山西長城微光器材股份有限公司

Shanxi Changcheng Microlight Equipment Co. Ltd.*

(a joint stock limited company incorporated in the People's Republic of China) (Stock Code: 8286)

Annual Report 2006

* For identification only

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This report, for which the directors (the "Directors") of Shanxi Changcheng Microlight Equipment Co. Ltd. (the "Company") collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the GEM for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquires, confirm that, to the best of their knowledge and belief: 1) the information contained in this report is accurate and complete in all material respects and not misleading; 2) there are no other matters the omission of which would make any statement in this report misleading; and 3) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

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Corporate Information

BOARD OF DIRECTORS

Executive Directors

Wang Gen Hai *(Chairman)*
Li Kang Sheng
Tian Qun Xu

Non-executive Director

Lin Yin Ping

Independent Non-executive Directors

Ni Guo Qiang
Shen Ming Hong
Li Li Cai
Chen Yue Jie

SUPERVISORS

Zhang Fu Sheng
Meng Yan
Wang Guang Hua
Bai Yin Quan

COMPANY SECRETARY

Poon Shiu Cheong *CPA*

COMPLIANCE OFFICER

Wang Gen Hai

AUTHORISED REPRESENTATIVES

Wang Gen Hai
Poon Shiu Cheong *CPA*

QUALIFIED ACCOUNTANT

Poon Shiu Cheong *CPA*

AUDITORS

Grant Thornton

PRINCIPAL BANKERS

DBS Bank (Hong Kong) Limited
Taiyuan City Commercial Bank
Hua Xia Bank
Industrial and Commercial Bank of China

AUDIT COMMITTEE

Ni Guo Qiang *(Committee Chairman)*
Shen Ming Hong
Li Li Cai
Chen Yue Jie

HONG KONG SHARE REGISTRAR AND TRANSFER OFFICE

Standard Registrars Limited
26/F Tesbury Centre
28 Queen's Road East
Hong Kong

REGISTERED OFFICE

No. 212 Nanneihuan Street
Taiyuan City
Shanxi Province
PRC

PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Rooms 1318-20, 13th Floor
Hollywood Plaza
610 Nathan Road
Kowloon
Hong Kong

STOCK CODE

8286

COMPLIANCE ADVISER

Quam Capital Limited

Corporate Profile

The Company is principally engaged in the design, research, development, manufacture and sale of image transmission fibre optic products in the People's Republic of China ("PRC"). Image transmission fibre optic products produced by the Company are currently used as intermediate products by different manufacturers in Japan, Korea, Singapore, India, Turkey, Europe, Canada and the US.

Image transmission fibre optic products manufactured by the Company are image transmission devices containing a rigidly fused bundle of optical fibres arranged in an ordered fashion so that images can be transmitted from one end of the optical fibre bundle and displayed on the other end of the bundle. A typical image transmission fibre optic product of the Company would consist of over 10 million optical fibres. Image transmission fibre optic products have become one of the key components for digital image transmission equipment. It is a major component for CCD coupling, one of the critical processes of digital imaging. When compared with the traditional way of using lenses to transmit images, image transmission fibre optic products allow images to be transmitted at a higher speed, and with higher efficiency and lower distortion. Even in a dark or dim environment, images can be transmitted through image transmission fibre optic products without the need for additional lighting.

Traditionally, image transmission fibre optic products are used for the manufacture of specialised image transmitting products such as night vision devices. Nowadays, the use of image transmission fibre optic products has been extended to other areas, such as medical radiography and high performance digital consumer products, including high performance photocopiers and digital cameras.

The Company's overseas listed foreign shares ("H Shares") were listed on GEM on 18 May 2004.

MISSION

The Company is poised to experience steady growth in the future and to be one of the major manufacturers of image transmission and light transmission fibre optic products in the PRC.

Chairman's Statement

On behalf of the board of Directors (the "Board"), I am pleased to present the audited results of Shanxi Changcheng Microlight Equipment Co. Ltd. (the "Company") for the year ended 31 December 2006 to the shareholders of the Company (the "Shareholders"). The results of the Company of the fiscal year 2006 had significantly improved when compared with the same period of last year. For the year ended 31 December 2006, turnover and profits attributable to the Shareholders were approximately RMB42.0 million and approximately RMB9.8 million respectively.

During the year under review, the Company recorded an increase in its results. Turnover and profits attributable to the Shareholders increased by approximately 42.3% and 171.6% respectively compared with last year. The Company's products were distributed to overseas markets such as Europe and Asia.

For the year 2006 ahead, the Company will continue to explore opportunities to strive for growth and profitability despite existing challenges. With the increase of production capacity and capability of Taiyuan Economic and Technology Development Zone (太原經濟技術開發區), the Company's production volume will be increased significantly. The Company will take advantage of low production cost in the PRC, its experience and technological expertise. The Company believes that the production capacity of transmission fibre optic products as well as its profits will increase significantly.

Finally, on behalf of the Board, I would like to express my heartfelt appreciation for the Shareholders' confidence and support in the Company's business and prospects, as well as our employees and staff for their devotion and hard work.

By order of the Board
SHANXI CHANGCHENG MICROLIGHT EQUIPMENT CO. LTD.
WANG GEN HAI
Chairman

Shanxi, the People's Republic of China, 27 March 2007

Financial Summary

The following table summarises the audited results, assets and liabilities of the Company for the five years ended 31 December 2006.

	Year ended 31 December				
	2002	2003	2004	2005	**2006**
	RMB'000	RMB'000	RMB'000	RMB'000	**RMB'000**
Turnover	24,769	30,766	34,968	29,491	**41,956**
Profit from operating activities	8,236	11,145	12,214	5,125	**11,575**
Share of profit/(loss) of an associate	(126)	(30)	7	10	**7**
Profit before income tax	7,422	10,560	11,406	5,135	**11,582**
Tax	434	(1,801)	(2,099)	(1,534)	**(1,802)**
Profit for the year	7,856	8,759	9,307	3,601	**9,780**
Dividend	6,266	–	4,633	–	**–**
Earnings per share – basic *(in RMB)*	0.038	0.042	0.034	0.012	**0.032**

	As at 31 December				
	2002	2003	2004	2005	**2006**
	RMB'000	RMB'000	RMB'000	RMB'000	**RMB'000**
ASSETS AND LIABILITIES					
Total assets	46,730	54,124	81,824	83,951	**94,127**
Total liabilities	(15,987)	(14,622)	(16,540)	(15,066)	**(15,462)**
Total equity	30,743	39,502	65,284	68,885	**78,665**

Note: Certain comparative amounts have been restated due to the adoption of the new or revised standards and interpretations of Hong Kong Financial Reporting Standards effective from 1 January 2005.

Business Review and Prospects

BUSINESS REVIEW

During the year, the Company was principally engaged in the design, research, development, manufacture and sale of image transmission fibre optic products in the PRC.

For the year ended 31 December 2006, the Company reported a turnover of approximately RMB42.0 million (2005: approximately RMB29.5 million), representing an increase of approximately 42.3% from previous year's turnover. This was mainly because the new product of "fibre optic tapers" had been promoted by the Company. The customers has became more familiar with this product. With higher demand and orders from customers, the Company's revenue had increased accordingly.

The gross profit margin ratio for the year ended 31 December 2006 is approximately 53.6%, representing an increase of approximately 2.8% as compared to the previous year. The increase was attributable to the higher gross profit margin ratio of fibre optic tapers. With significant increase in the revenue of fibre optic tapers during the year, the Company's overall gross profit margin increased accordingly.

The profit after tax for the year ended 31 December 2006 increased by approximately 171.6% from approximately RMB3.6 million to approximately RMB9.8 million. The increase in profit was mainly due to the increase of revenue and reduction of the general expenses during the year.

PROSPECTS

With the development of digital image transmission technology especially in the medical and commercial areas, the Directors believe that the demand for image transmission fibre optic products, which forms part of the major components of digital image transmission devices, will remain strong in the future. Hence, the Directors believe that the Company is poised to experience steady growth in the future and to be one of the major manufacturers of image transmission and light transmission fibre optic products in the PRC.

Management Discussion and Analysis

LIQUIDITY AND FINANCIAL RESOURCES

The Company financed its operation primarily with internally generated cash flows and the balance of the net proceeds from the listing of the Company's H Shares on GEM on 18 May 2004.

As at 31 December 2006, the Company had total assets of approximately RMB94.1 million (2005: approximately RMB84.0 million), of which approximately RMB2.8 million (2005: approximately RMB19.7 million) were cash and bank balances.

GEARING RATIO

The gearing ratio of the Company, based on total liabilities to total assets, was approximately 16.4% as at 31 December 2006 (2005: approximately 17.9%).

CAPITAL STRUCTURE AND FOREIGN EXCHANGE RISK EXPOSURE

The books and records of the Company are maintained in RMB. Foreign currency transactions are recorded at the applicable exchange rates ruling at the transaction date as quoted by the People's Bank of China (the "PBOC"). Monetary assets and liabilities denominated in other currencies at the balance sheet date are translated into RMB at the applicable exchange rates ruling at that date as quoted by the PBOC. Exchange differences are dealt with in the income statement.

A majority of the Company's sales was denominated in US dollars while a majority of the Company's cost of sales and capital expenditure were denominated in RMB. Accordingly, the Directors are of the view that, to a certain extent, the Company is exposed to foreign currency exchange risk. For the second half of year 2006, the exchange rate of US dollars to RMB had insignificant fluctuations. The Directors believe that such exposure does not have any significant adverse effects on the Company. Furthermore, the Company has not experienced any material operating difficulties or effects on liquidity as a result of fluctuations in currency exchange rates in the past. Therefore, the Company has not implemented any formal policy in dealing with this foreign exchange risk. For the year ended 31 December 2006, the Company did not enter into any arrangement to hedge its foreign exchange exposure.

PLEDGE OF ASSETS AND BANKING FACILITIES

As at 31 December 2006, the Company did not have any pledge of assets and banking facilities obtained from bank.

SIGNIFICANT INVESTMENT AND MATERIAL ACQUISITION AND DISPOSAL OF SUBSIDIARIES

The Company did not hold material investments or had made any material acquisition and disposal of subsidiaries and associates during the year ended 31 December 2006 (2005: Nil).

FUTURE PLANS FOR MATERIAL INVESTMENTS AND CAPITAL ASSETS

Details of significant future investment plans and expected financial resources for capital expenses of the Company are set out in the section headed “Business Objectives and Future Plans” in the prospectus of the Company dated 10 May 2004 (the “Prospectus”). Save as disclosed above and in the financial statements, the Company had no other significant future investment plan as at 31 December 2006.

EMPLOYEE INFORMATION AND REMUNERATION POLICY

For the year ended 31 December 2006, staff remuneration of the Company was approximately RMB8.2 million (2005: approximately RMB7.4 million) and the Company had a total of approximately 461 employees (2005: approximately 434 employees).

There is no significant change in the Company’s employees and remuneration policy as compared with last year. The Company remunerates its employee, including the Directors, based on their performance, experience and prevailing industry practice.

CAPITAL COMMITMENT

Details of capital commitment are set out in note 26(i) of the financial statements.

CONTINGENT LIABILITIES

As at 31 December 2006, the Company had no material contingent liabilities (2005: Nil).

SEGMENT INFORMATION

Details of the segment information for the year ended 31 December 2005 and 2006 are set out in note 6 to the financial statements.

Business Objectives Review

COMPARISON OF BUSINESS OBJECTIVES WITH ACTUAL BUSINESS PROGRESS

10 May 2004 to 30 June 2004

	Business objectives stated in the Prospectus	Actual progress as at 30 June 2004
Increase production capacity and capability • capital investment in a joint venture between the Company and Shanxi Economic and Trade Limited Liability Company (山西經貿資產經營有限責任公司) (“New Development Zone Joint Venture”) • purchase of machinery	Set up the New Development Zone Joint Venture (as defined below)	The application process of setting up the New Development Zone Joint Venture was still in progress. The Land Use Right Transfer Agreement was signed on 3 December 2004. The Land Use Right Certificate was pending. Upon obtaining the approval in respect of the New Development Zone Joint Venture and the Land Use Right Certificate, the construction of the production plant would commence and machinery would be purchased for production.

Business Objectives Review

From the date of listing on 18 May 2004, use of proceeds has not been utilised by the Company in the following areas because of pending establishment of the New Development Zone Joint Venture. Therefore, the Company could not utilise the proceeds from the placing to invest into the New Development Zone Joint Venture.

