



*Chairman — Mr. Zhang Fangyou*

To all Shareholders,

I hereby present the annual report of Denway Motors Limited (the “Company”), and the audited consolidated results of the Company and its subsidiaries (together the “Group”), non-consolidated subsidiaries, associates and jointly controlled entities for the year ended 31 December 2005.

### **BUSINESS REVIEW**

For the year ended 31 December, 2005, turnover from the continuing operations of the Group was approximately HK\$850,483,000 (2004: HK\$970,407,000, adjusted), a decrease of 12.4% over last year. Audited consolidated profit attributable to shareholders was HK\$1,905,529,000 (2004: HK\$2,062,447,000), a decrease of 7.6% over last year. Earnings per share from the continuing operations was HK26.2 cents (2004 : HK28.9 cents, adjusted), a decrease of 9.3% over last year.

Given the favourable macroeconomic environment in 2005, the automobile industry of China continued to sustain stable growth. Total automobile production and sales units for the year were approximately 5,707,700 and 5,758,200 respectively, representing year-on-year increases of

approximately 12.56% and 13.54% respectively, of which total production and sales units of passenger vehicles were approximately 3,930,700 and 3,971,100 respectively, representing year-on-year increases of approximately 19.73% and 21.40% respectively.

During 2005, the Group produced and sold an aggregate of 232,194 units and 231,437 units of motor vehicles respectively through a jointly controlled entity (the "Sedan Company") and its subsidiary (the "Bus Company"), representing an increase of approximately 14.1% and 13.8% respectively over those of the previous year. Among the total, the output and sales of the Sedan Company accounted for 231,550 units and 230,773 units respectively, representing an increase of approximately 14.5% and 14.2% respectively over that of the previous year. In order to expand its market share and maintain its competitiveness, the Sedan Company has implemented new pricing policy which led to decrease in corporate earnings. However, the Sedan Company's earnings level is still much higher than domestic and overseas peer groups' earnings level. The output and sales of the Bus Company accounted for 644 units and 664 units respectively, representing a decrease of approximately 48.5% and 49.2% respectively over that of the previous year. As the domestic bus industry at present is under an unhealthy situation, the management of the Company decided to dispose of the bus business and such disposal had been approved by the shareholders of the Company in the extraordinary general meeting held on 23 March, 2006.

The Group completed, in 2005, the acquisitions of the 5% equity interests in Guangzhou Denway Enterprises Development Company Limited and the 49% beneficial equity interests in Guangzhou Automobile Group Component Co., Ltd. and, in 2006, the disposal of the 50% equity interests in Guangzhou Denway Bus Co., Ltd pursuant to the approval of the said disposal obtained in the extraordinary general meeting held on 23 March, 2006. Such a series of transactions not only enable the Group to further enhance its asset structure by diversifying profit sources and underpinning earnings basis, but also fitting into its long-term development.

In 2005, the Group's other businesses, comprising vehicle trading, manufacture of vehicle-related equipment and components, and manufacture and trading of audio equipment, met our expectations.

### **FUTURE PROSPECTS**

The advent of China's Eleventh Five-Year Plan in 2006 will continue to foster a more stable, healthier and quicker development of the domestic economy. Establishment of the new rural village under socialism will be the guiding tune of the economic development of China, and facilitate the automobile marketplace a gigantic commercial opportunity. Battered by price wars and sweetened by robust growth, the PRC vehicle market is maturing gradually amidst market jitters. The car ownership per capita in China is far below that of the global average with ample room in the market. According to the forecast of the PRC Car Industry Association, the production and sales units for this year shall attain 6,400,000, representing a year-on-year increase of approximately 13%.

The Sedan Company plans to produce and sell 260,000 units of sedans in 2006, representing an increase of 13% over that of 2005. The Sedan Company will continue to adopt a market-oriented approach whereby more products, which may satisfy market demand and be welcomed by customers, will be introduced. Meanwhile, the Sedan Company will continue to expand and perfect the sales services system. Efforts will be dedicated to product technology, quality and services so as to continue to enhance customers' satisfaction and provide efficient services with high quality. The Sedan Company persists on a roll-over principle for its development. The construction of the second plant of the Sedan Company has been progressing smoothly and is now at the stage of equipment installation and testing. It is expected that the second plant will start production in the second half of this year.

Year 2006 will be a year of rapid development for the auto industry of Guangzhou. The Group will continue to pursue for better development opportunities in relation to the automobile business. The Board believes that the Group will maintain to seize such opportunities for further development, thereby generating attractive and better returns for its shareholders.

### FINANCIAL SUMMARY

The Group's turnover from the continuing operations of the Group for the year ended 31 December, 2005 was about HK\$850,483,000, representing a decrease of about 12.4% compared to that of 2004.

