



Management Discussion and Analysis



OPERATING ENVIRONMENT

During the year ended 31 December 2004 (the "Year"), the automobile industry in the People's Republic of China (the "PRC") did not sustain the explosive rapid growth as it did in the past two years. Instead, it had entered a stage of stable development following market adjustments. Affected by the negative impacts resulted from the State's implementation of macroeconomic control measures, the tightening of car loans, restraints on urban roads due to traffic environment, the upsurge of oil price and the wait-and-see consumer attitude caused by frequent price cuts of automobiles, there was a certain downward adjustment to the growth rate of the production and sales volume of automobiles as compared with those of the previous year. However, when taking into account the overall operation during the Year, the PRC automobile industry had sustained stable and rapid growth in sales and production volume in 2004.

According to the statistics of China Association of Automobile Manufacturers, the total production volume of automobiles in the PRC during the Year was 5,070,500 units, representing an increase of 14.11% as compared to that of 2003. Total sales volume of automobiles amounted to 5,071,100 units, representing an increase of 15.5% as compared to that of 2003. During the Year, there was an escalating demand for automobiles in the PRC automobile industry. However, the growth rate of automobiles during the Year was apparently more stable as compared with those of the past few years.

The automobile industry in the PRC is undergoing a new round of structural adjustments, which will lead the industry to a development stage marked by economies of scale, quality and low cost. The State's macroeconomic austerity measures and policies restricting vehicle gas consumption will eliminate small-scale manufacturers with low efficiency and low technical level, thereby accelerating market consolidation.

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FINANCIAL REVIEW

Turnover

During the Year, the Group's turnover amounted to RMB3,184,614,000, representing a decrease of 13.7% as compared to that of 2003. The decrease in turnover was mainly due to: (1) negative impacts resulted from the State's implementation of macroeconomic austerity measures, tightening of car loans, restraints on urban roads due to traffic environment, upsurge of oil price had affected both the overall automobiles sales in the market and that of the Group for the Year. The Group's sales volume fell from that of 2003; (2) the overall selling prices of automobiles continued to decrease during the Year as a result of fierce market competition. The Group's selling prices were adjusted downwards accordingly.

Automobile sales

During the Year, the Group sold 47,416 units of automobiles, representing a decrease of 9.8% as compared to 52,549 units sold in 2003. Automobiles sold in 2004 included 25,147 units (2003: 25,169 units) of pick-up trucks, representing a decrease of 0.1% as compared to that of 2003, 21,890 units (2003: 27,091 units) of sports utility vehicles ("SUV"), representing a decrease of 19.2% as compared to that of 2003, and 379 units (2003: 289 units) of large-sized buses and special vehicles, representing an increase of 31.1% as compared to that of 2003.

Analysis on automobile sales and production capacity

	2004			2003		
	Sales volume (units)	Turnover RMB'000	Percentage share of automobile sales (%)	Sales volume (units)	Turnover RMB'000	Percentage share of automobile sales (%)
Pick-up trucks	25,147	1,376,303	47.1	25,169	1,451,104	43.3
SUVs	21,890	1,481,391	50.7	27,091	1,849,729	55.1
Large-sized buses and special vehicles	379	65,498	2.2	289	54,410	1.6
Total	47,416	2,923,192	100.0	52,549	3,355,243	100.0
Production capacity (units)	70,000			70,000		

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Sales of automotive parts and components

In addition to the production of automobiles, the Group also engages in the sales of principal automotive parts and components used in the production of pick-up trucks and SUVs. These mainly include self-manufactured engines, front and rear axles, air-conditioning equipment and drag ball pins, lever assembly and other parts and components for production of automobiles. Sales of automotive parts and components not only enhanced the Group's revenue but also secured parts and components for after-sales services. During the Year, the Group reported a 22.3% decrease in sales of automotive parts and components, decreasing from RMB336,463,000 in 2003 to RMB261,422,000 in 2004. The drop was mainly attributable to the impact of the overall automobile sales market and decrease in sales of engines during the Year. The sales of engines represented 54.1% of the Group's sales of automotive parts and components during the Year.

