

Directors' Report

The directors present their annual report and the audited consolidated financial statements for the year ended 31 December 2006.

PRINCIPAL ACTIVITIES

The Company acts as an investment holding company. The activities of its principal subsidiaries are set out in note 30.

RESULTS AND APPROPRIATIONS

The results of the Group for the year ended 31 December 2006 are set out in the consolidated income statement on page 36 of the annual report.

The directors now recommend the payment of a final dividend of HKD 0.22 (Equivalent to RMB 0.22) per share to the shareholders on the register of member on 30 March, 2007, amounting to approximately HKD 228 million (Equivalent to RMB 229 million), and the retention of the remaining profit for the year of approximately RMB 395 million.

PROPERTY, PLANT AND EQUIPMENT

The Group continued its plant replacement policy and expended RMB 341 million on new plant and machinery during the year.

Details of the movement during the year in property, plant and equipment of the Group are set out in note 12 to the consolidated financial statements.

SUMMARY FINANCIAL INFORMATION

A summary of the published results and assets, liabilities and minority interest of the Group for the last five financial years is set out on page 74 of the annual report. This summary does not form part of the audited consolidated financial statements.

SHARE CAPITAL

Details of movements during the year in the share capital of the Company are set out in note 22 to the consolidated financial statements.



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DISTRIBUTABLE RESERVES OF THE COMPANY

Movements in the reserves of the Group during the year are set out on page 38 of the annual report.

The Company's reserves available for distribution represent the share premium, contributed surplus and accumulated profits which in aggregate amounted to approximately RMB 537 million as at 31 December, 2006 (2005: approximately RMB 566 million). Under the Companies Law (Revised) Chapter 22 of the Cayman Islands, the share premium of the Company is available for paying distributions or dividends to shareholders subject to the provisions of its Memorandum and Articles of Association and provided that immediately following the distribution or dividend the Company is able to pay its debts as they fall due in the ordinary course of business. In accordance with the Company's Article of Association, dividends shall be distributed out of the accumulated profits or other reserves, including the share premium account, of the Company.

DIRECTORS

The directors of the Company during the year and up to the date of this report were:

Executive directors:

Li San Yim (Chairman)	(appointed on 11 May 2004)
Qiu Debo (Chief Executive Officer)	(appointed on 17 February 2005)
Luo Jianru	(appointed on 17 February 2005)
Feng Wanru	(appointed on 17 February 2005 and resigned on 10 October 2006)
Chen Chao	(appointed on 17 February 2005)
Zhu Yong Sheng	(appointed on 17 February 2005 and resigned on 12 March 2007)
Zhang Hong	(appointed on 17 February 2005)
Mou Yan Qun	(appointed on 24 October 2006)
Lin Zhong Ming	(appointed on 24 October 2006)

Non-executive directors:

Ngai Ngan Ying	(appointed on 11 May 2004)
Zhu Mantian Myron	(appointed on 26 August 2005 and resigned on 16 March 2007)
Fang Deqin	(appointed on 16 March 2007)

Independent non-executive directors:

Yang Hongqi	(appointed on 13 June 2005)
Qian Shizheng	(appointed on 17 February 2005)
Lo Peter	(appointed on 17 February 2005)

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Pursuant to the Articles of Association, at each annual general meeting one-third of the directors for the time being (or if their number is not a multiple of three, the number nearest to but not less than one-third) shall retire from office by rotation provided that every director shall be subject to retirement at least once every three years. Each of Mr. Li San Yim, Mr. Qiu Debo, Mr. Luo Jianru, Mr. Chen Chao, Dr. Zhang Hong, Ms. Ngai Ngan Ying, Prof. Yang Hongqi, Dr. Qian Sizheng, and Mr. Lo Peter shall retire at the forthcoming annual general meeting (the "2006 AGM"). All the retiring directors are eligible for re-election at the 2006 AGM and all offer themselves for re-election at the 2006 AGM.

Under the Listing Rules, any person appointed by the directors to fill a casual vacancy on or as an addition to the board shall hold office only until the next following annual general meeting of the Company, and shall then be eligible for re-election. The Board has appointed Dr. Mou Yan Qun and Mr. Lin Zhong Ming as executive directors with effect from 24 October 2006 whereas Ms. Fang Deqin has been appointed as non-executive director with effect from 16 March 2007. Accordingly, they will hold office until the 2006 AGM and will be eligible for re-election. Dr. Mou Yan Qun, Mr. Lin Zhong Ming and Ms. Feng Deqin will offer themselves for re-election at the 2006 AGM.

The biographical details of the directors are set out on pages 13 to 18 of this annual report.

DIRECTORS' SERVICE CONTRACTS

No director proposed for re-election at the 2006 AGM has a service contract which is not determinable by the Group within one year without payment of compensation (other than statutory compensation).

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS IN SHARES AND UNDERLYING SHARES

As at 31 December 2006, the interests of the directors in the shares of the Company and its associated corporations as defined in the SFO as recorded in the register to be kept by the Company pursuant to Section 352 of Part XV of the SFO or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited pursuant to the Model Code for Securities Transaction by Directors of Listed Companies ("Model Code"), were as follows:

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(1) Long positions in shares and underlying shares of the Company

(a) Ordinary shares of HK\$0.10 each of the Company

Name of directors	Capacity	Number of shares held	Percentage of issued share capital as at 31 December 2006
Li San Yim and Ngai Ngan Ying	Held by controlled corporation (Note)	611,347,380	58.95%
Li San Yim and Ngai Ngan Ying	Beneficial owner	10,000,000	0.96%
		621,347,380	59.91%

Note: These shares were held through China Longgong Group Holdings Limited, a company that is wholly owned by Mr. Li, and Mrs. Li, (Ngai Ngan Ying) as to 55% and 45% respectively, which is the registered shareholder of these 611,347,380 shares.