	From 18 May 2004 (Date of Listing) to 30 June 2004	
	As stated in the Prospectus	**Actual business progress**
	HK$ million	HK$ million
Increase production capacity and capability		
• capital investment in New Development Zone Joint Venture	14	–
• purchase of machinery		

Note: The Land Use Right Certificate was still pending. A deposit of approximately RMB14.0 million was paid by the Company to the Management Committee of Taiyuan Economic and Technology Development Zone (太原經濟技術開發區管理委員會).

Business Objectives Review

1 July 2004 to 31 December 2004

	Business objectives stated in the Prospectus	Actual progress as at 31 December 2004
Increase production capacity and capability • capital investment in New Development Zone Joint Venture	Commence the construction of the new production plant in the New Development Zone in Taiyuan, Shanxi Province, the PRC	The application process of setting up the New Development Zone Joint Venture was still in progress and the Land Use Right Certificate was still pending. Upon obtaining the approval in respect of the New Development Zone Joint Venture and the Land Use Right Certificate, the construction of the production plant would commence and machinery would be purchased for production.
• purchase of machinery	Purchase of imported drawing machine, drawing machine, imported drawing pattern machine, type A heating oven, type B heating oven, type A heater, type B heater, vacuum pump, bridge crane, horizontal cutter, Φ200 cutter, etc.	

From 1 July 2004, use of proceeds has not been utilised by the Company in the following areas because of pending establishment of the New Development Zone Joint Venture. Therefore, the Company could not utilise the proceeds from the placing to invest into the New Development Zone Joint Venture.

	From 1 July 2004 to 31 December 2004	
	As stated in the Prospectus HK$ million	Actual business progress HK$ million
Increase production capacity and capability		
• capital investment in New Development Zone Joint Venture	7.2	–
• purchase of machinery		

1 January 2005 to 30 June 2005

	Business objectives stated in the Prospectus	**Actual progress as at 30 June 2005**
Increase production capacity and capability	Complete renovation works of the new production plant	The Land Use Right Certificate was issued.
• capital investment in New Development Zone Joint Venture	Install new production facilities in the production plant	The renovation of the new production plant has not yet been completed.
• purchase of machinery	Recruit more production staff and provide training for these new staff	The construction of the new production plant is in progress and the Company has purchased some machineries.

The Company has utilised the proceeds from the Placing in the following areas:

	From 1 January 2005 to 30 June 2005	
	As stated in the Prospectus	**Actual business progress**
	HK$ million	HK$ million
Increase production capacity and capability		
• capital investment in New Development Zone Joint Venture	2.0	11.7 *(Note)*
• purchase of machinery		

Note: For the period from 1 January 2005 to 30 June 2005, approximately HK$13.8 million (approximately RMB14.6 million) has been invested for the acquisition of a piece of land in which approximately HK$6.2 million (approximately RMB6.6 million) was funded by the proceeds from the Placing and approximately HK$7.6 million (approximately RMB8.0 million) was funded by its internal resources. The Directors further confirmed that approximately HK$3.6 million (approximately RMB3.8 million) has been invested into the design and construction of the new production plant and approximately HK$1.9 million (approximately RMB2 million) has been invested for the acquisition of machinery.

The establishment of the New Development Zone Joint Venture was still pending.

Business Objectives Review

1 July 2005 to 31 December 2005

	Business objectives stated in the Prospectus	Actual progress as at 31 December 2005
Increase production capacity and capability • capital investment in New Development Zone Joint Venture • purchase of machinery	Trial production of the new production plant Fine-tuning of the production lines Employ more production staff and provide training for these new staff	The application process of setting up the New Development Zone Joint Venture is still in progress. The Land Use Right Transfer Agreement was signed on 3 December 2004. The Land Use Right Certificate was issued on 2 June 2005. The construction of the production plant is commenced and machineries, like imported wiredrawing machine, wiredrawing block machine have been purchased for production.

The Company has utilised the proceeds from the placing in the following areas:

	From 1 July 2005 to 31 December 2005	
	As stated in the Prospectus	Actual business progress
	HK$ million	HK$ million
Increase production capacity and capability		
• capital investment in New Development Zone Joint Venture	1.0	15.9
• purchase of machinery		

Note: For the period from 1 July 2005 to 31 December 2005, approximately HK$2.1 million (approximately RMB2.2 million) has been invested for the acquisition of a piece of land which was funded by the proceeds from the Placing. Approximately HK$6.5 million (approximately RMB7.0 million) has been invested into the design and construction of the new production plant and approximately HK$7.3 million (approximately RMB7.8 million) has been invested for the acquisition of machinery.

The establishment of the New Development Zone Joint Venture was still pending.

Business Objectives Review

1 January 2006 to 30 June 2006

	Business objectives stated in the Prospectus	**Actual progress as at 30 June 2006**
Increase production capacity and capability • capital investment in New Development Zone Joint Venture • purchase of machinery	Commence commercial production in the new production facilities	The application process of setting up the New Development Zone Joint Venture is still in progress. The construction of production plant is still in progress and the Company had purchased some machinery.

The Company has utilised the proceeds from 1 January 2006 in the following areas:

	As stated in the Prospectus HK$ million	**Actual business progress** HK$ million
Increase production capacity and capability		
• capital investment in New Development Zone Joint Venture	1.0	9.6
• purchase of machinery		

Note: For the period from 1 January 2006 to 30 June 2006, approximately HK$6.5 million (approximately RMB6.8 million) has been invested into the design and construction of the new production plant and approximately HK$3.1 million (approximately RMB3.2 million) has been invested for the acquisition of machinery which was funded by the proceeds from the Placing.

The establishment of the New Development Zone Joint Venture was still pending.

Business Objectives Review

1 July 2006 to 31 December 2006

	Business objectives stated in the Prospectus	Actual progress as at 31 December 2006
Increase production capacity and capability • capital investment in New Development Zone Joint Venture • purchase of machinery	Extensive production.	The application process of setting up the New Development Zone Joint Venture is still in progress. The construction of the production plant and neighbouring roads had not been completed.

The Company has utilised the proceeds from the placing in the following areas:

	From 1 July 2006 to 31 December 2006	
	As stated in the Prospectus	Actual business progress
	HK$ million	HK$ million
Increase production capacity and capability		
• capital investment in New Development Zone Joint Venture	1.0	9.8
• purchase of machinery		

Note: For the period from 1 July 2006 to 31 December 2006, approximately HK$6.7 million (approximately RMB7.0 million) has been invested for the design and construction of the new production plant funded by the proceeds from the Placing. Approximately HK$3.1 million (approximately RMB3.2 million) has been invested for the acquisition of machinery.

The establishment of the New Development Zone Joint Venture was still pending.

Directors and Senior Management

BOARD OF DIRECTORS

Executive Directors

Mr. Wang Gen Hai (王根海), aged 59, is the chairman of the Company, and is mainly responsible for the Company's overall strategic planning, management, business development and new product strategy. Mr. Wang graduated from Shanxi Mining College (山西礦業學院) in 1976 after studying 3 years of mechanical engineering. He has been a senior engineer in the PRC since 1994. He has over 20 years of experience in research and general management in the fibre optic industry. Prior to joining the Company, he was with Taiyuan Changcheng Optics and Electronics Industrial Corporation (太原長城光電子工業公司) ("Taiyuan Changcheng") from 1983 to 2000 as General Manager. He joined the Company in November 2000. Mr. Wang Gen Hai is also the compliance officer of the Company.

Mr. Li Kang Sheng (李抗勝), aged 61, is a Director. Mr. Li has over 30 years of experience in research and general management in the fibre optic industry. Mr. Li graduated from Tianjin University (天津大學) in 1968 with a degree in radio engineering. He has been a senior engineer in the PRC since 1994 and is mainly responsible for overseeing the production and the technical department of the Company. Prior to joining the Company, he had been with Taiyuan Changcheng for 30 years. Mr. Li joined the Company in November 2000.

Mr. Tian Qun Xu (田群戌), aged 68, is a Director. Mr. Tian has over 30 years of experience in research and general management in the optical glass industry. Mr. Tian graduated from Taiyuan Industrial Professional School (太原工業專科學校) in 1961. He has been a senior engineer in the PRC since 1988 and is mainly responsible for the research and development department of the Company. Prior to joining the Company, he had been with Taiyuan Changcheng for almost 40 years. Mr. Tian joined the Company in November 2000.

Non-executive Director

Mr. Lin Yin Ping (林殷平), formerly known as Lin Peng, aged 42, is the vice chairman of the Company. Mr. Lin graduated from Guangdong Provincial Social Science College (廣東省社會科學院) with a master degree in politics and economics. Prior to joining the Company, Mr. Lin was with Shenzhen International Investment Securities Company Limited (深圳國投證券有限公司) as an investment banker. Since 2000, Mr. Lin has been the chairman and general manager of Beijing Gensir Venture Capital Management Limited (北京中澤創業投資管理有限公司) ("Beijing Gensir"), a substantial shareholder of the Company. Mr. Lin has over 10 years of experience in the investment and finance field. He joined the Company in November 2000. The daily management and operation of the Company is carried out by Mr. Wang Gen Hai, Mr. Tian Qun Xu and Mr. Li Kang Sheng and Mr. Lin does not take part in the daily management and operation of the Company. Mr. Lin attends the board of Directors meeting of the Company in the capacity of a director.

Directors and Senior Management

Independent non-executive Directors

Mr. Ni Guo Qiang (倪國強), aged 61, is an independent non-executive Director. Mr. Ni graduated from Beijing Institute of Technology (北京理工大學) in 1989 with a doctorate degree in optical and electrical engineering. He has worked with Beijing Institute of Technology since 1989 and currently is the chief professor of the optic technology doctorate programme in Beijing Institute of Technology. Mr. Ni has been engaged in the research and development of optical technology for more than 20 years. Mr. Ni was appointed by the Company in November 2000.

Mr. Shen Ming Hong (**沈明宏**), aged 39, is an independent non-executive Director. Mr. Shen is the chief executive of International New Economy Investment Company Limited (國科新經濟投資有限公司). Mr. Shen graduated from Hefei Industrial University (合肥工業大學) with a master degree. Mr. Shen was appointed by the Company in November 2000.

Mr. Li Li Cai (黎禮才), aged 66, is an independent non-executive Director. Mr. Li graduated from Wuhan Iron & Steel Institute (武漢鋼鐵學院). He joined Taiyuan Iron & Steel Factory (太原鋼鐵廠) in 1964. Since 1985, Mr. Li has been the Deputy General Manager of Taiyuan Iron & Steel Company (太原鋼鐵（集團）公司). Before his retirement, Mr. Li was the Vice Chairman of Shanxi Taiyuan Stainless Steel Company Limited (山西太鋼不銹鋼股份有限公司), a company listed on the Shenzhen Exchange in the PRC. He has over 30 years of experience in corporate management and investment. Mr. Li was appointed by the Company in June 2002.

Ms. Chen Yue Jie (陳月潔), aged 34, is an independent non-executive Director. Ms. Chen graduated from Shanxi University of Finance and Economics (山西省財經大學) in 1997. Ms. Chen is a qualified accountant registered in the PRC and has been involved in the audits of a number of major companies. Ms. Chen was appointed by the Company in April 2004.

Supervisors

Mr. Zhang Fu Sheng (張府生), aged 55, is a supervisor of the Company. Mr. Zhang completed high school courses and has been working with Taiyuan Wireless Number Six Factory (太原無線電六廠), and since 1994, he has been an assistant manager of Taiyuan Changcheng. He is also the supervisor (監事) of the labour union (聯工代表監事) of Taiyuan Changcheng since 1996. He joined the Company in 2000.

Mr. Meng Yan, (孟焰), aged 51, is a supervisor of the Company. Mr. Meng graduated from China Financial Science Research Institute (中國財政科學研究所) with a doctorate degree in accountancy. Mr. Meng is currently the dean of the faculty of accountancy in the Chinese Central Finance University (中國中央財經大學). Mr. Meng joined the Company in June 2002.

Mr. Wang Guang Hua (王光華), aged 46, is a supervisor of the Company. Mr. Wang is currently the head of one of the workshop of the Company. Prior to joining the Company in March 2002, he has been with Taiyuan Changcheng since 1988.

Mr. Bai Yin Quan (白銀泉), aged 41, is a supervisor of the Company. Mr. Bai graduated from Northeastern Finance University (東北財經大學) in 1988 with a bachelor degree in Finance. He became a registered accountant in the PRC in 1993. He is currently a supervisor of Shanxi Certified Public Accountants (山西會計師事務所). Mr. Bai has over 10 years of experience in accounting and finance. Mr. Bai joined the Company in June 2002.

