00	2,000,000.00
Sub-total	91,117,846.80	109,624,569.85
Less: impairment provision	<u>3,500,000.00</u>	<u>21,341,544.85</u>
Total	<u>87,617,846.80</u>	<u>88,283,025.00</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

(Continued)

### 3. Long-term equity investments (Continued)

(2) Analysis of changes of long-term equity investment for the year:

Unit: RMB

Invested company	Investment cost	Opening balance	Increase/decrease	Closing balance	Percentage of	Percentage of	Explanation for difference between (A) and (B)	Impairment provision	Impairment provision for the year	Cash dividend for the year
					shareholding in the invested company (%) (A)	voting rights in the invested company (%) (B)				
<b>Under equity method:</b>										
<b>jointly controlled enterprises</b>										
Kunming TOS	24,739,533.99	45,965,425.09	1,534,798.57	47,500,223.66	50.00	50.00	-	-	-	6,000,000.00
<b>Under equity method:</b>										
<b>associated company</b>										
Xi'an Ruite	14,000,000.00	14,624,334.06	(199,976.77)	14,424,357.29	23.34	23.34	-	-	-	-
<b>Under cost method:</b>										
<b>subsidiary</b>										
Xi'an Ser	21,693,265.85	21,693,265.85	-	21,693,265.85	45.00	60.00	Note	-	-	-
Kunji Transportation	500,000.00	500,000.00	(500,000.00)	-	100.00	100.00	-	-	-	-
Winko	19,341,544.85	19,341,544.85	(19,341,544.85)	-	96.74	96.74	-	-	-	-
General Machine	3,000,000.00	3,000,000.00	-	3,000,000.00	100.00	100.00	-	-	-	29,130,802.55
Fujian Kunji	2,500,000.00	2,500,000.00	-	2,500,000.00	50.00	60.00	Note	1,500,000.00	1,500,000.00	-
Sub-total	47,034,810.70	47,034,810.70	(19,841,544.85)	27,193,265.85	-	-	-	1,500,000.00	1,500,000.00	29,130,802.55
<b>Under cost method:</b>										
<b>other long-term equity investment</b>										
Yunnan Cheng Jiang										
Copper Products Plant	2,000,000.00	2,000,000.00	-	2,000,000.00	40.00	40.00	-	2,000,000.00	-	-
<b>Total</b>	<b>87,774,344.69</b>	<b>109,624,569.85</b>	<b>(18,506,723.05)</b>	<b>91,117,846.80</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>3,500,000.00</b>	<b>1,500,000.00</b>	<b>35,130,802.55</b>

Note: the percentage of voting rights of Company in the above companies is determined by the percentage to total voting rights in the board of directors of the above companies. The Company can have control to the above companies' finance and operating decisions. Therefore, the Company treated these companies as subsidiaries and adopts cost method for accounting.

(3) Information of jointly controlled enterprises and associated companies:

Please refer to note V.7(3) for information of jointly controlled enterprise and associated companies.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

(Continued)

### 4. Operating income and operating costs

(1) Operating income and operating costs

Items	Unit: RMB	
	2011	2010
Operating income	1,534,953,705.20	1,385,669,586.95
Including: Income from sales of products	1,514,575,688.54	1,369,877,289.73
Income from rendering services	20,378,016.66	15,792,297.22
Other operating income	8,065,349.58	9,278,693.96
Total operating income	<u>1,543,019,054.78</u>	<u>1,394,948,280.91</u>
Operating costs	<u>1,142,044,017.59</u>	<u>975,122,087.66</u>

(2) Operating income (by business line)

Business	2011		2010	
	Operating income	Operating cost	Operating income	Operating cost
Sales and service of boring machines	<u>1,543,019,054.78</u>	<u>1,142,044,017.59</u>	<u>1,394,948,280.91</u>	<u>975,122,087.66</u>

(3) Operating income from the top five customers in 2011

Ranking	Unit: RMB	
	Operating income	Percentage to total operating income (%)
1st	152,672,649.60	9.89
2nd	41,277,777.79	2.67
3rd	39,203,418.85	2.54
4th	38,358,974.37	2.49
5th	37,602,564.19	2.44
Total	<u>309,115,384.80</u>	<u>20.03</u>

The Company has not disclosed specific names of the top 5 companies for the year 2011, which involved commercial secret of the Group.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

(Continued)

### 5. Investment income

Items	Note	2011	Unit: RMB 2010
Income from long-term equity investment under equity method	(XI). 3	7,334,821.80	9,859,063.47
Income from long-term equity investment under cost method	(XI). 3	29,130,802.55	–
Investment income from disposal of subsidiaries		650,286.89	–
Total		<u>37,115,911.24</u>	<u>9,859,063.47</u>

(1) The amount of Long-term equity investment income under cost method:

Invested company	2011	2010
General Machine	<u>29,130,802.55</u>	<u>–</u>

The distribution of cash dividends of RMB29,130,802.55 to the Company was reviewed and approved at the general meeting of General Machine on 31st December 2011.