Gross profit and gross profit margin

During the Year, the Group's gross profit decreased to RMB887,946,000 (2003: RMB1,196,188,000), representing a decrease of approximately 25.8% as compared to that of 2003. The decrease in the Group's gross profit was mainly due to the decrease in both the Group's sales volume of automobiles and the gross profit margin of automobiles attained by the Group. The Group's gross profit margin decreased from 32.4% in 2003 to 27.9% in 2004. The decrease in gross profit margin was mainly due to (1) the selling prices of many branded automobiles were reduced in response to the fierce competition of automobile market. As a result, the Group adjusted the price downwards accordingly; and (2) upgrade of functions and modification of appearances for the Group's existing automobiles, and the rise in cost of steels had led the additional cost of raw materials.

Profit attributable to shareholders and earnings per share

The Group's profit attributable to shareholders for the Year decreased to RMB402,917,000 from RMB523,398,000 for 2003. The decrease in the Group's profit attributable to shareholders was due to the decrease in gross profit of automobiles and the surge in research and development expenses.

For the year ended 31 December 2004, the basic earnings per share of the Company were RMB0.43. The Company did not present diluted earnings per share as it did not have any potential ordinary share for dilution during the Year.

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Selling and distribution costs and administrative expenses

During the Year, the selling and distribution costs and administrative expenses of the Group amounted to RMB298,063,000 (2003: RMB304,918,000), representing a decrease of 2.2% as compared to that of 2003. The decrease was mainly due to: (1) reduction in transportation expenses resulted from decrease in sales volume; and (2) reduction in provision for product warranties resulted from the stable production and improvement in quality of the Group's automobiles. The percentage of selling and distribution costs and administrative expenses to the Group's turnover increased from 8.3% in 2003 to 9.4% in 2004.

Finance costs

During the Year, the Group reported finance costs of approximately RMB619,000 as compared to approximately RMB5,093,000 in 2003. The decrease in interest expenses is mainly due to the repayment of most of the bank loans in the first half of 2003.

Liquidity and financial resources

As at 31 December 2004, the Group's current assets mainly included cash and cash equivalents of approximately RMB2,082,413,000, pledged deposits of approximately RMB168,464,000, trade receivables of approximately RMB49,826,000, inventories of approximately RMB405,772,000, bills receivable of approximately RMB562,314,000, short term investments of approximately RMB509,000, and other receivables of approximately RMB79,096,000. The Group's current liabilities as at the same date mainly included trade payables of approximately RMB617,033,000, bills payable of approximately RMB290,397,000, tax payable of approximately RMB102,033,000, other payables of approximately RMB276,701,000, provision for product warranties of approximately RMB25,335,000 and dividend payables of approximately RMB7,301,000.

Acquisitions

During the Year, the Company and its subsidiaries did not have any material acquisitions.

Capital structure

The Group generally finances its operation with internally generated cash flows. As at 31 December 2004, the Group was at a debt-free position.

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Exposure to foreign exchange risk

All the Group's domestic sales were settled in RMB while sales to overseas customers were settled in US dollars or Euro. During the Year, the Group did not experience any material difficulties or negative effects on its operations or liquidity as a result of fluctuations in currency exchange rates. The board of directors (the "Board") believes that the Group will have sufficient foreign exchange reserves to meet its foreign exchange requirements.

Employment, training and development

As at 31 December 2004, the Group employed a total of about 6,993 employees, approximately 993 more as compared to 2003. Employees were remunerated on the basis of their performance, experience and prevailing industry practices. The Group's remuneration policies and packages were reviewed on a regular basis. Bonuses and cash awards may also be given to employees based on individual performance evaluation. Total staff cost accounted for 3.8% of the Group's turnover for the Year.