Senior Management

Mr. Zhu Au Ying (朱歐英), aged 54, is the Production Manager of the Company. Prior to joining the Company in 2000, he was responsible for production management in Taiyuan Changcheng from 1969 to 2000. He is mainly responsible for the overall production management of the Company.

Ms. He Ling Xian (和玲仙), aged 56, is the Financial Controller of the Company. She graduated from Chinese Communist Central College (中共中央學校) in 1995 after studying 3 years of economics. She has been a qualified accountant in the PRC since 1992 and a registered accountant since 2000. Prior to joining the Company in 2000, she was with an accounting firm in Shanxi.

Mr. Fan Ji Min (范繼民), aged 45, is the Technical Improvement Manager of the Company. He graduated from Shanxi Provincial Electronics School (山西省電子工業學校) in 1981 after studying 2 years of radio technology. Prior to joining the Company in February 2001, he had been working in Taiyuan Changcheng since 1981. He became an engineer in the PRC in 1999. He is mainly responsible for overall improvement programmes of the Company. Mr. Fan is an engineer in PRC.

Mr. Guo Zhi Hong (郭志宏), aged 40, is the Administration Manager of the Company. He graduated from Shanxi University (山西大學) in 1989 with a degree in physics. Prior to joining the Company, he has been working in Taiyuan Changcheng from 1989 to 2000. He is mainly responsible for administration and management of the Company.

Ms. Zhang Shu Qin (張淑琴), aged 43, is the Chief Engineer of the Company. She graduated from Shanxi University (山西大學) in 1986 with a degree in chemistry. Prior to joining the Company, she was working in Taiyuan Changcheng from 1986 to 2000. She is mainly responsible for the overall management of the technical department. Ms. Zhang is an advance engineer in the PRC.

Mr. Xie An Ye (解安業), aged 39, is the Secretary of the Board of the Company. He graduated from Technological Management University (中國科技經營管理大學) in 1989 with a professional qualification in applied electronic technology. Prior to joining the Company in 2000, he was with Taiyuan Changcheng from 1990 to 2000. He is mainly responsible for the management and administration of the Company. Mr. Xie is an engineer in the PRC.

Mr. Poon Shiu Cheong (潘兆昌), aged 36, is the Company Secretary and Qualified Accountant of the Company. Mr. Poon graduated from Southern Cross University Australia in 1997 with a Master degree in Business Administration. In 2001, he also obtained Master of Accounting from Central Queensland University Australia. He is a Certified Practising Accountant of CPA Australia and a Certified Public Accountant of the Hong Kong Institute of Certified Public Accountants. Mr. Poon has over 10 years of experience in the field of auditing and accounting. He joined the Company in April 2005.

Report of the Directors

The Directors have the pleasure to present their report together with the audited financial statements of the Company for the year ended 31 December 2006.

PRINCIPAL ACTIVITIES

The Company is principally engaged in the design, research, development, manufacture and sale of image transmission fibre optic products in the PRC.

MAJOR CUSTOMERS AND SUPPLIERS

For the year ended 31 December 2006, the five largest customers and the largest customer of the Company accounted for approximately 97.9% and 51.7% respectively of the Company's total turnover. (For the year ended 31 December 2005: 99.9% and 66.6% respectively). For the year ended 31 December 2006, the five largest suppliers and the largest supplier of the Company accounted for approximately 75.8% and 16.2% respectively of the Company's total purchases (For the year ended 31 December 2005: 74.8% and 19.1% respectively). None of the Directors, or any of their associates, or any shareholder (which, to the best knowledge of the Directors, own more than 5% of the Company's issued share capital) had any beneficial interest in the Company's five largest customers or suppliers.

RESULTS AND APPROPRIATIONS

Details of the Company's results for the year ended 31 December 2006 are set out in the income statement on page 36.

The Directors did not recommend the payment of a final dividend for the year ended 31 December 2006.

FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of the Company for the past five financial years is set out on page 6.

SHARE CAPITAL

There were no movements in either the Company's authorised or issued share capital during the year.

RESERVES

Details of movements in the reserves of the Company during the year are set out in the statement of changes in equity on page 38.

DISTRIBUTABLE RESERVES

As at 31 December 2006, the Company's reserves available for distribution, calculated in accordance with the relevant rules and regulations, amounted to approximately RMB21.1 million (2005: approximately RMB12.3 million).

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company's Articles of Association and there is no restriction against such rights under the Companies Law (Revised) of the PRC.

PROPERTY, PLANT AND EQUIPMENT

Details of movements in property, plant and equipment of the Company during the year are set out in note 12 to the financial statements.

RETIREMENT PLANS

All members of staff are entitled to participate in the public welfare fund, which was set up for the purpose of ensuring that the participating employees will have sufficient means to support their living after retirement. Upon participation, the Company and its employees are required to contribute to such fund. The contributions made by the Company are on the basis of not more than 20% (2005: 20%) of the employees' salaries while the employees are required to contribute at least 8% of their salaries each month.

Once the contribution has been made by the Company for its employees, the Company cannot withdraw the contribution on the basis that the employee has left the Company. For the two years ended 31 December 2005 and 2006, the amount paid by the Company for the pension scheme was approximately RMB1.2 million and RMB1.5 million respectively.

CONNECTED TRANSACTIONS

For the year ended 31 December 2006, the Company had several continuing connected transactions in relation to the lease of land and property from Taiyuan Changcheng to the Company which were exempt from all the reporting, announcement and independent shareholders' approval requirement under Chapter 20 of the Rules Governing the Listing of Securities on GEM ("the GEM Listing Rules").

DIRECTORS AND SUPERVISORS

The Directors who held office during the year and up to the date of this report are:

Executive Directors
Mr. Wang Gen Hai
Mr. Li Kang Sheng
Mr. Tian Qun Xu

Non-executive Director
Mr. Lin Yin Ping

Independent non-executive Directors
Mr. Ni Guo Qiang
Mr. Shen Ming Hong
Mr. Li Li Cai
Ms. Chen Yue Jie

The Supervisors who held office during the year and up to the date of this report are:

Zhang Fu Sheng
Meng Yan
Wang Guang Hua
Bai Yin Quan

DIRECTORS' AND SUPERVISORS' SERVICE CONTRACTS

Except for Ms. Chen Yue Jie, each of the Executive Directors, Non-executive Directors and Independent non-executive Directors has entered into a service contract with the Company for an initial term of three years commencing from 10 November 2003. For Ms. Chen Yue Jie, the service contract with the Company is for an initial term of three years commencing from 20 April 2004. The said service contracts shall continue thereafter until terminated by either party after the expiration of the agreed initial fixed term.

Each of the supervisor of the Company (the Supervisor) has entered into an appointment contract with the Company with effect from 10 November 2003 to 9 November 2006 whereby each of the Supervisors was appointed subject to termination on certain circumstances as stipulated in the relevant appointment contract. The said service contracts shall continue until terminated by either party.

Save as disclosed above, none of the Directors or the Supervisor had entered into service contracts with the Company which were not terminable by the Company within one year without compensation (other than statutory compensation).

DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S BIOGRAPHIES

Biographical details of the Directors, Supervisors and the senior management of the Company are set out on pages 17 to 19.

DIRECTORS' AND SUPERVISORS' INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

As at 31 December 2006, so far as the Directors are aware, the Directors who have any interest and short position in shares, underlying shares or debentures of the Company in the registered capital of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO") (a) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 & 8 of Part XV of the SFO (including interests and short positions which are taken or deemed to have taken under such provisions of the SFO) or (b) which were required pursuant to section 352 of the SFO; to be entered in the register referred to in that section, or (c) which were required, pursuant to the required standards of dealing by the Directors as referred to in Rule 5.46 of the GEM Listing Rules), to be notified to the Company and the Stock Exchange are as follows:

Name	Nature and capacity in the shareholding of the Company	Number of domestic shares	Approximate percentage of holding of the domestic shares of the Company*	Approximate percentage of holding of the total share capital of the Company*
Lin Yin Ping	Interest in a controlled corporation	82,200,000	41.34%	26.61%

Note:

1. Lin Yin Ping holds approximately 78.52% of the equity interest in Beijing Gensir Venture Capital Management Limited ("Beijing Gensir") and Beijing Gensir holds approximately 36.37% of the equity interest in Taiyuan Tanghai Automatic Control Company Limited ("Taiyuan Tanghai"). As Lin Yin Ping is entitled to exercise or control the exercise of one-third or more of the voting power at the general meeting of Beijing Gensir, for the purpose of the SFO, Lin Yin Ping is deemed to be interested in the entire 57,300,000 domestic shares held by Beijing Gensir and 24,900,000 domestic shares held by Taiyuan Tanghai.

* *Shareholding percentages have been rounded to the nearest two decimal places.*

DIRECTORS' AND SUPERVISORS' RIGHTS TO ACQUIRE H SHARES

During the year ended 31 December 2006, none of the Directors or Supervisors of the Company was granted options to subscribe for H shares of the Company. As at 31 December 2006, none of the Directors or the Supervisors nor their spouses or children under the age of 18 had any right to acquire H shares in the Company or had exercised any such right during the year.

DIRECTORS' AND SUPERVISORS' INTERESTS IN CONTRACTS

Save as disclosed, the Directors and Supervisors did not have contracts of significance in relation to the Company's business to which the Company was a party and in which a Director or Supervisor of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or any time during the year.

SHARE OPTION SCHEME

The Company does not have any share option scheme.

SUBSTANTIAL SHAREHOLDERS

As at 31 December 2006, so far as the Directors are aware, the persons who have an interest or short position in the shares and underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Division 2 and 3 of Part XV of the SFO or which will be required, pursuant to section 336 of the SFO to be recorded in the register of the Company or be directly or indirectly interested in 5% or more of the nominal value of any class of issued share capital carrying rights to vote in all circumstances of general meetings are as follows:

Name	Nature and capacity in the shareholding of the Company	Number and type of domestic shares/H shares	Approximate percentage of holding of the domestic shares of the Company*	Approximate percentage of the holding of the H shares of the Company*	Approximate percentage of holding of the total share capital of the Company*
Taiyuan Changcheng Optics and Electronics Industrial Corporation	Registered and beneficial owner of the domestic shares	80,160,000 domestic shares	40.31%	–	25.95%

Name	Nature and capacity in the shareholding of the Company	Number and type of domestic shares/H shares	Approximate percentage of holding of the domestic shares of the Company*	Approximate percentage of the holding of the H shares of the Company*	Approximate percentage of holding of the total share capital of the Company*
Beijing Gensir	Registered and beneficial owner of the domestic shares and interest in a controlled corporation	82,200,000 domestic shares *(Note 1)*	41.34%	–	26.61%
Dandong Shuguang Industrial Group Company Limited ("Dandong Shuguang")	Registered and beneficial owner of the domestic shares	34,000,000 domestic shares	17.10%	–	11.01%
Taiyuan Tanghai	Registered and beneficial owner of the domestic shares	24,900,000 domestic shares	12.52%	–	8.06%
Lin Yin Ping	Interest in a controlled corporation	82,200,000 domestic shares *(Note 2)*	41.34%	–	26.61%
Shen Gang	Interest in a controlled corporation	24,900,000 domestic shares *(Note 3)*	12.52%	–	8.06%
Li Jin Dian	Interest in a controlled corporation	34,000,000 domestic shares *(Note 4)*	17.10%	–	11.01%
Zhang Wen Qin	Family interest	82,200,000 domestic shares *(Note 2)*	41.34%	–	26.61%
Liu Gui Ying	Family interest	34,000,000 domestic shares *(Note 4)*	17.10%	–	11.01%
Ma Fong Ping	Family interest	24,900,000 domestic shares *(Note 3)*	12.52%	–	8.06%

Name	Nature and capacity in the shareholding of the Company	Number and type of domestic shares/H shares	Approximate percentage of holding of the domestic shares of the Company*	Approximate percentage of the holding of the H shares of the Company*	Approximate percentage of holding of the total share capital of the Company*
Liu Li, Luis	Beneficial owner of H shares and interest in a controlled corporation	35,055,000 H shares *(Note 5)*	–	31.87%	11.35%
Lu Jun	Family interest	35,055,000 H shares *(Note 6)*	–	31.87%	11.35%
Kwong Tat Finance Limited	Beneficial owner of H shares	34,155,000 H shares *(Note 5)*	–	31.05%	11.06%

* *Shareholding percentages have been rounded to the nearest two decimal places.*

Notes:

1. Part of these domestic shares (24,900,000 domestic shares) are registered in the name of Taiyuan Tanghai. Taiyuan Tanghai is owned as to approximately 36.37% by Beijing Gensir. As Beijing Gensir is entitled to exercise or control the exercise of one-third or more of the voting power at the general meeting of Taiyuan Tanghai, for the purpose of the SFO, Beijing Gensir is deemed to be interested in the entire 24,900,000 domestic shares held by Taiyuan Tanghai.

