Management Discussion and Analysis

OVERVIEW

The Group's turnover and profit attributable to shareholders for the year amounted to approximately RMB218 million and RMB13 million respectively, representing a decrease of approximately 4% and an increase of approximately 12% respectively when compared with last year. The gross margin remained at 30%. As at 31 December 2004, the Group had commitments of capital expenditure in respect of the acquisition of land use right and buildings for production purposes amounted to approximately RMB15 million (2003: approximately RMB20 million) and investment in a sino-foreign equity joint venture at approximately RMB6 million (2003: Nil). The amounts are expected to be financed by internal funding.

For the year ended 31 December 2004, the basic earnings per share of the Group were approximately RMB0.032 (2003: approximately RMB 0.029).

OPERATING ENVIRONMENT

2004 is a challenging year for the automobile manufacturing sector in China. The price of steel and raw materials for manufacturing vehicles, recorded a substantial increase. Meanwhile, the selling prices of vehicles saw a continuous decrease, putting pressure on the gross profit of the automobile manufacturing sector. On the other hand, domestic banks tightened their financing on automobiles and the price of crude oil rose, these reduced the appetite of consumers for automobiles. A majority of consumers maintained a "wait-and-see" attitude, thus slowing down the growth of domestic sales of automobile.

According to the statistics of China Association of Automobile Manufactures, the production and sales volumes of vehicles in China for the year 2004 were both 5 million units, representing an increase of 14% and 16% respectively when compared with 2003. This has demonstrated that the demand for vehicles in China is still strong, however, the growth rate has become steady.

In the previous year, there was a strategic adjustment in the automobile maintenance market. In the past, players of the sector focused on setting up 4-in-1 (vehicles sales, after-sales services and provision of spare parts and information) service centres. This practice has been gradually changed to the establishment of well planned and convenient "express service centres". These "express service centres" are relatively smaller in scale, and can satisfy vehicle users' demand for instant inspection and repair. Throughout the automobile maintenance sector, the existing equipment-intensive integrated services are now being replaced by low-investment but high-quality convenient services.

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AUTOMOBILE MAINTENANCE EQUIPMENT BUSINESS

In 2004, the Group focused on developing high value-added products with high technology for its automobile maintenance equipment business. The Group's three investment projects in Yancheng Economic Development District, Jiangsu Province, will commence trial production soon. Production capacity of lifters will increase to 8,000 units from 2,000 units. Sales volume also increases in 2004.

During the year, the sales of the Group's automobile inspection equipment were approximately RMB20 million, an increase of 60% compared with that of the previous year. Sales of automobile inspection equipment represented 9% of the total sales of the Group. Sales from lacquer rooms showed a slight increase but sales from large-scale surface treatment lines recorded a decrease. Large-scale surface treatment lines had a higher unit selling price, hence reducing its sales volume. This had certain impact on the Group's overall sales.

Technical problems associated with the Group's car washing machine venture with an Italian listed company, were solved during the year 2004. Plant construction and equipment installation were completed, and trial production was started at the beginning of 2005. Annual production capacity for the phase one plant construction is 500 units of car washing machine.

During the year, export sales of the Group were RMB32 million, representing approximately 15% of the total turnover. The Group mainly exported lifters and lacquer rooms in 2004.

The Group changed its distribution mode for its export products during the year, from distributing by itself to engaging distributors. The Group has 3 distributors in the eastern, middle and western parts of the United States. In 2004, approximately 90% of the products exporting to the United States were distributed by local distributors.

On the other hand, the Group further expanded its overseas markets. Products were sold to new markets like the Middle East and Russia.

To cope with market demand, the Group continued to inject resources for strengthening the research and development of products. The Group launched several new products like integrated inspection equipment and safety inspection equipment during the year. These products have gained a good response from the market.

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AUTOMOBILE MANUFACTURING BUSINESS

During the year, the Group established Nanjing Zhongda Jinling Double-Decker Bus Manufacture Company Limited ("Zhongda Jinling") with Jiangsu Jinling Transportation Group Limited and Sichuan Zhongda Emei Coach Manufacturing Limited ("Zhongda Emei") with Sichuan Bus Manufacture Limited respectively. The Group indirectly held 60% and 71% interests in Zhongda Jinling and Zhongda Emei respectively. These joint-ventures are still in an start-up stage and had slight turnover contribution to the Group during the year.

Zhongda Jinling is the only enterprise designated by the state for developing city double-deck buses. Zhongda Jinling possesses advanced technologies on products of the same kind in China. Jinling brand double-deckers have a share of approximately 80% in the turnover of the urban transportation market in China. Major cities like Beijing and Shanghai have purchased Jinling brand double-deckers.

During the year, the Group upgraded the technologies of Zhongda Jinling, resulting in an increase in production capacity from 500 units to 2,000 units.