On 17 February, 2006, the Group announced a connected transaction to dispose the equity interest in a subsidiary ("the Disposed Subsidiary") solely conducting business in the manufacturing and assembly of motor vehicles. In accordance with HKFRS, the relevant items relating to the Disposed Subsidiary in the income statement in 2004 and 2005 and the balance sheet in 2005 were classified separately as a discontinued operation. The transaction was approved by independent shareholders and completed on 23 March, 2006.

The turnover of the trading of motor vehicles decreased by HK\$150,092,000 which represented a decrease of about 21.0% in 2005 compared that of 2004. However, the operating profit of this segment increased by HK\$13,353,000 or an increase of about 243.0% in 2005, mainly due to reduction of cost of goods sold. The turnover of the manufacturing and trading of automotive equipment and parts decreased by HK\$7,423,000 which represented a decrease of about 39.5% in 2005, mainly due to the disposal and liquidation of subsidiaries in the second half of 2004. The turnover of manufacturing and trading of audio equipment increased by HK\$37,591,000 which represented an increase of about 15.8% in 2005, mainly due to increase of sales orders. The operating profit of this segment increased by HK\$16,403,000 or an increase of about 140.3% in 2005, mainly due to increase of sales orders and reduction of cost of goods sold. The order on hand of the Group for the business of the manufacturing and trading of audio equipment was about HK\$26,654,000 as at 31 December, 2005.

The total borrowings of the Group decreased from about HK\$94,279,000 at the end of 2004 to about HK\$19,249,000 at the end of 2005, mainly due to exclusion of borrowings related to the Disposed Subsidiary. The Group maintained a low ratio of borrowings relative to total equity at about 0.2% as at 31 December, 2005 compared with that of at about 1.3% as at 31 December, 2004. The ratio of total liabilities relative to total equity decreased to only about 4.6% as at 31 December, 2005 from about 6.4% as at 31 December, 2004. The Group's borrowings were secured by leasehold land, property, plant and equipment and investment properties with a total net book value of about HK\$31,587,000 and bank balances of about HK\$30,684,000. As at 31 December, 2005, the Group had contingent liabilities of about HK\$14,125,000 which mainly represented guarantees of bank loans borrowed by an associate.

The Group had cash and bank balances of about HK\$1,663,197,000 as at 31 December, 2005. This included the net cash inflow from operating activities of about HK\$55,463,000. During the year, the payment of dividend by the Company was financed by the receipt of cash dividend from the investment vehicles.

The Group's general and administrative expenses for the year ended 31 December, 2005 were about HK\$94,852,000, representing a decrease of about 10.6% compared with that of 2004, mainly due to implementation of effective cost controls within the Group. The finance costs had no material variation. The interest cover remained at a high level of 1,398 multiples in 2005 compared to that of

1,460 multiples in 2004. The Group enjoyed the benefit of the currency appreciation of Renminbi, the major operating currency of the Group for the year ended 31 December, 2005, which was effective in July 2005 and resulted a significant exchange gains upon realization.

Share of losses of non-consolidated subsidiaries were about HK\$966,000 in 2005 compared with that of share of profits of about HK\$93,000 in 2004. Further, share of profits of associated companies were about HK\$13,137,000 in 2005, represented an increase of about 114.6% compared to that of 2004.

On 6 October, 2005, the Group announced a connected transaction to acquire 49% effective equity interest in a jointly controlled entity. The jointly controlled entity holds other jointly controlled entities and the Group classified all of them as other jointly controlled entities for presentation purpose. The transaction was approved by independent shareholders and completed on 2 November, 2005. After the completion of the transaction, the Group shared profits of HK\$16,232,000 from other jointly controlled entities in 2005.

Share of profit from a jointly controlled entity was the major source of profit for the Group, which contributed about HK\$1,900,443,000, and represented a decrease of about 8.5% compared with that of 2004, mainly due to the introduction of a new sales policy during the year. Due to its importance to the Group, the Group announced a connected transaction on 4 January, 2005 to acquire further interest in the jointly controlled entity and the transaction was approved by independent shareholders and completed on 4 February, 2005.

### EMPLOYEES AND REMUNERATION POLICY

As at 31 December 2005, the continuing operations of the Group employed approximately 1,800 (2004: 3,000) staffs in the PRC, Hong Kong and Australia.

The remuneration package adopted by the Group includes discretionary bonus and share options being granted to eligible staff based on the Group's performance and individual performance. Staff training and development programs are conducted on a regular basis.

### ACKNOWLEDGEMENTS

I would like to extend my appreciation to all shareholders for their support and to thank the Directors for their guidance and the staff members for their dedication and hard work.

**Zhang Fangyou**  
*Chairman*

Hong Kong, 19 April 2006