(2) The amount of long-term equity investment income under equity method:

Invested company	2011	2010
Kunming TOS	7,534,798.57	9,275,207.46
Xi'an Ruite	(199,976.77)	583,856.01
Total	<u>7,334,821.80</u>	<u>9,859,063.47</u>

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XI). NOTES TO PRINCIPLE ITEMS OF THE PARENT COMPANY'S FINANCIAL STATEMENTS

(Continued)

### 6. Related information of cash flow statement

(1) Supplementary information of the cash flow statement

Supplemental information	Unit: RMB	
	2011	2010
<b>1. Reconciliation of net profit to cash flows from operating activities:</b>		
Net profit	74,831,789.76	187,738,250.72
Add: Provision for impairment of assets	61,489,436.88	394,749.38
Depreciation of fixed assets	32,780,206.96	29,394,932.31
Amortization of intangible assets	2,741,409.28	2,435,077.08
Amortization of long-term deferred expenses	122,044.57	175,362.69
Amortization of deferred income	(205,300.20)	(205,300.20)
Gain on disposal of fixed assets	(1,442,999.72)	(624,889.14)
Financial expenses	2,418,248.06	2,644,083.44
Investment gain	(37,115,911.24)	(9,859,063.47)
Decrease in deferred tax assets ("—" for increase)	9,551,910.99	(649,019.69)
Increase in inventories	(244,262,507.33)	(151,981,978.86)
Increase in operating receivable	(65,530,028.58)	(13,318,285.60)
Increase in operating payable	158,264,235.15	79,027,693.36
Net cash flows from operating activities	<u>(6,357,465.42)</u>	<u>125,171,612.02</u>
<b>2. Net movements in cash and cash equivalents:</b>		
Closing balance of cash	143,087,572.52	248,304,966.05
Less: Opening balance of cash	<u>248,304,966.05</u>	<u>237,844,655.24</u>
Net increase of cash and cash equivalents ("—" for decrease)	<u>(105,217,393.53)</u>	<u>10,460,310.81</u>

(2) Composition of cash and cash equivalents

Items	Unit: RMB	
	2011	2010
1. Cash	143,087,572.52	248,304,966.05
Including: cash on hand	440,099.83	1,031,490.85
bank deposits available on demand	<u>142,647,472.69</u>	<u>247,273,475.20</u>

Note: the above disclosed cash and cash equivalents do not include the amounts monetary funds with restricted usage and short-term investments.

# NOTES TO THE FINANCIAL STATEMENTS

(All amounts expressed in RMB unless otherwise specified)

## (XII). NET CURRENT ASSETS

Items	2011		2010	
	The Group	The Group	The Company	The Company
Current assets	1,658,789,391.49	1,484,762,803.80	1,367,095,530.03	1,155,896,709.04
Less: current liabilities	<u>1,025,911,421.35</u>	<u>771,813,323.08</u>	<u>768,950,641.39</u>	<u>504,847,400.92</u>
Net current assets	<u>632,877,970.14</u>	<u>712,949,480.72</u>	<u>598,144,888.64</u>	<u>651,049,308.12</u>

Unit: RMB  
2010

## (XIII). TOTAL ASSETS LESS CURRENT LIABILITIES

Items	2011		2010	
	The Group	The Group	The Company	The Company
Total assets	2,558,664,361.12	2,247,730,361.63	2,214,523,709.43	1,870,968,386.41
Less: current liabilities	<u>1,025,911,421.35</u>	<u>771,813,323.08</u>	<u>768,950,641.39</u>	<u>504,847,400.92</u>
Total assets less current liabilities	<u>1,532,752,939.77</u>	<u>1,475,917,038.55</u>	<u>1,445,573,068.04</u>	<u>1,366,120,985.49</u>

Unit: RMB  
2010

## SUPPLEMENTAL INFORMATION

### 1. NON-RECURRING GAINS AND LOSSES FOR THE YEAR 2011

<b>Items</b>	<i>Unit: RMB</i> <b>Amount</b>
Gain or loss on disposal of non-current assets	1,393,630.93
Government grants included in the profit or loss for the period (other than those closely related to the normal operating activities of the Company and those subject to a standard fixed amount and intervals in accordance with State policies)	2,552,408.50
Gain or loss from debt restructuring	(905,350.26)
Other non-operating income and expenses other than the above	123,986.64
Effect of income tax	(475,562.62)
Effect of minority interests (after tax)	(19,918.60)
Total	<u>2,669,194.59</u>