Taxation

Tax of the Group decreased from RMB187,608,000 in 2003 to RMB69,160,000 in 2004, representing a drop of 63.1%. This decrease was primarily due to reduction in profit before tax.

Segment information

During the Year, over 90% of the Group's revenue and results were derived from the manufacture and sale of automobiles in the PRC and from PRC customers. Therefore, no business and geographical segmental analysis are presented.

Contingent liabilities

As at 31 December 2004, except for the fact that the Group's bills receivables amounting to RMB134,650,000 were pledged to banks for issuing an equivalent amount of bills payables, the Group did not have any significant contingent liabilities.

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BUSINESS REVIEW

Products

The Group's principal products are pick-up trucks and SUVs. In addition, the Group also produces large-sized buses and special vehicles. In 2004, a large proportion of the automotive parts and components produced by the Group were used for the assembly of the Group's pick-up trucks and SUVs, while the remaining portion (mainly comprising engines and drag ball pins) was sold to independent third parties. In 2004, the Group sold 47,416 units of automobiles, with a sales revenue of RMB3,184,614,000. The directors of the Company (the "Directors") believe this was a result of the Group's accurate market positioning and implementation of flexible production approaches. Capitalising on these competitive edges, the Group adopted flexible pricing strategy and exercised effective cost control. As a result, the Group produced products with high quality-price ratio. In fact, the Group achieved effective cost control through enhancing productivity, thereby mitigating much of the impact from price reduction.

(1) *Pick-up trucks*

According to 全國皮卡車市場數據信息聯合會 (National Pick-up Truck Market Information Association), the sales volume of pick-up trucks of the Group continued to rank first in the PRC market during the Year. The sales volume of pick-up trucks reached 25,147 units with sales revenue amounting to RMB1,376,303,000, representing a decrease of 0.1% and 5.2%, respectively when compared with those of 2003. 14,173 units of the *Deer* pick-up trucks were sold with revenue amounting to RMB698,107,000, representing an increase of 10.8% and 2.9%, respectively when compared with those of 2003. 9,965 units of the *Sailor* pick-up trucks were sold with revenue amounting to RMB620,369,000, representing a decrease of 19.5% and 19.7%, respectively when compared with those of 2003. During the Year, a total of 1,009 units of the newly launched *So Cool* pick-up truck series were sold, with a revenue of RMB57,828,000.

(2) *SUVs*

The sales volume of SUVs of the Group during the Year was 21,890 units, with sales revenue amounting to RMB1,481,391,000, representing a decrease of 19.2% and 19.9%, respectively when compared with those of 2003. During the Year, 9,581 units of the *Safe* SUVs were sold with revenue amounting to RMB641,166,000, representing a decrease of 55.4% and 56.8%, respectively when compared with those of 2003. 11,969 units of the *Sing* SUVs were sold with revenue amounting to RMB817,957,000, representing an increase of 113.2% and 123.2%, respectively when compared with those of 2003. During the Year, a total of 340 units of the newly launched *Pegasus* SUV series were sold, with a revenue of RMB22,268,000.

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(3) Large-sized buses and special vehicles

For large-sized buses and special vehicles of the Group, the sales volume and sales revenue during the Year amounted to 379 units and RMB65,498,000 respectively, representing increases of 31.1% and 20.4% respectively when compared with those of 2003. Sales revenue from large-sized buses and special vehicles accounted for approximately 2.1% of the Group's total turnover in 2004.

(4) Automotive parts and components

During the Year, the sales revenue of automotive parts and components amounted to RMB261,422,000, representing a decrease of 22.3% when compared with that of 2003.

During the Year, the Group cooperated with quality domestic and overseas automotive components enterprises to jointly establish several automotive parts and components enterprises. Products to be manufactured will include air-conditioners, cushions, decorations and seats for automobiles. At present, the Group is actively holding discussion with renowned domestic automotive parts and components manufacturers, with the aim of optimising the supply chain of the Group's automotive parts and components.

