Management's Discussion and Analysis

BUSINESS REVIEW

The consolidated net sales of the Company and its major operating subsidiaries, Shenyang Brilliance JinBei Automobile Co., Ltd. ("Shenyang Automotive"), Shenyang XingYuanDong Automobile Component Co., Ltd. ("Xing Yuan Dong"), Ningbo Yuming Machinery Industrial Co., Ltd. ("Ningbo Yuming"), Ningbo Brilliance Ruixing Auto Components Co., Ltd. ("Ningbo Ruixing"), Mianyang Brilliance Ruian Automotive Components Co., Ltd. ("Mianyang Ruian"), Shenyang Brilliance Dongxing Automotive Component Co., Ltd. ("Dongxing Automotive"), Shenyang ChenFa Automobile Component Co., Ltd. ("ChenFa") and Shenyang Jindong Development Co., Ltd. (together, the "Group") for the year ended 31st December, 2005 were RMB5,469.0 million, representing a 16.4% decrease from RMB6,542.0 million for the year ended 31st December, 2004. The decrease in sales was primarily due to a decrease in average unit selling prices and volume of Shenyang Automotive's minibuses and Zhonghua sedans in 2005.

Shenyang Automotive sold approximately 60,000 minibuses in 2005, representing a 2.6% decrease from approximately 61,630 minibuses sold in 2004. Of these vehicles sold, approximately 50,060 were mid-priced minibuses, representing a 9.0% decrease from approximately 55,000 units sold in 2004. Unit sales of deluxe minibuses, however, increased by 50.0% from approximately 6,630 units in 2004 to approximately 9,940 units in 2005. Shenyang Automotive sold approximately 9,000 Zhonghua sedans in 2005, representing a 18.0% decrease from approximately 10,980 sedans sold in 2004.

Cost of sales decreased by 9.5% from RMB5,487.0 million in 2004 to RMB4,964.8 million in 2005. The decrease was primarily due to the decrease in unit sales of minibuses and Zhonghua sedans. Furthermore, the unit production costs of minibuses have decreased as a result of the reduction of materials and component costs in 2005. The overall gross profit margin of the Group decreased from 16.1% in 2004 to 9.2% in 2005. The decrease in gross profit margin resulted mainly from the decrease in gross margin of both Zhonghua sedans and mid-priced minibuses due to the lower sales volume and decrease in average unit selling prices.

Other revenue increased by 22.2% from RMB111.2 million in 2004 to RMB135.9 million in 2005. The increase was primarily due to a service income received from a jointly controlled entity in 2005.

Selling expenses decreased by 12.8% from RMB500.3 million, representing 7.6% of turnover in 2004, to RMB436.5 million, representing 8.0% of turnover in 2005. The decrease was primarily due to the reduction in advertising, promotion and marketing expenses resulting from the decrease in sales volume of the Zhonghua sedans and minibuses in 2005 as compared to 2004.

General and administrative expenses decreased by 15.9% from RMB732.6 million in 2004 to RMB616.3 million in 2005. The decrease was mainly due to the reduction in research and development cost.

Other operating expenses increased by 26.2% from RMB70.6 million in 2004 to RMB89.1 million in 2005. The increase was mainly due to the impairment loss of certain fixed assets in two of the subsidiaries.

In 2005, the Group recognised an impairment loss on intangible assets in relation to the Zhonghua sedans in the amount of RMB300.0 million and an impairment loss on goodwill in a subsidiary in the amount of RMB50.0 million.

Interest expense net of interest income increased by 41.2% from RMB123.7 million in 2004 to RMB174.7 million in 2005. The increase was mainly due to the increase in effective finance expenses from the convertible bonds resulting from the adoption of the new Hong Kong Accounting Standard 39 in 2005.