Zhongda Emei focuses on manufacturing long-haul buses for mountainous areas and its sales are mainly to western provinces like Yunnan, Guizhou and Sichuan. The annual production capacity of Zhongda Emei is 1,500 buses and the production target for 2005 is 600 buses.

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LIQUIDITY AND FINANCIAL RESOURCES

As at 31 December 2004, the Group's total assets amounted to approximately RMB459 million (2003: approximately RMB317 million), representing an increase of RMB142 million. As at 31 December 2004, the Group had bank balances and cash of approximately RMB32 million (2003: approximately RMB46 million) and bank loans were approximately RMB113 million (2003: approximately RMB66 million). The Group's bank borrowings were mainly secured by charges on certain land use rights and buildings of the Group with a net book value of approximately RMB100 million (2003: approximately RMB31 million).

Liabilities increased from approximately RMB147 million in the previous year to approximately RMB267 million in this year, which was mainly attributable to the two new joint ventures (Zhongda Jinling and Zhongda Emei) and the transfer of approximately RMB100 million debt owed by the local shareholders while injecting their assets. Bank loans of the Group increased during the year as a result of acquisition, plant construction and land acquisition. The Group is planning a debt restructuring for the new joint ventures and is negotiating with suppliers and banks for waiving part of the debts and deferring repayments. Initial results are encouraging.

There were no material changes in bad debt and inventory provisions. Bad debt provision had a net increase of approximately RMB800,000 (2003: an increase of approximately RMB1.6 million) and no changes were recorded for inventory provision (2003: an increase of approximately RMB800,000). Inventories at the end of 2004 increased by approximately RMB19 million when compared with that of 2003. The increase was mainly attributable to the inventories of the 2 newly established joint-ventures added to the consolidated account. These inventories were audited, and stated at their fair values at the time when they were injected into the joint-ventures. Accordingly, no changes were recorded to the inventory provision. Revenue of the Group is mainly denominated in RMB and USD and borrowings are mainly settled in RMB. As the exchange rate of RMB to USD is stable, the Directors consider that the Group has no significant exposure to exchange rate fluctuation. Interest on bank borrowings was charged at 3.98% to 6.59% (2003: 3.98% to 7.13% per annum). As at 31 December 2004, the debt to equity ratio of the Group was 67.4% (2003: 42.7%). The debt to equity ratio is computed on the basis of total bank borrowings divided by the shareholders' fund of the Group.

DIVIDEND

The Board of Directors do not recommend the payment of a dividend for the year ended 31 December 2004 (2003: Nil).

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PROSPECT

The domestic automobile market is expected to grow steadily in 2005. It is anticipated that imported vehicles will boost the demand for automobile maintenance equipment. Beijing and Shanghai will hold the Olympic Games and World Expo respectively, and these high-profile international activities will provide an effective impetus to the demand for vehicles. To cope with the heavy traffic during these activities, the Group expects that Beijing and Shanghai will need to build 1,000 and 500 "express service centres" respectively for the provision of inspection and maintenance services for different kinds of vehicle.

In order to enhance environmental protection and to comply with international standards, China required the existing 760,000 coaches which have already attained the Euro I Emission Standard to meet the higher Euro II Emission Standard within five years. In the coming five years, it is expected that approximately 150,000 coaches will be replaced each year due to the above requirement. In the year 2004, total sales of coaches in China was 98,000 units.

On the other hand, the Chinese government is currently holding the campaign "Cun Cun Tong" ("Connecting the Villages") to improve the standard of living in rural areas. The project is aimed at extending the coverage of television broadcast, asphalt highways and public bus service to the rural areas. It is estimated that the project would create a demand for up to 100,000 buses per annum.

With the tightened up of vehicle emission restriction, extension of highway coverage and increase in long distance traffic flow, China has a huge market potential for double-deckers and long-haul coaches .

The Group is committed to strengthening the business models and management operations of its joint-ventures. A market-oriented approach for development is adopted to increase the sales of Jiangsu Jinling and Sichuan Emei and enhance their operating efficiency.

The Group will also work to strengthen its capabilities of market expansion and technologies development, with its focus on multi-fuel (LPG, gasoline, electricity) vehicles and development of low platform public buses and other buses exclusive for the "Cun Cun Tong" project.

In addition, the Group will expand the after-sales product range for vehicles through, for example, boosting sales to shorten the transformation to mass production of car washing machines, increasing the target sales volume for inspection machines, developing new types of lacquer room and maximizing sales from surface treatment.

In response to the market trend, the Group will supply professional equipment for the emerging "express service centres". At the same time, the Group will assess the feasibility of establishing its own express service centres .

Looking forward, the Group expects to achieve better sales, profitability and management results.