During the Year, the Group has established the following new joint ventures:

Name of company	Main products	Shareholding	Joint venture parties	Registered capital (RMB)
Macs (Baoding) Auto A/C System Co., Limited	Air conditioning equipment and other parts and components for automobiles	51%	Automart Holding Limited	16,500,000
Baoding Huanqiu Auto Spare Parts Co., Limited	Upholstery components for automobiles (cushions, roofs, carpets, etc)	51%	Wenzhou Huanqiu Automobile Gasket Co., Ltd.	10,000,000
Baoding Deye Automobile Inner Decoration Co., Limited	Upholstery components for automobiles (combined dashboard, etc)	49%	Deye (H.K.) Technological Electric Appliance Company Limited, Ningbo Deye Chemical Material Co., Ltd.	30,000,000
Baoding Jiehua Automobile Components and Accessories Company Limited	Automotive parts and components, design, development and production of seats	50%	Shanghai Jiehua Automobile Decoration Development Center	18,000,000

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Domestic market

In light of industry consolidation and unfavourable market factors, the Group adjusted its selling prices through reducing energy consumption and production wastage. The Group also strengthened its collaboration with agents and enhanced marketing efforts, which effectively raised its competitiveness and increased sales volume and revenue.

Clientele

The domestic sales volume of pick-up trucks and SUVs of the Group during the Year amounted to 22,065 units and 21,384 units, respectively, and the sales revenue amounted to RMB1,229,704,000 and RMB1,442,342,000, respectively. The sales revenue from the two main groups of customers, namely (1) dealers, and (2) government entities and individual customers amounted to RMB2,586,128,000 and RMB149,238,000, respectively.

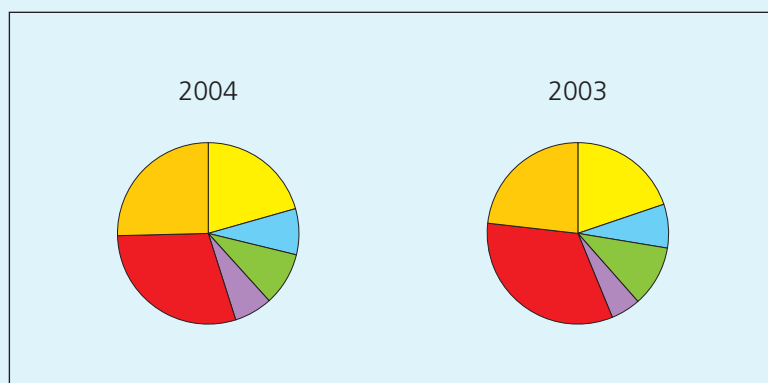
	2004			2003		
	Sales volume (units)	RMB'000	Percentage share of domestic automobile sales (%)	Sales volume (units)	RMB'000	Percentage share of domestic automobile sales (%)
Dealers	41,474	2,586,128	94.5	49,439	3,167,727	96.4
Government entities and individual customers	2,348	149,238	5.5	1,935	117,196	3.6
Total	43,822	2,735,366	100.0	51,374	3,284,923	100.0

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The Group's domestic sales by geographical distribution

The following table and charts set out the geographical breakdown of the Group's domestic sales in 2003 and 2004:

	2004		2003	
	Sales revenue <i>RMB'000</i>	Percentage share of domestic automobile sales (%)	Sales revenue <i>RMB'000</i>	Percentage share of domestic automobile sales (%)
Northern Region	563,872	20.6	647,894	19.8
Northeastern Region	225,335	8.2	255,555	7.8
Northwestern Region	261,008	9.5	359,613	10.9
Southwestern Region	184,171	6.8	172,849	5.3
Eastern Region	807,428	29.5	1,085,362	33.0
Central Region	693,552	25.4	763,650	23.2
Total	2,735,366	100.0	3,284,923	100.0



