

## BUSINESS REVIEW AND OPERATION ANALYSIS

During the first half of the year 2001, the PRC government continued to implement prudent monetary policy and positive fiscal policy, which facilitated the economic development with approximately 8% growth of the national economy. However, agricultural machinery industry was adversely affected by factors including the slow increase in farmers' income, adjustment in economic structure of the agricultural sector and the reduction in traditional agricultural areas. Consequently, the sluggish market conditions continued and there was no improvement in the keen competition of the market. The production and sales of the agricultural machinery industry continued to decline dramatically during the first half of the year 2001. The sales of large and medium tractors in the market decreased by 23.42% over the same period of last year, while the sales of small tractors decreased by 28.47% over the same period of last year.

For the six months ended 30 June 2001, the Group recorded a turnover of RMB912,170,000, representing a decrease of 11.24% over the corresponding period of last year and incurred a loss of RMB37,950,000, the loss was reduced by RMB59,150,000 when compared to the corresponding period of last year. The operating results have been improved.

During the period, the Company sold 3,343 large and medium tractors, representing a decrease of 1.2% over the corresponding period of previous year, of which 2,359 are crawler tractors, representing a decrease of 27.99% over the corresponding period of previous year. The Company also sold 28,880 small tractors, representing a decrease of 28.22% over the corresponding period of previous year. Although the sales of large and medium wheeled tractors increased by 811% over the same period of last year, the sales volume was too small to compensate for the decrease in profit from principal products.

Confronting the severe market situation and keen competition, the management strengthened its control over target cost and adjustment in product mix which received obvious results: gross profit margin increased by 1.5 percentage points over the same period of previous year; the newly developed large wheeled tractors and Dongfanghong 30/40 achieved positive sales results with their good quality and capacity. Sales of these two products increased substantially over the corresponding period of last year. The export of large tractors increased significantly over the corresponding period of last year. Sales of other products including T90 industrial bulldozer, harvesting machinery, self-generated power station, and Dongfanghong-1000 increased substantially over the previous year.

During the reporting period, the sales of 50-65 horse-power medium tractors of First Tractor Qingjiang Tractor Company Limited, the Company's subsidiary, decreased by 26.4% over the same period of last year. The sales of 25-40 horse-power medium tractors of First Tractor Ningbo C.S.I. Tractor and Automobile Corp., Limited increased by 23% over the same period of last year. The sales of harvesting machinery of Yituo (Luoyang) Harvester Co., Ltd. increased by 199% over the corresponding period of last year. The turnover and profit of Zhenjiang Huachen Huatong Road Machinery Company Limited, with road machines as its principal products, increased significantly through their efforts in utilizing the benefits of infrastructure investment, adjusting product mix, developing new products and improving the operating system.

During the first half of the year 2001, the Company actively established a new reward sharing system to motivate employees' initiatives and implemented a series of effective measures in new quality management and product mix adjustment.

As a result of various measures, there was improvement in the Company's operating results as compared with the corresponding period of last year despite of the decrease in sales volume in the first half of the year.