The Group's share of operating results of jointly controlled entities and associates (excluding an impairment loss on goodwill in a jointly controlled entity) decreased by 52.4% to RMB49.0 million in 2005 from RMB103.0 million (as restated) in 2004. The decrease was mainly due to the decrease in profit contributed by jointly controlled entities and associates and the losses of one of the jointly controlled engine companies in 2005. In addition, the Group also recognised an impairment loss on goodwill in a jointly controlled entity in the amount of RMB179.0 million in 2005. Net profits contributed to the Group by BMW Brilliance Automotive Ltd., the Group's 49% indirectly owned jointly controlled entity, increased 45.0% from RMB21.8 million in 2004 to RMB31.6 million in 2005. The BMW joint venture achieved sales of 17,501 BMW sedans in 2005, an increase of 101.0% as compared to 8,708 BMW sedans in 2004.

The Group recorded a loss before taxation amounting to RMB1,156.4 million in 2005 as compared to a loss before taxation amounting to RMB458.1 million (as restated) in 2004. The Group recorded tax expenses of RMB89.1 million in 2005 as compared to net tax credit of RMB50.3 million (as restated) in 2004, resulting mainly from the de-recognition of deferred tax assets in 2005.

As a result, the Group recorded a loss attributable to equity holders of the Company of RMB649.6 million in 2005 as compared to a profit attributable to equity holders of the Company of RMB48.6 million in 2004. Basic loss per share in 2005 amounted to RMB0.1771 against the basic earnings per share of RMB0.0132 in 2004. Diluted loss per share in 2005 amounted to RMB0.1771 against the diluted earnings per share of RMB0.0132 in 2004.

LIQUIDITY AND FINANCIAL RESOURCES

As of 31st December, 2005, the Group had RMB843.4 million in cash and cash equivalents, RMB1,053.8 million in short-term bank deposits and RMB1,932.6 million in pledged short-term bank deposits. The Group had bank notes payable of RMB3,101.0 million and outstanding short-term bank borrowings of RMB496.5 million, but had no long-term bank borrowings outstanding as of 31st December, 2005. On 28th November, 2003, the Company, through its wholly owned subsidiary, Brilliance China Automotive Finance Ltd. ("Brilliance Finance"), issued Zero Coupon Guaranteed Convertible Bonds due 2008 (the "Convertible Bonds") with principal amount of US$200 million (equivalent to approximately RMB1,654.3 million at the time of issue). Up to 31st December, 2005, none of the Convertible Bonds had been converted into ordinary shares of the Company.

CONTINGENT LIABILITIES

Details of the contingent liabilities are set out in note 42 to the financial statements.

DEBT TO EQUITY RATIO

As of 31st December, 2005, the debt to equity ratio, computed by dividing total liabilities by total equity attributable to equity holders of the Company, was approximately 1.29 (31st December, 2004: 1.39). The decrease of the ratio is primarily due to the decrease in the outstanding principal amount of the notes payable.

USE OF PROCEEDS

On 28th November, 2003, Brilliance Finance issued the Convertible Bonds. The net proceeds of the sale of the Convertible Bonds was approximately US$194 million. As at 31st December, 2005, the Group had utilised all the said proceeds for general corporate and working capital purposes.

FOREIGN EXCHANGE RISKS

The Group does not consider exchange rate fluctuations to have any material effect on the overall financial performance of the Group, but may consider entering into hedging transactions through exchange contracts in order to minimise foreign exchange risks, if and when necessary. There were no outstanding hedging transactions as of 31st December, 2005.

EMPLOYEES AND REMUNERATION POLICY

The Group employed approximately 8,900 employees as at 31st December, 2005. Employee costs (excluding directors' emoluments) amounted to approximately RMB321.5 million for the year ended 31st December, 2005. The Group will endeavour to ensure that the pay levels of its employees are in line with industry practices and prevailing market conditions and employees are rewarded on a performance-related basis, and eligible for share options under the share option scheme adopted by the Company. More details in respect of the Company's emolument policy and the basis of determining the emolument payable to the Company's directors are set out in note 14 to the financial statements.