- Eastern region: Shanghai, Jiangsu, Zhejiang, Anhui, Fujian, Jiangxi, Shandong
- Central region: Henan, Hubei, Hunan, Guangdong, the Guangxi Zhuangzu Autonomous Region, Hainan
- Northern region: Beijing, Tianjin, Hebei, Shanxi, the Inner Mongolia Autonomous Region
- Northwestern region: Shanxi, Gansu, Qinghai, the Ningxia Hui Autonomous Region, the Xinjiang Uygur Autonomous Region
- Northeastern region: Liaoning, Jilin, Heilongjiang
- Southwestern region: Chongqing, Sichuan, Guizhou, Yunnan, the Tibet Autonomous Region

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Export market

During the Year, the export sales of the Group's automobiles reached its record high, with 3,082 units and 506 units of pick-up trucks and SUVs sold to overseas markets respectively. Export sales amounted to RMB187,827,000, representing an increase of 167.1% from that of last year and accounting for 5.9% of the Group's total turnover. The Group's main foreign markets are mainly the African and Middle Eastern countries including Saudi Arabia, United Arab Emirates, Bahrain, and Kuwait. The sales volume of pick-up trucks and SUVs accounted for 78.1% and 20.8%, respectively of the Group's export sales.

Under the trend of globalisation, the overseas market demand for pick-up trucks and SUVs has been increasing gradually. The Group is actively working on plans for developing various new markets, such as Vietnam, the Philippines and Zimbabwe.

Technical capability

In order to consolidate its local and overseas markets and to keep abreast of the development of the automobile industry, the Group has established Great Wall Automobile Technical Research and Development Center of national standard. The research centre comprises state-of-the-art design, inspection and testing facilities including a computer centre, styling centre, prototyping workshop, emissions laboratory, environment simulation laboratory, chassis performance laboratory, parts performance laboratory, proving ground, tooling centre, etc. The research centre was manned by more than 500 engineers, over 150 of which were doctoral and master degree holders and senior technicians.

Launch of new products

The Group adapted swiftly to market changes through flexible allocation of resources to meet market demand. During the Year, the Group offered 139 models of pick-up trucks under three major series and 152 models of SUVs under three major series. Great Wall Automobile also launched "2004 edition" of *Safe*, and new models of *So Cool* pick-up truck and *Pegasus* SUV, which were well received by the market.

Quality control

In 2004, all of the Company's new products passed the CCC certification of 國家質量監督檢驗檢疫總局 (State General Administration of Quality Supervision, Inspection and Quarantine) and applied for inclusion in the 國家環保目錄 (List of environmental friendly companies recognised by the Environmental Protection Administration of China). About 36 vehicle models passed the certification for new car inspection exemption from 國家發展和改革委員會 (National Development and Reform Commission) and 公安部 (Ministry of Public Security).

Management Discussion and Analysis

Sales and after-sales service network

In order to provide better service, the Group has, as at 31 December 2004, increased its sales network to 455 units and after-sales service centres to 351, spanning 22 provinces and five autonomous regions in the PRC.

Production and production capacity

As at 31 December 2004, the Group's total annual production capacity of SUVs and pick-up trucks reached approximately 70,000 units. With the commencement of production of the Phase I project at Great Wall Motor Industry Zone in March 2005, the Group's total annual production capacity increases to 170,000 units.

OUTLOOK

Overview

Both opportunities and challenges exist in 2005 for the development of the automobile industry. On the one hand, steady economic growth, the State's continued implementation of stable and healthy fiscal and monetary policies and constant improvement in living standard will facilitate healthy development of the automobile industry. On the other hand, the macroeconomic control measures taken by the government in 2004 will have lingering effect on the automobile industry in 2005. Moreover, the removal of import quota on vehicles and the lowering of tariffs on automobiles and automotive parts to 30% and 13%, respectively, will further intensify the competition between imported and domestic-produced automobiles. As such, consumers become more rational, and the growth in local automobile sales will remain at a steady pace.