2. Part of these domestic shares (57,300,000 domestic shares) are registered in the name of Beijing Gensir. Beijing Gensir is owned as to an approximately 78.52% by Lin Yin Ping, a non-executive Director. The rest of these shares are registered in the name of Taiyuan Tanghai in which Lin Yin Ping has an indirect interest through his shareholdings in Beijing Gensir. As Lin Yin Ping is entitled to exercise or control the exercise of one-third or more of the voting power at the general meeting of Beijing Gensir, for the purpose of the SFO, Lin Yin Ping is deemed to be interested in the entire 57,300,000 domestic shares held by Beijing Gensir and 24,900,000 domestic shares held by Taiyuan Tanghai. Ms. Zhang Wen Qin (張文琴), as the wife of Lin Yin Ping, is taken to be interested in the shares held by Lin Yin Ping by virtue of Part XV of the SFO.

3. These 24,900,000 domestic shares are registered in the name of Taiyuan Tanghai. Taiyuan Tanghai is owned as to approximately 47.28% by Shen Gang. As Shen Geng is entitled to exercise or control the exercise of one-third or more of the voting power at the general meeting of Taiyuan Tanghai, for the purpose of the SFO, Shen Geng is deemed to be interested in the entire 24,900,000 domestic shares held by Taiyuan Tanghai. Ma Fong Ping (馬鳳萍), as the wife of Shen Gang, is taken to be interested in the shares held by Shen Gang by virtue of Part XV of the SFO.

4. These 34,000,000 domestic shares are registered in the name of Dandong Shuguang. Dandong Shuguang is owned as to approximately 48.11% by Li Jin Dian. As Li Jin Dian is entitled to exercise or control the exercise of one-third or more of the voting power at the general meeting of Dandong Shuguang, for the purpose of the SFO, Li Jin Dian is deemed to be interested in the entire 34,000,000 domestic shares held by Dandong Shuguang. Liu Gui Ying (劉桂英), as the wife of Li Jin Dian, is taken to be interested in the shares held by Li Jin Dian by virtue of Part XV of the SFO.

5. Part of these H shares (34,155,000 H shares) are registered in the name of Kwong Tat Finance Limited. Kwong Tat Finance Limited is wholly owned by Liu Li, Luis. The rest of these H shares (900,000 H shares) are registered in the name of Liu Li, Luis. For the purpose of SFO, Liu Li, Luis is deemed to be interested in all the H shares held by Kwong Tat Finance Limited.

6. Lu Jun is the spouse of Liu Li, Luis and is deemed to be interested in all 35,055,000 H shares held by Liu Li, Luis by virtue of Part XV of the SFO.

COMPETING INTEREST

Up to 31 December 2006, none of the Directors, Supervisors and management shareholders of the Company (as defined under the GEM Listing Rules) had any interest in a business which competes or may compete with the business of the Company.

COMPLIANCE ADVISER'S INTEREST

As notified and updated by the Company's compliance adviser, Quam Capital Limited ("QCL") that as at 31 December 2006, Well Foundation Co. Ltd., an associate of QCL was interested in 280,000 H Shares of the Company. Save as disclosed above, none of QCL, its directors, employees and their associates (as defined under the GEM Listing Rules) has an interest in the share capital of the Company, or any right to subscribe for or to nominate persons to subscribe for the shares of the Company.

Pursuant to the compliance adviser agreement dated 1 June 2006 entered into between QCL and the Company, QCL will receive fees for acting as the Company's compliance adviser for the period from 1 June 2006 up to 31 December 2006 or until the compliance adviser agreement is terminated upon the terms and conditions set out therein.

AUDIT COMMITTEE

In compliance with Rules 5.28 and 5.29 of the GEM Listing Rules, the Company has established an audit committee with written terms of reference. The primary duties of the audit committee are to review the Company's annual report and accounts, half-year report, quarterly report and to provide advice and comments thereon to the Board. The audit committee is also responsible for reviewing and supervising the financial reporting procedures and internal control system of the Company.

The audit committee comprises four independent non-executive Directors, Ni Guo Qiang, Shen Ming Hong, Li Li Cai and Chen Yue Jie. Ni Guo Qiang is appointed as the chairman of the audit committee. The audit committee has reviewed with the management the accounting principles and practices adopted by the Company and discussed internal controls and financial reporting matters, including a review of the annual report of the Company for the year ended 31 December 2006, with the Directors.

CORPORATE GOVERNANCE

The Company has complied throughout the period under review with the provisions on board practice and procedures in the GEM Listing Rules, which was substantially revised with effect from 1 January 2005. Subject to the transitional arrangements, the Company will comply with the revised GEM Listing Rules, in particular, the Code on Corporate Governance Practices set out in Appendix 15 of the GEM Listing Rules, from the financial year commencing on 1 January 2005 except that:

The remuneration committee has not yet been established by the Company. This was mainly due to the restricted availability of time for most of the Directors, in particular the Independent non-executive Directors. The Company is now in the progress of forming its remuneration committee and drafting its term of reference. Currently, the Board is responsible for considering the suitability of the Director's remuneration.

The nomination committee has not yet been established by the Company. The Company currently does not have any plans to set up a nomination committee considering the small size of the Board. The Board is responsible for considering the suitability of an individual to act as a Director, and approving and terminating the appointment of a Director.

CODE OF CONDUCT REGARDING SECURITIES TRANSACTIONS BY DIRECTORS

During the year ended 31 December 2006, the Company had adopted a code of conduct regarding securities transactions by Directors on terms no less exacting than the required standard of dealings set out in Rules 5.48 to 5.67 of the GEM Listing Rules. The Company had also made specific enquiry of all Directors and the Company was not aware of any non-compliance with the required standard of dealings and its code of conduct regarding securities transactions by Directors.

PURCHASE, SALES OR REDEMPTION OF LISTED SECURITIES OF THE COMPANY

During the year ended 31 December 2006, there was no purchase, sales or redemption of the Company's listed securities by the Company.

AUDITORS

The Company's auditors, Grant Thornton retire and, being eligible, offer themselves for re-appointment.

DIRECTORS

Executive Directors: Mr. Wang Gen Hai, Mr. Li Kang Sheng and Mr. Tian Qun Xu. Non-executive Director: Mr. Lin Yin Ping. Independent non-executive Directors: Mr. Ni Guo Qiang, Mr. Shen Ming Hong, Mr. Li Li Cai and Ms. Chen Yue Jie.

The Company confirmed that it has received from each of its independent non-executive Directors an annual confirmation of his/her independence pursuant to Rule 5.09 of the GEM Listing Rules and the Company considers each of the independent non-executive Directors to be independent.

On behalf of the Board of Directors
WANG GEN HAI
Chairman

Shanxi, the People's Republic of China, 27 March 2007

Corporate Governance Report

INTRODUCTION

Subject to the deviations as disclosed in this report, the Company has complied with all the code provisions on Corporate Governance Practices as set out in the GEM Listing Rules by establishing a formal and transparent procedure to protect and maximize the interests of shareholders during the period under review.

DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted a code of conduct regarding Directors' securities transactions on terms no less exacting than the required standard of dealings as set out in Rules 5.48 to 5.67 of the GEM Listing Rules. Having made specific enquiry of all Directors, the Directors have complied with such code of conduct and the required standard of dealings and its code of conduct regarding securities transactions by the Directors throughout the year ended 31 December 2006.

BOARD OF DIRECTORS AND BOARD MEETING

The board of Directors, which currently comprises eight Directors, is responsible for corporate strategy, annual and interim results, succession planning, risk management, major acquisitions, disposals and capital transactions, and other significant operational and financial matters. Major corporate matters that are specifically delegated by the board of Directors to the management including the preparation of annual and interim accounts for board approval before public reporting, execution of business strategies and initiatives adopted by the board of Directors, implementation of adequate systems of internal controls and risk management procedures, and compliance with relevant statutory requirements and rules and regulations.

Details of backgrounds and qualifications of the chairman of the Company and other Directors are set out in the section of Directors and Senior Management. All Directors have given sufficient time and attention to the affairs of the Company. Each executive Director has sufficient experience to hold the position so as to carry out his duties effectively and efficiently. Mr. Wang Gen Hai is the chairman of the board of Director and an executive Director and Mr. Li Kang Sheng is the chief executive officer of the Company and an executive Director. There is no relationship among the members of the board of Directors.

To improve the transparency and independency of the corporate governance, the chairman and chief executive officer of the Company are segregated and are not exercised by the same individual since August 2004.

The Company appointed four independent non-executive Directors who have appropriate and sufficient experience and qualification to carry out their duties so as to protect the interests of shareholders. Mr. Ni Guo Qiang, Mr. Shen Ming Hong, Mr. Li Li Cai and Ms. Chen Yue Jie are the independent non-executive Directors. Except Ms. Chen Yue Jie who was appointed on 20 April 2004, all has been appointed as an independent non-executive Director for a term of three years commencing on 10 November 2003 and is subject to re-election at the annual general meeting in accordance with the Company's articles of association. The Company appointed Mr. Lin Yin Ping as a non-executive Director for a term of three years commencing on 10 November 2003 and is subject to re-election at the annual general meeting in accordance with the Company's articles of association.

The board of Directors held a full board meeting for each quarter.

Details of the attendance of the board of Directors are as follows:–

Directors	Attendance
Mr. Wang Gen Hai	4/4
Mr. Li Kang Sheng	4/4
Mr. Tian Qun Xu	4/4
Mr. Lin Yin Ping	0/4
Mr. Ni Guo Qiang	4/4
Mr. Shen Ming Hong	4/4
Mr. Li Li Cai	4/4
Ms. Chen Yue Jie	4/4

Apart from the above regular board meetings of the year, the board of Directors will meet on other occasions when a board-level decision on a particular matter is required. The Directors will receive details of agenda items for decision and minutes of committee meetings in advance of each board meeting.

REMUNERATION OF DIRECTORS

The remuneration committee has not yet been established by the Company. This was mainly due to the restricted availability of time for most of the Directors, in particular the Independent non-executive Directors. The Company is now in the progress of forming its remuneration committee and drafting its term of reference. Currently, the Board is responsible for considering the suitability of the Director's remuneration.

NOMINATION OF DIRECTORS

The nomination committee has not yet been established by the Company. The Company currently does not have any plans to set up a nomination committee considering the small size of the Board. The Board is responsible for considering the suitability of an individual to act as a Director, and approving and terminating the appointment of a Director.

AUDITORS' REMUNERATION

The audit committee of the Company is responsible for considering the appointment of the external auditor and reviewing any non-audit functions performed by the external auditor, including whether such non-audit functions could lead to any potential material adverse effect on the Company. During the year under review, the Company is required to pay an aggregate of approximately RMB340,000 to the external auditors for their audit service. Non-audit services have not been provided by the external auditors to the Company.

AUDIT COMMITTEE

The Company established an audit committee with written terms of reference in compliance with Rules 5.28 and 5.33 of the GEM Listing Rules. The primary duties of the audit committee are to review and supervise the financial reporting process and internal controls system of the Company. The audit committee comprises four members, Mr. Ni Guo Qiang, Mr. Shen Ming Hong, Mr. Li Li Cai and Ms. Chen Yue Jie. All of them are independent non-executive Directors. The chairman of the audit committee is Mr. Ni Guo Qiang.

The audit committee held four meetings during the year under review. Details of the attendance of the audit committee meetings are as follows:

Members	Attendance
Mr. Ni Guo Qiang	4/4
Mr. Shen Ming Hong	4/4
Mr. Li Li Cai	4/4
Ms. Chen Yue Jie	4/4

The Company's unaudited quarterly and interim results and annual audited results during the year ended 31 December 2006 have been reviewed by the audit committee, which was of the opinion that the preparation of such results complied with the applicable accounting standards and requirements and that adequate disclosure have been made.

DIRECTORS' AND AUDITORS' RESPONSIBILITIES FOR ACCOUNTS

The Directors' responsibilities for the accounts and the responsibilities of the external auditors to the shareholders are set out on page 34.