### 2. DIFFERENCE BETWEEN DOMESTIC ACCOUNTING STANDARDS AND INTERNATIONAL ACCOUNTING STANDARDS

In 2010, differences of net profit and net asset attributable to the Group in the consolidated financial statement prepared in accordance with China Accounting Standards and Hong Kong Financial Reporting Standards are as follows:

	<i>Unit: RMB'000</i> <b>Net profit</b>	<b>Net asset</b>
In accordance with China Accounting Standards	178,325	1,374,125
Gain on investment in jointly controlled enterprises	–	(8,869)
Amortization of goodwill	–	(1,428)
Adjustment on deferred income	49	–
Others	(4)	185
In accordance with Hong Kong Financial Reporting Standards	<u>178,370</u>	<u>1,364,013</u>

KMPG was the international auditor responsible for auditing the financial statements prepared in accordance with Hong Kong Financial Reporting Standards for the year 2010.

In 2011, the Group prepared and disclosed financial reports only in accordance with China Accounting Standards.

### 3. RETURN ON NET ASSETS AND EARNINGS PER SHARE

The return on net assets and earnings per share prepared in accordance with No.9 of Rules for the Compilation and Submission of Information Disclosure by Public Offering Companies issued by China Securities Regulatory Commission (2010 revised) and regulations of relevant accounting standards are as follows:

<b>Earnings during the reporting period</b>	<b>Weighted average of return on net assets (%)</b>	<b>Earnings per share</b>	<b>Basic earnings per share</b>	<b>Diluted earnings per share</b>
Net earnings attributable to the ordinary shareholders of the Company	3.93%		0.10	0.10
Net earnings attributable to the shareholders of the Company excluding non-recurring gains and losses	3.74%		0.10	0.10

## DOCUMENTS AVAILABLE FOR INSPECTION

- (I) Financial statements signed and stamped by legal representative and financial officer of the Company
- (II) Original copy of Auditors' Report bearing the signatures and seals of the Accounting Firm and Certified Public Accountants
- (III) Original copy of all documents and the drafts of announcements as disclosed in newspapers as specified by the CSRC during the reporting period
- (IV) 2011 Annual Report
- (V) Written confirmation for the 2011 Annual Report by directors and senior management officers
- (VI) Written approval by supervisory committee for 2011 Annual Report prepared by the Board

**Shenji Group Kunming Machine Tool Co., Ltd.**  
**Wang Xing**  
Chairman  
29th March 2012

*Note:* Written confirmation by directors and senior management officers for the 2011 Annual Report

## DECLARATION

The board of directors (the "Board"), directors and senior management officers of the Company warrant that there are no false representations, misleading statements and material omissions in the 2011 annual report of the Company, and are severally and jointly responsible for the authenticity, accuracy and completeness of the content herein.

### Signature of declaratory persons:

#### Directors:

Wang Xing	Zhang Xiaoyi	Li Zhenxiong	Guan Xin
Gao Minghui	Ye Nong	Li Shunzhen	Zhang Tao
Liu Minghui	Li Dongru	Chen Fusheng	Xiao Jianming

#### Senior management officers:

Zhu Xiang	Zhou Guoxing	Xu Kunping	Luo Tao
-----------	--------------	------------	---------

Board of directors  
**Shenji Group Kunming Machine Tool Co., Ltd.**  
29th March 2012

*Note:* Written approval by supervisory committee for 2011 Annual Report prepared by the Board



# DOCUMENTS AVAILABLE FOR INSPECTION

## OPINIONS OF THE SUPERVISORY COMMITTEE

Regarding the 2011 Annual Report (hereafter as the “Annual Report”) provided by the Board, we have the following opinions:

1. The preparation of the Annual Report and the auditing procedures are in strict compliance with laws and regulations, the Articles of Association and rules of the Company’s internal management system;
2. The content and format of the Annual Report were in strict compliance with the regulations of the China Securities Regulatory Commission and Shanghai Stock Exchange. The information included in the Annual Report can truly reflect in all respects the Company’s operating management and financial status and other matters of the year;
3. There is no objection on internal control self-assessment offered by the board of directors;
4. Before providing the above opinions, we did not discover any person related in the preparation of the Annual Report nor has any auditing personnel violated the rule of confidentiality.

### Supervisors:

Shao Li

Tang Hua

Fan Hong

Cai Zemin

Qin Jianzhong

**Shenji Group Kunming Machine Tool Co., Ltd.**

Supervisory Committee

29th March 2012