(2) Long positions in shares and underlying shares of the associated corporation of the Company, Longgong (Shanghai) Machinery Company Limited.

(a) Ordinary shares of HK\$0.10 each of the Company

Name of directors	Capacity	Number of shares held	Percentage of issued share capital as at 31 December 2006
Li San Yim	Held by controlled corporation (Note)	480,000	0.375%
Ngai Ngan Ying	Held by controlled corporation (Note)	480,000	0.375%

Note: The 0.375% interest of Longgong (Shanghai) Machinery Company Limited, is held by Shanghai Longgong Machinery Company limited, which is owned by Mr. Li and Mrs. Li as to 39.5% and 60.5% respectively.

Save as disclosed above as at 31 December 2006, none of the directors, chief executives of the Company or any of their associates, had registered any interests or short positions in any shares and underlying shares of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) that was required to be recorded and kept in the register by the Company in accordance with the Section 352 of the SFO, or any

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interests required to be notified to the Company and the Stock Exchange pursuant to the Model Code.

ARRANGEMENTS TO PURCHASE SHARES OR DEBENTURES

At no time during the year was the Company, or any of its holding companies, subsidiaries or fellow subsidiaries, a party to any arrangements to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

DIRECTORS' INTERESTS IN CONTRACTS OF SIGNIFICANCE

No contracts of significance to which the Company, or any of its holding companies, subsidiaries, or fellow subsidiaries, was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

SUBSTANTIAL SHAREHOLDERS

As at 31 December 2006, the register of substantial shareholders maintained by the Company pursuant to Section 336 of the SFO shows that other than the interests disclosed above in respect of directors and chief executives, the following shareholders had notified the Company of the relevant interests in the issued share capital of the Company.

Long positions

Ordinary shares of HK\$0.10 each of the Company

Name of shareholder	Capacity	Number of ordinary shares held	Percentage of issued share capital as at 31 December 2006
China Longgong Group Holdings Limited (Note 1)	Beneficial owner	611,347,380	58.95%
Horseman Global Fund Limited	Beneficial owner	72,540,000	6.99%
Cazenove Asia Limited	Beneficial owner	60,414,000	5.83%
JPMorgan Cazenove Limited (Note 2)	Held by controlled corporation	60,414,000	5.83%
JPMorgan Cazenove Holdings (Note 3)	Held by controlled corporation	60,414,000	5.83%

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Cazenove Holdings Limited (Note 4)	Held by controlled corporation	60,414,000	5.83%
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Note 1: Mr Li and Mrs. Li own 55% and 45%, respectively, of the issued shares in the share capital of China Longgong Group Holdings Limited.

Note 2: These shares were held through Cazenove Asia Limited, a wholly owned subsidiary of JPMorgan Cazenove Limited.

Note 3: These shares were held through Cazenove Asia Limited, a wholly owned subsidiary of JPMorgan Cazenove Limited, which is in return wholly owned by JPMorgan Cazenove Holdings.

Note 4: These shares were held through Cazenove Asia Limited, a wholly owned subsidiary of JPMorgan Cazenove Limited, which is in return wholly owned by JPMorgan Cazenove Holdings. JPMorgan Cazenove Holdings is owned by Cazenove Holdings Limited as to 49.99%.

Saved as disclosed above, as at 31 December 2006, the Company has not been notified of any interests in the issued share capital of the Company as recorded and kept under section 336 of the SFO as having an interest of 5% or more of or any short positions in the issued share capital of the Company.

APPOINTMENT OF INDEPENDENT NON-EXECUTIVE DIRECTORS

The Company has received, from each of the independent non-executive directors, an annual confirmation of his independence pursuant to Rule 3.13 of the Rules Governing the Listing Securities on the Stock Exchange of Hong Kong Limited. The Company considers all of the independent non-executive directors are independent.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

There was no purchase, sales or redemption by the Company or any of its subsidiaries, of the Company's listed securities during the year ended 31 December 2006.

EMOLUMENT POLICY

The emolument policy of the employees of the Group is set up by the Human Resources Division on the basis of their merit, qualifications and competence.

The emoluments of the directors of the Company are decided by the Remuneration Committee, having regard to the Company's operating results, individual performance and comparable market statistics.

MAJOR CUSTOMERS AND SUPPLIERS

The five largest customers accounted for approximately 23% (2005: 27%) of the Group's total turnover for the

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year. The five largest suppliers accounted for approximately 38% (2005: 21%) of the Group's total purchases for the year and the largest supplier accounted for approximately 18% (2005: 19%) of the total purchases.

At no time during the year did a director, an associate of a director or a shareholder of the Company (which to the knowledge of the directors own more than 5% of the Company's issued share capital) have interest in any of the Group's five largest suppliers or customers.

POST BALANCE SHEET EVENTS

Details of significant events occurring after the balance sheet date are set out in note 31 to the consolidated financial statements.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's articles of association, or articles of association or the laws of Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

SUFFICIENCY OF PUBLIC FLOAT

The Company has maintained a sufficient public float throughout the year ended 31 December 2006.

AUDITORS

A resolution will be submitted to the annual general meeting of the Company to re-appoint Messrs. Deloitte Touche Tohmatsu as auditors of the Company.

On behalf of the Board

Mr. Li San Yim

CHAIRMAN

Shanghai 12 March 2007