INTERNAL CONTROL

The Company has conducted a review of its system of internal control periodically to ensure the effective and adequate internal control system. The Company convened meeting periodically to discuss financial, operational and risk management control.

INVESTORS RELATIONS

The Company has disclosed all necessary information to the shareholders in compliance with GEM Listing Rules. Meetings are held with media and investors periodically. The Company also replied the enquiries from shareholders timely. The Directors convene the annual general meeting each year to meet the shareholders and answer their enquiries.

Report of the Supervisory Committee

To the shareholders of Shanxi Changcheng Microlight Equipment Co. Ltd.:

The supervisory committee (”the Supervisory Committee”) of Shanxi Changcheng Microlight Equipment Co. Ltd. (the ”Company”) has performed its duties conscientiously in compliance with the Company Law of the PRC, relevant laws and regulations of Hong Kong and the articles of association of the Company. By adhering to the principle of good faith, it has discharged its duties diligently and carried out its work in an honest, reasonable, prudent and proactive manner to safeguard the interests of the Company and the shareholders.

During the year under review, the Supervisory Committee has carefully reviewed the use of proceeds from the placing in accordance with the plan disclosed in the Prospectus of the Company and put forward reasonable recommendations and opinions to the Board in respect of the operation and development plans of the Company. It has monitored strictly and effectively various important decisions made by the Board of directors to ensure that such decisions are in compliance with the laws and regulations of the PRC and the articles of association of the Company, and in the best interests of the shareholders.

The Supervisory Committee has reviewed diligently and was satisfied with the report of the Directors, the audited financial statements to be tabled at the forthcoming annual general meeting of the Company. In the opinion of the Supervisory Committee, the members of the Board, the Chairman and other senior management of the Company have strictly followed the principle of good faith, discharged their duties diligently, honestly worked for the best interests of the Company, performed their duties in accordance with the articles of association, standardised the operation and enhanced the internal control system. No abuse of rights, acts detrimental to the interests of the Company, shareholders and staff, infringement of laws, regulations or the articles of association of the Company by the Directors, chairman and senior management was found.

The Supervisory Committee considered that the performance and economic results of the Company for 2006 were satisfactory and was confident of the development prospect of the Company.

By order of the Supervisory Committee
Zhang Fu Sheng
Chairman of the Supervisory Committee

Shanxi, the People’s Republic of China, 27 March 2007

Independent Auditors' Report

Certified Public Accountants
Member of Grant Thornton International

Grant Thornton
均富會計師行

To the shareholders of Shanxi Changcheng Microlight Equipment Co. Ltd.
(incorporated in the People's Republic of China with limited liability)

We have audited the financial statements of Shanxi Changcheng Microlight Equipment Co. Ltd. (the "Company") set out on pages 36 to 70, which comprise the balance sheet as at 31 December 2006, and the income statement, the statement of changes in equity and the cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The directors of the Company are responsible for the preparation and the true and fair presentation of these financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit and to report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to 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' judgement, 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 true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, 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.

Independent Auditors' Report

OPINION

In our opinion, the financial statements give a true and fair view of the state of affairs of the Company as at 31 December 2006 and of its profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Grant Thornton
Certified Public Accountants
13th Floor, Gloucester Tower
The Landmark
15 Queen's Road Central
Hong Kong

27 March 2007

Income Statement

for the year ended 31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
Revenue	*5*	**41,956**	29,491
Cost of sales		**(19,475)**	(14,507)
Gross profit		**22,481**	14,984
Other income	*5*	**655**	730
Selling and distribution expenses		**(870)**	(823)
Administrative expenses		**(9,981)**	(9,192)
Other operating expenses		**(710)**	(574)
Operating profit		**11,575**	5,125
Share of profit of an associate		**7**	10
Profit before income tax	*7*	**11,582**	5,135
Income tax expense	*10*	**(1,802)**	(1,534)
Profit for the year		**9,780**	3,601
Earnings per share for profit attributable to the equity holders of the Company during the year	*11*		
– Basic		**RMB0.032**	RMB0.012
– Diluted		**N/A**	N/A

Balance Sheet

as at 31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
ASSETS AND LIABILITIES			
Non-current assets			
Property, plant and equipment	*12*	**29,196**	18,156
Land use rights	*13*	**16,773**	17,126
Deposits for acquisition of property, plant and equipment		**14,186**	7,947
Interest in an associate	*14*	**3,073**	3,066
		63,228	46,295
Current assets			
Due from shareholders	*15*	**5,214**	1,815
Due from a director	*16*	**133**	71
Inventories	*17*	**3,096**	4,999
Trade receivables	*18*	**13,416**	9,864
Prepayments, deposits and other receivables		**5,850**	1,104
Tax recoverable		**191**	–
Financial assets at fair value through profit or loss	*19*	**171**	102
Cash and cash equivalents	*20*	**2,828**	19,701
		30,899	37,656
Current liabilities			
Due to directors	*16*	**71**	30
Trade payables	*21*	**266**	321
Tax payable		**–**	377
Accrued liabilities, deposits received and other payables		**4,765**	4,178
		5,102	4,906
Net current assets		**25,797**	32,750
Total assets less current liabilities		**89,025**	79,045
Non-current liability			
Deferred government grants	*22*	**10,360**	10,160
Net assets		**78,665**	68,885
EQUITY			
Equity attributable to Company's equity holders			
Share capital	*23*	**30,886**	30,886
Reserves	*24*	**47,779**	37,999
Total equity		**78,665**	68,885

Wang Gen Hai
Director

Tian Qun Xu
Director

Statement of Changes in Equity

for the year ended 31 December 2006

	Equity attributable to equity holders of the Company					
	Share capital RMB'000 *(Note 23)*	Capital surplus* RMB'000 *(Note 24)*	Statutory surplus reserve* RMB'000 *(Note 24)*	Statutory public welfare fund* RMB'000 *(Note 24)*	Retained earnings* RMB'000	Total equity RMB'000
At 1 January 2005	30,886	18,561	3,976	1,988	9,873	65,284
Profit for the year	–	–	–	–	3,601	3,601
Total recognised income and expense for the year	–	–	–	–	3,601	3,601
Transfer from retained earnings to statutory reserves	–	–	768	384	(1,152)	–
At 31 December 2005 and 1 January 2006	30,886	18,561	4,744	2,372	12,322	68,885
Profit for the year	–	–	–	–	9,780	9,780
Total recognised income and expense for the year	–	–	–	–	9,780	9,780
Transfer from retained earnings to statutory surplus reserve	–	–	976	–	(976)	–
Transfer from statutory public welfare fund to statutory surplus reserve	–	–	2,372	(2,372)	–	–
At 31 December 2006	**30,886**	**18,561**	**8,092**	**–**	**21,126**	**78,665**

* These reserve accounts comprise the reserves of RMB47,779,000 (2005: RMB37,999,000) in the balance sheet.

Cash Flow Statement

for the year ended 31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
Cash flows from operating activities			
Profit before income tax		**11,582**	5,135
Adjustments for:			
Depreciation	7	**2,701**	2,930
Amortisation of land use rights	7	**353**	353
Amortisation of deferred government grants	5	**(300)**	(200)
Fair value gain on financial assets at fair value through profit or loss	5	**(69)**	(2)
Interest income	5	**(245)**	(185)
Dividend income from financial assets at fair value through profit or loss	5	**(17)**	(3)
Loss on disposal of property, plant and equipment	7	**376**	–
Share of profit of an associate		**(7)**	(10)
Write back of allowance for doubtful trade receivables	5	**(4)**	–
Operating profit before working capital changes		**14,370**	8,018
Increase in amount due from shareholders		**(3,399)**	(1,589)
Net movement in balances with the directors		**(21)**	(71)
Decrease in inventories		**1,903**	1,011
(Increase)/decrease in trade receivables		**(3,548)**	228
Increase in prepayments, deposits and other receivables		**(4,746)**	(597)
(Decrease)/increase in trade payables		**(55)**	188
Increase in accrued liabilities, deposits received and other payables		**587**	1,320
Cash generated from operations		**5,091**	8,508
Income taxes paid		**(2,370)**	(1,222)
Net cash from operating activities		**2,721**	7,286

Cash Flow Statement

for the year ended 31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
Cash flows from investing activities			
Additions to land use rights		**–**	(580)
Purchases of property, plant and equipment		**(13,657)**	(7,486)
Government grants received	*22*	**500**	360
Proceeds from disposal of property, plant and equipment		**5**	–
Deposit paid for acquisition of property, plant and equipment		**(6,704)**	(7,947)
Interest received		**245**	185
Dividend income from financial assets at fair value through profit or loss		**17**	3
Net cash used in investing activities		**(19,594)**	(15,465)
Cash flows from financing activities			
Dividends paid		**–**	(3,020)
Net cash used in financing activities		**–**	(3,020)
Net decrease in cash and cash equivalents		**(16,873)**	(11,199)
Cash and cash equivalents at 1 January		**19,701**	30,900
Cash and cash equivalents at 31 December		**2,828**	19,701

Notes to the Financial Statements

for the year ended 31 December 2006

1. GENERAL INFORMATION

Shanxi Changcheng Microlight Equipment Co. Ltd. (the "Company") was incorporated in the Mainland of the People's Republic of China (the "PRC") on 10 November 2000 as a joint stock limited company. The Company was established by Taiyuan Changcheng Optics and Electronics Industrial Corporation ("Taiyuan Changcheng"), transferring all of its operational net assets to the Company for 9,016,000 domestic shares as capital contribution by Taiyuan Changcheng to the Company, and Beijing Gensir Venture Capital Management Limited, Dandong Shuguang Industrial Group Company Limited, Taiyuan Tanghai Automatic Control Company Limited ("Taiyuan Tanghai") and Shanxi Shenhua Material Company Limited subscribing for 5,730,000, 3,400,000, 2,490,000 and 250,000 domestic shares respectively of the Company of nominal value of RMB1.00 each, in cash. Since then, the principal activities of the Company were the manufacture and sale of optical fibre products.

On 28 April 2002, the shareholders of the Company authorised the Company to sub-divide the Company's 20,886,000 issued domestic shares of nominal value of RMB1.00 each into 208,860,000 issued domestic shares of RMB0.1 each.

In connection with the listing of the Company's H shares on the Growth Enterprise Market (the "GEM") of The Stock Exchange of Hong Kong Limited (the "Stock Exchange"), 10,000,000 domestic shares of the Company of RMB0.10 each held by Taiyuan Changcheng was converted into 10,000,000 H shares of RMB0.10 each (the "Sale H Shares").

The Company was listed on the GEM of the Stock Exchange on 18 May 2004 and 110,000,000 H shares, consisting of 100,000,000 new shares and 10,000,000 Sale H Shares with a par value of RMB0.10 each were issued to the public by way of placement at HK$0.40 each.

The financial statements of the Company on pages 36 to 70 have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards and Interpretations issued by The Hong Kong Institute of Certified Public Accountants ("HKICPA"). The financial statements also include the applicable disclosure requirements of the Hong Kong Companies Ordinance and the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited ("GEM Listing Rules").

The registered office of the Company is located at No.212 Nanneihuan Street, Taiyuan City, Shanxi Province, PRC.

The financial statements for the year ended 31 December 2006 were approved for issue by the board of directors on 27 March 2007.

2. ADOPTION OF NEW OR AMENDED HKFRSs

(a) Adoption of new HKFRSs

From 1 January 2006, the Company has adopted all the new and amended HKFRSs, which are first effective on 1 January 2006 and relevant to the Company. The adoption of these new and amended HKFRSs did not result in significant changes in the Company's accounting policies. The specific transitional provisions contained in some of these new or amended HKFRSs have been considered. The adoption of these new and amended HKFRSs did not result in any significant changes in the Company's accounting policies.

(b) New and amended HKFRSs that have been issued but are not yet effective

The Company has not early adopted the following HKFRSs that have been issued but are not yet effective for the year ended 31 December 2006. The directors of the Company anticipate that the adoption of such HKFRSs will not result in material financial impact on the Company's financial statements.