Pursuant to industry consolidation in 2004, the Group will upgrade its existing products while maintaining the leadership in the pick-up truck and SUV markets in the current year. The Group will also strengthen its research capability, with an aim to develop high quality models with low engine emission, low energy consumption and low gas consumption.

New products

In 2005, the launch of *Hover* CUV, which receives great accolade from the media in the PRC, will provide the Group greater room for development. *Hover* CUV marks a major step forward in the Group's expansion into the high-end SUV market. *Hover* CUV integrates the comfort of a sedan and toughness of an SUV, and is competitive even when it is compared with similar models of international brands.

In addition, the Group's newly developed pick-up truck and commercial vehicle will be produced on the same production line as the *Hover* CUV to effectively reduce cost. By that time, three new types will be added to the current product portfolio.

Management Discussion and Analysis

New facilities

The Group plans to complete the construction of a production facility with a capacity of 200,000 units of multi-purpose vehicles ("MPVs") series of passenger vehicles in 2006 (the "Passenger Vehicle Project").

The objective of implementing the 200,000 units per annum Passenger Vehicle Project is to develop and produce new passenger vehicles with proprietary intellectual property rights. This strategic move can enhance the Group's research and development capability and market competitiveness, as well as promote the development of local automobile industry. The product under this project is a type of energy-saving vehicle for family use with low engine emission, which complies with the requirements of the government's policy on the industry and is in line with the State's sustainable development strategies. The new product, enriching the Group's product variety, will enable the Group to meet market demand for passenger vehicles featuring low engine emission and consumers' requirements for product variety and personality. Moreover, when this new facility reaches its designed capacity, the Group's total annual production capacity will increase to 370,000 units, which will enable the Group to lower production cost, increase economic efficiency and to be one of the first to ride out the severe market competition.

To support the development of the Passenger Vehicle Project, the Group submitted to China Securities Regulatory Commission an "Application for Great Wall Automobile Holding Company Limited's Initial Public Offering of A Shares" at the end of 2004. The proceeds will be used for the construction of the passenger vehicle production facility and upgrading of the technical centre, which will enable the Group to broaden its product variety and maximise economies of scale.

At present, China Securities Regulatory Commission is processing the Group's application for listing, and has issued 《中國證監會行政許可項目審查反饋意見通知書》 ("Notice Regarding China Securities Regulatory Commission's Examination Opinion on Matters Subject to Administrative Approval"). Other preparations for the Group's A share offer are in progress and the Group's A share offer plan is well under way according to the schedule set for related procedures.

Production scale

The Board believes that operational efficiency and domestic market share can be further enhanced through expansion of the existing production scale.

The Group started the commercial production of *Hover* CUV at the new facility at the newly constructed Phase I of the Group's industry zone in March 2005, and will gradually launch new models of pick-up trucks and commercial vehicles. When the facility reaches its designed capacity, the Company's annual production capacity will reach 170,000 units.

As at 31 December 2004, the Group had a production capacity of 200,000 units of engines.

Management Discussion and Analysis

Enlarged client base

The Group will continue to develop the large volume purchase sector, which mainly consists of government authorities.

Under the trend for globalisation, demand from developing countries for automobiles continues to rise. In order to further increase its export sales volume, the Group will continue to enhance its marketing and promotion activities in overseas markets, which are expected to be one of the Group's important sources of clientele.

Future vision

The Group will capture the golden opportunity of industry consolidation by assessing the feasibility of acquiring relevant businesses, thereby enhancing its competitiveness. The Group will also actively seek collaborations on various aspects in China and overseas to prepare itself for the continuous development of the industry in the future.

The Group will strive to stay ahead of its competitors in the fast growing PRC's automobile market in order to be the first to seize opportunities. All these are aimed at generating greater value and return to the Group's shareholders.