HKAS 1 (Amendment)	Capital Disclosures [1]
HKFRS 7	Financial Instruments: Disclosures [1]
HK(IFRIC) – Int 7	Applying the Restatement Approach under HKAS 29 Financial Reporting in Hyperinflationary Economies [2]
HK(IFRIC) – Int 8	Scope of HKFRS 2 [3]
HK(IFRIC) – Int 9	Reassessment of Embedded Derivatives [4]
HK(IFRIC) – Int 10	Interim Financial Reporting and Impairment [5]
HK(IFRIC) – Int 11	Group and Treasury Share Transactions [6]

1 Effective for annual periods beginning on or after 1 January 2007
2 Effective for annual periods beginning on or after 1 March 2006
3 Effective for annual periods beginning on or after 1 May 2006
4 Effective for annual periods beginning on or after 1 June 2006
5 Effective for annual periods beginning on or after 1 November 2006
6 Effective for annual periods beginning on or after 1 March 2007

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of preparation

The significant accounting policies that have been used in the preparation of these financial statements are summarised below. These policies have been consistently applied to all the years presented unless otherwise stated.

The financial statements have been prepared on the historical cost basis except for financial assets and liabilities. The measurement bases are fully described in the accounting policies below.

It should be noted that accounting estimates and assumptions are used in preparation of the financial statements. Although these estimates are based on management's best knowledge and judgement of current events and actions, actual results may ultimately differ from those estimates. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in note 4.

(b) Associates

Associates are those entities over which the Company is able to exert significant influence, generally accompanying a shareholding of between 20% and 50% of voting rights but which are neither subsidiaries nor investment in a joint venture.

Investment in associates is initially recognised at cost and subsequently accounted for using the equity method. Under the equity method, the Company's interest in the associate is carried at cost and adjusted for the post-acquisition changes in the Company's share of the associate's net assets less any identified impairment loss.

Unrealised gains on transactions between the Company and its associates are eliminated to the extent of the Company's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

(c) Foreign currency translation

The financial statements are presented in Renminbi ("RMB"), which is also the functional currency of the Company.

In the financial statements of the Company, foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. At balance sheet date, monetary assets and liabilities denominated in foreign currencies are translated at the foreign exchange rates ruling at the balance sheet date. Foreign exchange gains and losses resulting from the settlement of such transactions and from the balance sheet date retranslation of monetary assets and liabilities are recognised in the income statement.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

(d) Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Company and when the revenue can be measured reliably on the following bases:

(i) Revenue from the sale of goods is recognised when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Company maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold; and

(ii) Interest income is recognised on a time-proportion basis using the effective interest method.

(e) Property, plant and equipment

Property, plant and equipment, other than construction in progress, are stated at acquisition cost less accumulated depreciation and impairment losses.

The gain or loss arising on retirement or disposal is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the income statement.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. All other costs, such as repairs and maintenance, are charged to the income statement during the financial period in which they are incurred.

Depreciation is provided to write off the cost less residual values over their estimated useful lives, using the straight-line method, at the following rates per annum:

Medium term leasehold building	10 years or over the lease terms, whichever is shorter
Leasehold improvements	10 years or over the lease terms, whichever is shorter
Plant and machinery	10 years
Furniture and fixtures	5 years
Motor vehicles	5 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Construction in progress represents property, plant and equipment under construction, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

(f) Impairment of assets

The Company's land use rights, property, plant and equipment and interest in an associate are subject to impairment testing. They are tested for impairment whenever there are indications that the asset's carrying amount may not be recoverable.

An impairment loss is recognised as an expense immediately for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of fair value, reflecting market conditions less costs to sell, and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of time value of money and the risk specific to the asset.

For the purposes of assessing impairment, where an asset does not generate cash inflows largely independent from those from other assets, the recoverable amount is determined for the smallest group of assets that generate cash inflows independently (i.e. a cash-generating unit). As a result, some assets are tested individually for impairment and some are tested at cash-generating unit level.

An impairment loss is reversed if there has been a favourable change in the estimates used to determine the asset's recoverable amount and only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(g) Leases (as the lessee)

Where the Company has the use of asses held under operating leases, payments made under the leases are charged to the income statement on a straight line basis over the lease terms except where an alternative basis is more representative of the pattern of benefits to be derived from the leased assets. Affiliated costs, such as maintenance and insurance, are expensed as incurred.

(h) Financial assets

The Company's accounting policies for financial assets other than interest in an associate are set out below.

Financial assets other than hedging instruments are classified into the following categories:

– financial assets at fair value through profit or loss

– loans and receivables

Management determines the classification of its financial assets at initial recognition depending on the purpose for which the financial assets were acquired and where allowed and appropriate, re-evaluates this designation at every reporting date.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

(h) Financial assets *(Continued)*

All financial assets are recognised when, and only when, the Company becomes a party to the contractual provisions of the instrument. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

Derecognition of financial assets occurs when the rights to receive cash flows from the investments expire or are transferred and substantially all of the risks and rewards of ownership have been transferred. At each balance sheet date, financial assets are reviewed to assess whether there is objective evidence of impairment. If any such evidence exists, impairment loss is determined and recognised based on the classification of the financial asset.

(i) Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss includes financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit or loss.

Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term.

Financial assets may be designated at initial recognition as at fair value through profit or loss if the following criteria are met:

– the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognising gains or losses on them on a different basis; or

– the assets are part of a group of financial assets which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management strategy and information about the group of financial assets is provided internally on that basis to the key management personnel; or

– the financial asset contains an embedded derivative that would need to be separately recorded.

Subsequent to initial recognition, the financial assets included in this category are measured at fair value with changes in fair value recognised in income statement.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

(h) Financial assets *(Continued)*

(ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are subsequently measured at amortised cost using the effective interest method, less any impairment losses. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction cost.

(i) Inventories

Inventories are carried at the lower of cost and net realisable value. Cost is determined using the weighted average basis, and in the case of work in progress and finished goods, comprise direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is the estimated selling price in the ordinary course of business less the estimated cost of completion and applicable selling expenses.

(j) Accounting for income taxes

Income tax comprises current tax and deferred tax.

Current income tax assets and/or liabilities comprise those obligations to, or claims from, tax authorities relating to the current or prior reporting period, that are unpaid at the balance sheet date. They are calculated according to the tax rates and tax laws applicable to the periods to which they relate, based on the taxable profit for the year. All changes to current tax assets or liabilities are recognised as a component of tax expense in the income statement.

Deferred tax is calculated using the liability method on temporary differences at the balance sheet date between the carrying amounts of assets and liabilities in the financial statements and their respective tax bases. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are recognised for all deductible temporary differences, tax losses available to be carried forward as well as other unused tax credits, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, unused tax losses and unused tax credits can be utilised.

Deferred tax assets and liabilities are not recognised if the temporary difference arises from initial recognition of assets and liabilities in a transaction that affects neither taxable nor accounting profit or loss.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in associates, except where the Company is able to control the reversal of the temporary differences and it is probable that the temporary differences will not reverse in the foreseeable future.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

(j) Accounting for income taxes *(Continued)*

Deferred tax is calculated, without discounting, at tax rates that are expected to apply in the period the liability is settled or the asset realised, provided they are enacted or substantively enacted at the balance sheet date.

Changes in deferred tax assets or liabilities are recognised in the income statement, or in equity if they relate to items that are charged or credited directly to equity.

(k) Cash and cash equivalents

Cash and cash equivalents include cash at bank and in hand.

(l) Retirement benefit costs and short term employee benefits

The Company participates in a central pension fund (the “CPS”), operated by the PRC government, for its eligible staff. The Company is required to contribute a certain percentage of its payroll to the CPS to fund the benefits. The only obligation to the Company with respect to the CPS is to pay the ongoing required contributions under the CPS. Contributions under the CPS are charged to the income statement as they become payable in accordance with the rules of the CPS.

Short-term employee benefits are recognised for the number of paid leave days (usually holiday entitlement) remaining at the balance sheet date. They are included in accrued liabilities and other payables at the undiscounted amount that the Company expects to pay as a result of the unused entitlement.

(m) Financial liabilities

The Company’s financial liabilities include amount due to directors and trade and other payables. They are included in balance sheet line items ‘Trade payables’, ‘Accrued liabilities, deposits received and other payables’ and ‘Due to directors’.

Financial liabilities are recognised when the Company becomes a party to the contractual provisions of the instrument.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Trade and other payables are recognised initially at their fair value and subsequently measured at amortised cost, using the effective interest method.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

(n) Government grants

Grants from the government are recognised at their fair value where there is a reasonable assurance that the grant will be received and the Company will comply with all attached conditions. Government grants relating to costs are deferred and recognised in the income statement over the period necessary to match them with the costs that they are intended to compensate. Government grants relating to the purchase of property, plant and equipment are included in non-current liabilities as deferred government grants and are recognised in the income statement on a straight line basis over the expected useful lives of the related assets.

(o) Research and development cost

Costs associated with research activities are expensed in the income statement as they occur. Costs that are directly attributable to the development phase are recognised as intangible assets provided they meet the following recognition requirements:

(i) demonstration of technical feasibility of the prospective product for internal use or sale;

(ii) the intangible asset will generate probable economic benefits through internal use or sale;

(iii) sufficient technical, financial and other resources are available for completion; and

(iv) the intangible asset can be reliably measured.

Direct costs include employee costs incurred on development along with an appropriate portion of relevant overheads. The costs of internally generated projects developments are recognised as intangible assets. They are subject to the same subsequent measurement method as externally acquired intangible assets.

All other development costs are expensed as incurred.

(p) Related parties

A party is considered to be related to the Company if:

(a) the party, directly or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with, the Company; (ii) has an interest in the Company that gives it significant influence over the Company; or (iii) has joint control over the Company;

(b) the party is an associate;

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

(p) Related parties *(Continued)*

(c) the party is a jointly-controlled entity;

(d) the party is a member of the key management personnel of the Company or its parent;

(e) the party is a close member of the family of any individual referred to in (a) or (d);

(f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or

(g) the party is a post-employment benefit plan for the benefit of employees of the Company, or of any entity that is a related party of the Company.

(q) Provisions, contingent liabilities and contingent assets

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditure expected to settle the obligation.

All provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

Probable inflows of economic benefits to the Company that do not yet meet the recognition criteria of an asset are disclosed as contingent assets.

(r) Share capital

Ordinary shares are classified as equity. Share capital is determined using the nominal value of shares that have been issued.

Any transaction costs associated with the issuing of shares are deducted from the proceeds (net of any related income tax benefit) to the extent they are incremental costs directly attributable to the equity transaction.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets within the next financial year are discussed below:

Net realisable value of inventories

This estimate is based on the current market condition and the historical experience of selling products of similar nature. It could change significantly as a result of competitor actions in response to severe industry cycles. The Company's management reassesses this estimation at the balance sheet dates.

Impairment of receivables and advances

The policy for the impairment of receivables and advances of the Company is based on, where appropriate, the evaluation of collectibility and ageing analysis of accounts and on the management's judgement. A considerable amount of judgement is required in assessing the ultimate realisation of these receivables and advances, including the current creditworthiness and the past collection history of each debtor. If the financial conditions of debtors of the Company were to deteriorate, resulting in an impairment of their ability to make payments, additional provision for impairment may be required.

5. REVENUE AND OTHER INCOME

Revenue, which is also the Company's turnover, represents the net invoiced value of goods sold, after allowances for returns, trade discounts and other taxes related to sales where applicable.

An analysis of the Company's revenue and other income recognised during the year is as follows:

	2006 RMB'000	2005 RMB'000
Revenue:		
Sale of goods	**41,956**	29,491
Other income:		
Amortisation of deferred government grants	**300**	200
Government grants	**20**	340
Bank interest income	**65**	185
Other interest income*	**180**	–
Write back of allowance for doubtful trade receivables	**4**	–
Fair value gain on financial assets at fair value through profit or loss	**69**	2
Dividend income from financial assets at fair value through profit or loss	**17**	3
	655	730

* Other interest income was derived from an advance of RMB5 million to an investment company in the PRC which was unsecured, bore interest at 3.6% per annum and repayable within one year from the balance sheet date. This amount was included in "Prepayments, deposits and other receivables" in the balance sheet.

6. SEGMENT INFORMATION

As over 90% of the turnover and the profit from operating activities of the Company for the years ended 31 December 2005 and 2006 are generated from the manufacture and sale of optical fibre products, no further segment information by business activity has been presented.

The Company has determined that geographical segment based on the location of customers is its primary segment reporting format. The Company's operating businesses are organised and managed separately, according to the location of the customers. In determining the Company's geographical segments, revenues and results are attributed based on the location of the customers. Over 90% of the Company's assets are located in the PRC.

6. SEGMENT INFORMATION *(Continued)*

The following table presents revenue and profit information for each of the Company's geographical segments:

	Hong Kong		PRC		Europe		Total	
	2006	2005	**2006**	2005	**2006**	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000
Segment revenue:								
Sales to external customers	**16,709**	8,068	**4,015**	2,122	**21,232**	19,301	**41,956**	29,491
Segment results	**8,907**	4,216	**2,103**	959	**11,191**	9,531	**22,201**	14,706
Bank interest income							**65**	185
Administrative expenses							**(9,981)**	(9,192)
Other operating expenses							**(710)**	(574)
Operating profit							**11,575**	5,125
Share of profit of an associate							**7**	10
Profit before income tax							**11,582**	5,135
Income tax expense							**(1,802)**	(1,534)
Profit for the year							**9,780**	3,601

7. PROFIT BEFORE INCOME TAX

	2006 RMB'000	2005 RMB'000
Profit before income tax is arrived at after charging:		
Auditors' remuneration	**340**	400
Cost of inventories sold	**19,475**	14,507
Staff costs (including directors' and supervisors' emoluments – Note 8):		
Wages, salaries and other benefits	**6,679**	6,159
Pension scheme contributions	**1,503**	1,196
	8,182	7,355
Depreciation	**2,701**	2,930
Amortisation of land use rights	**353**	353
Net foreign exchange loss	**138**	–
Research and development costs	**558**	468
Minimum lease payments under operating lease rentals in respect of:		
Land and buildings	**672**	672
Loss on disposal of property, plant and equipment	**376**	–

8. DIRECTORS' AND SUPERVISORS' REMUNERATION

Director's and supervisors' remuneration for the year disclosed pursuant to the GEM Listing Rules and Section 161 of the Hong Kong Companies Ordinance is as follows:

	2006 RMB'000	2005 RMB'000
Directors		
Fees	**–**	–
Other emoluments		
Salaries, allowances and benefits in kind	**599**	751
Pension scheme contributions	**9**	14
	608	765

8. **DIRECTORS' AND SUPERVISORS' REMUNERATION** *(Continued)*

The emoluments of each director, on a named basis, are set out below:

	Fees	Salaries, allowances and benefits in kind	Pension scheme contributions	Total
	RMB'000	RMB'000	RMB'000	RMB'000
2006				
Executive directors				
Wang Gen Hai	**–**	**265**	**9**	**274**
Tian Qun Xu	**–**	**163**	**–**	**163**
Li Kang Sheng	**–**	**75**	**–**	**75**
Non executive directors				
Lin Yin Ping	**–**	**48**	**–**	**48**
Ni Guo Qiang#	**–**	**12**	**–**	**12**
Shen Ming Hong#	**–**	**12**	**–**	**12**
Li Li Cai#	**–**	**12**	**–**	**12**
Chen Yue Jie#	**–**	**12**	**–**	**12**
	–	**599**	**9**	**608**
2005				
Executive directors				
Wang Gen Hai	–	290	8	298
Tian Qun Xu	–	182	–	182
Li Kang Sheng	–	183	6	189
Non executive directors				
Lin Yin Ping	–	48	–	48
Ni Guo Qiang#	–	12	–	12
Shen Ming Hong#	–	12	–	12
Li Li Cai#	–	12	–	12
Chen Yue Jie#	–	12	–	12
	–	751	14	765

\# Independent non-executive directors

8. DIRECTORS' AND SUPERVISORS' REMUNERATION *(Continued)*

	2006 RMB'000	2005 RMB'000
Supervisors		
Fees	–	–
Other emoluments		
Salaries, allowances and benefits in kind	14	14
	14	14

The emoluments of each supervisor, on a named basis, are set out below:

	Fees RMB'000	Salaries, allowances and benefits in kind RMB'000	Pension scheme contributions RMB'000	Total RMB'000
2006				
Zhang Fu Sheng	–	2	–	2
Meng Yan	–	5	–	5
Wang Guang Hua	–	2	–	2
Bai Yin Quan	–	5	–	5
	–	14	–	14
2005				
Zhang Fu Sheng	–	2	–	2
Meng Yan	–	5	–	5
Wang Guang Hua	–	2	–	2
Bai Yin Quan	–	5	–	5
	–	14	–	14

8. DIRECTORS' AND SUPERVISORS' REMUNERATION *(Continued)*

There was no arrangement under which a director or supervisor waived or agreed to waive any remuneration during the year.

During the year, no emoluments were paid by the Company to a director or supervisor as an inducement to join, or upon joining the Company, or as compensation for loss of office.

Included in staff costs is key management personnel compensation which comprises the following categories:

	2006	2005
	RMB'000	RMB'000
Short term employee benefits	**613**	765
Post-employment benefits	**9**	14
	622	779

9. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees in the Company for the year included three (2005: three) directors, details of whose remuneration are reflected in the analysis presented in note 8 above. Details of the remuneration of the remaining two (2005: two) non-director, highest paid employees for the year are as follows:

	2006	2005
	RMB'000	RMB'000
Salaries and allowances	**388**	211
Pension scheme contributions	**9**	13
	397	224

9. FIVE HIGHEST PAID EMPLOYEES *(Continued)*

The remuneration of each of the non-director, highest paid individuals is as follows:

	2006	2005
	RMB'000	RMB'000
I	**113**	126
II	**–**	98
III	**284**	–
	397	224

During the year, no emoluments were paid by the Company to the non-director, highest paid employees as an inducement to join or upon joining the Company, or as compensation for loss of office.

10. INCOME TAX EXPENSE

	2006	2005
	RMB'000	RMB'000
Current tax		
– PRC	**1,802**	1,100
Deferred	**–**	434
Total income tax expense	**1,802**	1,534

Hong Kong profits tax has not been provided as the Company had no assessable profits arising in Hong Kong during the year (2005: Nil). Taxes on profits assessable elsewhere have been calculated at the applicable rates of tax prevailing in the jurisdiction in which the Company operates, based on existing legislation, interpretations and practices in respect thereof during the year.

According to the applicable corporate income tax law of the PRC, the Company, which operates in the high technology industrial development zone in Taiyuan (太原高新技術產業開發區), the PRC, and which is registered as a high technology development enterprise, is entitled to a concessionary corporate income tax rate of 15%, which has been applied for the two years ended 31 December 2006 and 2005.

10. INCOME TAX EXPENSE *(Continued)*

Reconciliation between tax expense applicable to profit before income tax using the applicable rate in the PRC to the tax expense at the applicable tax rate is as follows:

	2006 RMB'000	2005 RMB'000
Profit before income tax	**11,582**	5,135
Tax at applicable tax rate of 33% (2005: 33%)	**3,822**	1,695
Effect of concessionary rate granted by local authority and others, net	**(2,018)**	(592)
Effect of temporary differences in prior years	**–**	434
Effect of share of after tax profit of an associate	**(2)**	(3)
Income tax expense	**1,802**	1,534

11. EARNINGS PER SHARE

The calculation of basic earnings per share is based on the profit attributable to equity holders of the Company of RMB9,780,000 (2005: RMB3,601,000) and 308,860,000 shares in issue during the year.

No diluted earnings per share amounts have been presented for the two years ended 31 December 2006 and 2005 as there was no dilutive potential share.

12. PROPERTY, PLANT AND EQUIPMENT

	Medium term leasehold building RMB'000	Leasehold improvements RMB'000	Plant and machinery RMB'000	Furniture and fixtures RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
At 1 January 2005							
Cost	2,539	781	18,220	2,847	1,436	–	25,823
Accumulated depreciation	(1,037)	(268)	(7,856)	(2,027)	(1,185)	–	(12,373)
Net book amount	1,502	513	10,364	820	251	–	13,450
Year ended 31 December 2005							
Opening net book amount	1,502	513	10,364	820	251	–	13,450
Additions	–	–	562	64	–	7,010	7,636
Depreciation	(254)	(78)	(1,839)	(575)	(184)	–	(2,930)
Closing net book amount	1,248	435	9,087	309	67	7,010	18,156
At 31 December 2005							
Cost	2,539	781	18,782	2,911	1,436	7,010	33,459
Accumulated depreciation	(1,291)	(346)	(9,695)	(2,602)	(1,369)	–	(15,303)
Net book amount	1,248	435	9,087	309	67	7,010	18,156
Year ended 31 December 2006							
Opening net book amount	1,248	435	9,087	309	67	7,010	18,156
Additions	–	–	808	149	–	13,165	14,122
Disposals	–	(349)	(32)	–	–	–	(381)
Depreciation	(254)	(78)	(1,851)	(458)	(60)	–	(2,701)
Closing net book amount	994	8	8,012	–	7	20,175	29,196
At 31 December 2006							
Cost	2,539	432	19,502	3,060	1,436	20,175	47,144
Accumulated depreciation	(1,545)	(424)	(11,490)	(3,060)	(1,429)	–	(17,948)
Net book amount	994	8	8,012	–	7	20,175	29,196

The leasehold building of the Company is located at No.212 Nanneihuan Street, Taiyuan City, Shanxi Province in the PRC. The land use right to which the medium term leasehold building attached is held by Taiyuan Changcheng and is leased to the Company for use under an operating lease (Note 26).

13. LAND USE RIGHTS

The Company's interests in land use rights represent prepaid operating lease payments and their net book values are analysed as follows:

	2006 RMB'000	2005 RMB'000
At beginning of the year		
Cost	**17,634**	3,000
Accumulated amortisation	**(508)**	(155)
Net book value	**17,126**	2,845
For the year ended		
Opening net book value	**17,126**	2,845
Additions	**–**	14,634
Amortisation	**(353)**	(353)
Closing net book value	**16,773**	17,126
At end of the year		
Cost	**17,634**	17,634
Accumulated amortisation	**(861)**	(508)
Net book value	**16,773**	17,126

The Company's land use rights are situated in the PRC and are held under medium term leases.

14. INTEREST IN AN ASSOCIATE

	2006 RMB'000	2005 RMB'000
Share of net assets	**3,186**	3,179
Due to an associate	**(113)**	(113)
	3,073	3,066

14. INTEREST IN AN ASSOCIATE *(Continued)*

Particulars of the associate at 31 December 2006 are as follows:

Name	Business structure	Place of registration and operation	Particulars of registered capital	Percentage of equity interest directly attributable to the Company	Principal activities
Shanxi Huayuan Transport Optical Technology and Engineering Company Limited*#	Corporate	PRC	RMB11,000,000	36.36%	Development of fibre optic intelligent transport system business in the PRC

* Not audited by Grant Thornton

\# Registered as a limited liability company under the PRC law

The amount due to an associate is unsecured, interest-free and not repayable within one year.

A summary of the results for the years ended 31 December 2006 and 2005, and of the assets and liabilities of the associate at the respective balance sheet date is set out below:

	2006 RMB'000	2005 RMB'000
Total revenue	**2,744**	1,256
Profit for the year	**18**	28

	2006 RMB'000	2005 RMB'000
Total assets	**11,179**	11,624
Total liabilities	**541**	1,005

15. DUE FROM SHAREHOLDERS

Details of the amounts due from shareholders are set out below:

Name	2006 RMB'000	2005 RMB'000
Taiyuan Changcheng	**5,139**	1,777
Taiyuan Tanghai	**75**	38
	5,214	1,815

The maximum amounts outstanding during the years are as follows:

Name	2006 RMB'000	2005 RMB'000
Taiyuan Changcheng	**5,139**	1,777
Taiyuan Tanghai	**75**	38

The increase in the balance with Taiyuan Changcheng in current year was mainly attributable to the fund advanced to Taiyuan Changcheng.

The amounts due from shareholders are unsecured, interest-free and repayable on demand.

16. BALANCES WITH DIRECTORS

Particulars of the amount due from a director, disclosed pursuant to Section 161B of the Hong Kong Companies Ordinance, are as follows:

Name	2006 RMB'000	Maximum amount outstanding during the year RMB'000	2005 RMB'000
Wang Gen Hai	**133**	137	71

Balances with directors are unsecured, interest-free and repayable on demand.

17. INVENTORIES

	2006	2005
	RMB'000	RMB'000
Raw materials	**569**	410
Work in progress	**1,761**	2,271
Finished goods	**766**	2,318
	3,096	4,999

18. TRADE RECEIVABLES

	2006	2005
	RMB'000	RMB'000
Trade receivables, net	**13,416**	9,864

An allowance for impairment has been made for estimated irrecoverable amounts from the sales of goods of RMB496,000 (2005: RMB500,000). The bases of determination for an allowance for impairment are set out in note 4.

An ageing analysis of the Company's net trade receivables as at the balance sheet date is as follows:

	2006	2005
	RMB'000	RMB'000
0-90 days	**11,361**	7,655
91-180 days	**2,006**	1,848
181-365 days	**49**	361
	13,416	9,864

The trading terms with customers are largely on credit. Invoices are normally payable within three months of issuance. The Company maintains strict control over its outstanding receivables and has credit control policy in place to minimise its credit risk. Overdue balances are regularly reviewed by management.

19. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2006 RMB'000	2005 RMB'000
Held for trading:		
Fair value of interest in unlisted investment fund	**171**	102

The financial assets at fair value through profit or loss of the Company as at the balance sheet date, which are stated at their fair value, represent interest in an unlisted investment fund registered in the PRC.

20. CASH AND CASH EQUIVALENTS

Cash and cash equivalents include the following components:

	2006 RMB'000	2005 RMB'000
Cash at bank and in hand	**2,828**	19,701

Included in cash and cash equivalents of the Company is RMB2,783,000 (2005: RMB19,598,000) of bank balances denominated in RMB placed with banks in the PRC. RMB is not a freely convertible currency.

Cash at bank earns interest at floating rates based on daily bank deposit rates.

At 31 December 2005, certain bank deposits of the Company amounted to RMB2,005,000 were held as guarantee in respect of acquisition of machineries and temporarily not available for use by the Company. This guarantee has been released in January 2006.

21. TRADE PAYABLES

An ageing analysis of the Company's trade payables as at the balance sheet date is as follows:

	2006 RMB'000	2005 RMB'000
0-90 days	**194**	284
91-180 days	**30**	–
181-365 days	**5**	6
Over 365 days	**37**	31
	266	321

22. DEFERRED GOVERNMENT GRANTS

	Notes	RMB'000
At 1 January 2005	(a)	10,000
Additions during the year	(b)	360
Amortisation during the year		(200)
At 31 December 2005 and 1 January 2006		10,160
Additions during the year	(c)	500
Amortisation during the year		(300)
At 31 December 2006		**10,360**

Notes:

(a) The balance represented a subsidy granted by the Taiyuan Ministry of Finance and the Taiyuan City Development and Planning Bureau (太原市發展計劃委員會) for the Company's business expansion project (the "Project") in the Taiyuan ETD Zone.

(b) The balance represented subsidies granted by the Taiyuan Ministry of Finance, the Taiyuan Foreign Trade Bureau (太原市外經貿廳) and the Taiyuan City Science and Technology Bureau (太原市科技局) for enhancing the Company's facilities for development of foreign trade and research and development.

(c) The balance of RMB500,000 represented additional subsidies granted by the Taiyuan Ministry of Finance for the development of the Project.

23. SHARE CAPITAL

	2006	2005
	RMB'000	RMB'000
Authorised, issued and fully paid:		
198,860,000 (2005: 198,860,000) domestic shares of RMB0.10 each	**19,886**	19,886
110,000,000 (2005: 110,000,000) H shares of RMB0.10 each	**11,000**	11,000
	30,886	30,886

Expect for the currency in which dividends are paid and the restrictions as to whether the shareholders can be the PRC investors or foreign investors, domestic shares and H shares rank pari passu with each other.

24. RESERVES

The amounts of the Company's reserves and the movements therein for the current and prior years are presented in the statement of changes in equity on page 38.

The statutory reserves consist of the statutory surplus reserve and the statutory public welfare fund:

(a) Statutory surplus reserve

The Company's articles of association require the appropriation of 10% of the Company's profit after tax each year to the statutory surplus reserve until the balance reaches 50% of the Company's registered capital. According to the provisions of the Company's articles of association, in normal circumstances, the statutory surplus reserve shall only be used for making up losses, capitalisation into share capital and expansion of the Company's production and operations. For the capitalisation of the statutory surplus reserve into share capital, the remaining amount of such reserve shall not be less than 25% of the registered capital.

(b) Statutory public welfare fund

Prior to 1 January 2006, pursuant to the PRC Company Laws, the Company shall make an allocation from its profit after tax at the rate of 5% to 10% to the statutory public welfare fund. The statutory public welfare fund may only be utilised for capital items for the collective welfare of the employees. Individual employees only have the right to the use of the facilities purchased with the statutory public welfare fund and the titles to such facilities will remain with the Company. The statutory public welfare fund forms part of the total equity but is non-distributable other than in the event of liquidation.

Starting from 1 January 2006, pursuant to certain amendments of the PRC Company Laws, the Company is not allowed to establish the statutory public welfare fund. Thus, the balance of statutory public welfare fund of the Company was transferred to statutory surplus reserve during the year and the balance of the statutory public welfare fund as at 31 December 2006 is Nil (2005: RMB 2,372,000).

The capital surplus of the Company represents the excess of the issue price over the nominal value of the Company's shares issued at a premium.

In accordance with the article of association of the Company, the Company's profit available for distribution is determined based on the lower of the amounts reported in accordance with the PRC accounting standards and regulations and those reported in accordance with accounting principles generally accepted in Hong Kong.

25. NOTE TO THE CASH FLOW STATEMENT

Major non-cash transactions

During the year ended 31 December 2006, the Company had the following major non-cash transactions:

(i) A deposit of RMB465,000 paid in the prior year for acquisition of property, plant and equipment was capitalised as property, plant and equipment.

During the year ended 31 December 2005, a deposit of RMB150,000 paid in the prior year for acquisition of property, plant and equipment was capitalised as property, plant and equipment and a deposit of RMB14,054,000 paid in prior year for acquisition of a land use right was capitalised as a land use right.

26. COMMITMENTS

At the balance sheet date, the Company had the following outstanding commitments:

(i) Capital commitments

	Note	**2006 RMB'000**	2005 RMB'000
Contracted, but not provided for			
– Buildings		**10,143**	9,192
– Plant and machinery		**8,860**	5,593
		19,003	14,785
Authorised, but not contracted for			
– Establishment of a joint venture	*(a)*	**15,000**	15,000
		15,000	15,000

Note:

(a) On 18 September 2002, the Company entered into a letter of intent with Shanxi Economic and Trade Limited Liability Company to establish a joint venture, which the Company will own a 60% interest, for the development of the Project (Note 22). The Company's contribution to the joint venture will amount to approximately RMB15,000,000. Up to the date of these financial statements, the joint venture has not yet been established.

26. COMMITMENTS *(Continued)*

(ii) Operating lease commitments

The Company leases its office properties and land use right from Taiyuan Changcheng under operating lease arrangements for terms ranging from five to thirty years with an option to renew the lease and renegotiate the terms at the expiry dates or at dates mutually agreed between the Company and Taiyuan Changcheng. None of the leases include contingent rentals.

At the balance sheet date, the total future minimum lease payments under non-cancellable operating leases payable by the Company are as follows:

	2006	2005
	RMB'000	RMB'000
Within one year	**672**	672
In the second to fifth years, inclusive	**2,488**	2,538
After five years	**11,991**	12,613
	15,151	15,823

27. RISK MANAGEMENT OBJECTIVES AND POLICIES

The Company is exposed to market risk, including primarily changes in currency exchange rates.

The Company does not have written risk management policies and guidelines. However, the board of directors meets periodically to analyse and formulate measures to manage the Company's exposure to market risk, including primarily changes in currency exchange rates. Generally, the Company uses a conservative strategy towards its risk management. As the Company's exposure to the market risk is not significant, the Company has not used any derivatives and other instruments for hedging purposes. The Company does not hold or issue derivative financial instruments for trading purposes.

(a) Interest rate risk

The Company has no significant interest rate risk as there are no interest-bearing borrowings.

(b) Foreign currency risk

The Company is exposed to foreign exchange risk arising from the exposure of RMB against United States Dollars ("USD") and Hong Kong Dollars ("HKD"), respectively, in respect of its receipt of settlement from overseas customers. The directors of the Company believe its exposure to exchange rate risk is not high, and accordingly, the Company does not intend to hedge its exposure to foreign exchange movements.

27. RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

(c) Credit risks

Generally, the maximum credit risk exposure of financial assets is the carrying amount of the financial assets as shown on the face of the balance sheet. Credit risk, therefore, is only disclosed in circumstances where the maximum potential loss differs significantly from the financial asset's carrying amount.

The Company's bank deposits are mainly deposited with banks in Hong Kong and the PRC.

The Company has concentration of credit risk due to its relatively small customer base. The Company performs ongoing credit evaluation of its customers' financial positions. Provision for impairment is based upon a review of the expected collectibility of all receivables.

(d) Fair value

The fair values of current financial assets and financial liabilities are not materially different from their carrying amounts because of their immediate or short term maturity.

28. RELATED PARTY TRANSACTIONS

In addition to the transactions and balances detailed elsewhere in these financial statements, the Company had the following material related party transactions:

	Notes	**2006** **RMB'000**	2005 RMB'000
Rental expenses incurred to a shareholder	*(i)*	**672**	672

Notes:

(i) The rental expenses incurred to Taiyuan Changcheng are for the leases of the office premises and a land use right. The rental expenses incurred to Taiyuan Changcheng were based on mutually agreed terms.

(ii) During the year ended 31 December 2005, the Company entered into an agreement amounted to RMB3,089,400 with Taiyuan Tanghai for acquisition of machineries. A deposit of RMB1,109,000 (2005: RMB309,000) was paid by the Company to Taiyuan Tanghai and was included in "Deposits for acquisition of property, plant and equipment" in the balance sheet.

The directors of the Company have confirmed that all of the above transactions were entered into in the ordinary course of the Company's business.

Notice of Annual General Meeting

NOTICE IS HEREBY GIVEN that an annual general meeting ("**AGM**") of Shanxi Changcheng Microlight Equipment Co. Ltd. (the "**Company**") will be held at No. 212 Nanneihuan Street, Taiyuan City, Shanxi Province, the People's Republic of China (the "**PRC**") on 17 May 2007 (Thursday) at 4:00 p.m. for the following purposes:

I. As ordinary resolutions:

1. to consider and approve the report of the directors of the Company for the year ended 31 December 2006;

2. to consider and approve the report of the supervisory committee of the Company for the year ended 31 December 2006;

3. to consider and approve the audited financial statements of the Company for the year ended 31 December 2006;

4. to consider and approve the re-appointment of Grant Thornton as the auditors of the Company for the year 2007 with a term of office until the conclusion of the next AGM and to authorise the board of directors to fix their remunerations; and

5. to discuss any other issues.

By order of the Board
Wang Gen Hai
Chairman

Taiyuan City, Shanxi Province, the PRC, 28 March 2007

Notes:

1. Any shareholder of the Company entitled to attend and vote at the AGM mentioned above is entitled to appoint one or more proxies to attend and vote at the AGM on his or her behalf in accordance with the articles of association of the Company. A proxy needs not be a shareholder of the Company.

2. In order to be valid, a proxy form of holder of H Shares and, if such proxy form is signed by a person under a power of attorney or other authority on behalf of the appointer, a notarially certified copy of that power of attorney or authority shall be deposited at the Standard Registrars Limited at 26/F Tesbury Centre, 28 Queen's Road East, Hong Kong ("the Company's Share Registrar") not less than 24 hours before the time for holding the AGM or 24 hours before the time appointed for taking the poll.

3. In order to be valid, a proxy form of holder of domestic shares and, if such proxy form is signed by a person under a power of attorney or other authority on behalf of the appointer, a notarially certified copy of that power of attorney or authority shall be deposited at the registered address of the Company not less than 24 hours before the time for holding the AGM or 24 hours before the time appointed for taking the poll.

4. Shareholders of the Company or their proxies shall produce documents of their proof of identity when attending the AGM.

Notice of Annual General Meeting

5. A proxy may exercise the right to vote by a show of hands or by poll. However, if more than one proxy is appointed by a shareholder, such proxies shall only exercise the right to vote by poll.

6. The register of shareholders of the Company will be closed from 17 April 2007 to 17 May 2007 (both days inclusive), during which no transfer of shares will be registered. As regards holders of H Shares and in order to ascertain the entitlement to attendance at the AGM, all properly completed transfer forms accompanied by the relevant share certificate must be lodged with the Company's Share Registrar not later than 16 April 2007 at 4:00 p.m. for registration.

7. Shareholders of the Company who intend to attend the AGM have to notify in writing of their attendance by sending such notice to the Company by hand, post or fax (fax number: 86 351 706 5996) not later than 26 April 2007.

8. Registered address of the Company and the contact details of the Company are as follows:

   No. 212 Nanneihuan Street
   Taiyuan City
   Shanxi Province
   The PRC
   Fax number: 86 351 706 5996

9. The AGM is expected to last for about half a day. Shareholders or proxies are reminded that any expenses in transportation, accommodation and meals will be incurred at their own cost.