

CHAIRMAN'S STATEMENT



To shareholders,

On behalf of the board (the "Board") of directors (the "Directors") of First Tractor Company Limited ("First Tractor" or the "Company"), I am pleased to present the annual report of the Company and its subsidiaries (collectively the "Group") to shareholders (the "Shareholders") of the Company for the year ended 31 December 2006 (the "Reporting Period").

During the Reporting Period, the Group recorded a turnover of RMB6,101,451,000, representing an increase of 28% over the same period last year. Earnings attributable to ordinary equity holders of the parent was RMB72,849,000, representing an increase of RMB123,285,000 over the same period last year. Earnings per share was 9.28 cents, representing an increase of 15.70 cents over the same period last year.

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BUSINESS REVIEW

During the Reporting Period, the agricultural machinery market experienced booming demands due to the farmers' strengthened purchasing power along with the increased income, as driven by the State's policies including the exemption of agricultural taxation and the granting of subsidies for the purchase of agricultural machinery and to grain-growers. Meanwhile, the farmers have greater incentive to purchase agricultural machinery with the improved systematisation of agricultural machinery services as a result of the farmers' enthusiasm in using agricultural machinery to ameliorate the agricultural operation environment. As a result, the demand of agricultural machinery was increased. The Group grasped such opportunities to strengthen technologies for the agricultural machinery business and speeded up adjustment to product mix. During the Reporting Period, the Group invested RMB50,790,000 in research and development of agricultural machinery with 48 projects completed, of which 17 projects were put into production in scale. The Group's production capacity and product quality were essentially improved. During the Reporting Period, the Group sold 154,000 units of agricultural machinery products with turnover amounting to RMB4,699,191,000, representing a year-on-year increase of 25.26%. Among them, sales of large/medium wheeled tractors were 42,166 units, rising by 68.86% over last year.

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During the Reporting Period, as driven by the rapid increase in investments in fixed assets in society and the extensive rise in export of construction machinery products, there was an overall recovery in the construction machinery industry. As such, having analysed the market opportunities and the problems in its construction machinery business, the Group took a series of measures including enhancement of internal management, consolidation of internal marketing resources and increase in development of new products, thereby improving the economic operation of such segment. During the Reporting Period, 9,403 units of construction machinery products of various types were sold with turnover amounting to RMB1,198,603,000 in 2006, representing a year-on-year increase of 18.22%. Albeit the loss has been decreased noticeably, the operational result was not satisfactory.

On 28 July 2006, the Group completed assets swap with China Yituo Group Corporation Limited ("China Yituo"), a holding company of the Company, by acquisition of the equity interests in the engine machinery business of China Yituo and disposal of casting factories interests to China Yituo, so as to accomplish vertical integration and improve quality of assets and the Company's profitability. The engine machinery business provided a new scope of development of the Group. For the period from 1 August 2006 to 31 December 2006, the engine machinery business achieved a turnover of RMB203,614,000.

During the Reporting Period, the Group maintained a stable increase in its financial business, which has provided an effective support on the Group's internal financial resources management and production operation, and has a positive effect on the profitability of the Group.

During the Reporting Period, apart from its efforts in strengthening its status in the local market, the Group strengthened its expansion to the international markets in order to develop an international marketing network and system for a shift from the passive sale to the active marketing. As a consequence of the intensified product export pattern focusing on agricultural machinery and construction machinery, the altered export modes, the optimised export product mix and timely adjusted international marketing modes, sales volume of the Group's products were substantially increased in the international markets. Particularly, the Group exported 1,211 large and medium wheeled tractors to Kyrgyzstan in one lot, setting a new record in terms of the export volume of a single order for the domestic tractor business. With 3,175 and 368 units of agricultural machinery of various types and construction machinery exported respectively during the Reporting Period, the Group recorded an aggregate turnover of US\$42,141,500 from export business in 2006, representing a rise of 76.10% from the same period last year.

CORPORATE GOVERNANCE

During the Reporting Period, the Company has enhanced and improved its corporate governance, implemented its duties to the Directors, proposed new requirements to the Company's operation and internal control. The Group improved its regulations and rules on the internal control system and evaluated and reviewed the operation effectiveness thereof. To enhance the management on the Company's subsidiaries, the Group formulated "Opinions on Standardising Subsidiaries' Corporation Governance Structure", thus ensuring the standard operation and proper decisions of the subsidiaries of the Company. During the Reporting Period, the Group did not have any significant risk or loss.

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BUSINESS OUTLOOK

As a large agricultural country, China's agricultural mechanisation and modernization strategically guarantee the national food supply. Therefore, the Government, by adopting a series of policies of supporting agricultural sector, building new countryside and accelerating agricultural mechanisation, has increased investment in agricultural sector and raised the income of farmers. Given the State's "three policies for agriculture" and structural change in domestic economy, rural lands are in the process of transition to intensive operation at a faster pace. All the factors above brought huge opportunities for the rapid and stable development of agricultural machinery. China is currently at an early stage of agricultural mechanisation and is progressing into a middle stage. In order to meet the needs arising from agricultural mechanisation, the Group will accelerate technological innovation and structural adjustment of agricultural machinery. The Company also strives to explore international markets for more developmental opportunities. In the meantime, the Government put efforts on infrastructure construction and road construction in rural areas during the period of "Eleventh Five-Year Plan", which have created opportunities for machinery and small construction machinery of the Group. Following rising environmentally-technological requirement for engine machinery imposed by the Government, the engine machinery business of the Group will face new developmental opportunities.

Looking ahead, following the development trend of China's agricultural mechanisation, the Group will stick to the philosophy of "creating value for shareholders and users" to secure the continuous and stable growth in the results and requite shareholders by launching various agricultural mechanical products that address the domestic agricultural mechanisation and the demands from international markets, and pressing ahead adjustments to industrial structure and product mix as well as consolidation of resources and business based on independent innovation, introduction and absorption.

Sustaining the fast growth of agricultural machinery business: In 2007, the Group will put more efforts in research and development of technology as well as research on market segment for large/medium wheeled tractors. By upgrading products with increased adaptability, broadening and deepening the product lines and highlighting branding operation to exert brand advantages, the Group aims to strengthen its prime position in the industry.

Crawler tractor: the Group will upgrade the market structure and product mix to further improve existing products, as to meet customers' needs.

Large/medium wheeled tractors: capturing the market capacity for large/medium wheeled tractors resulting from the expedited development of new countryside, the Group wishes to expand continuously on the fast growth of large/medium wheeled tractors, to maintain its leading status in the industry and to participate in international competition through development of new products and market exploration.

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Small wheeled tractors: along with the rising demands for large/medium wheeled tractors in the tractor market, the traditional small wheeled tractors market is expected to further shrink. In order to improve its competitiveness and profitability, the Company will alter its structure upgrade its products, develop modified product varieties and to strengthen its cost control.

Harvesters and agricultural machinery: the Group will upgrade the sales network and improve services for wheat harvesters based on its well-developed product techniques. Meanwhile, it will accelerate development of rice and corn harvesters as well as the large-feeding wheat and rice harvesters with enhanced adaptability and reliability in order to enhance its status in the industry.

Improving the operation of construction machinery business: In 2007, while capturing the time and opportunities of constructing new countryside by the Government, the Group provides new equipments that meet the needs of construction of new countryside. The Group also consolidated and improved the competitiveness of road machinery and small construction machinery products, through acceleration of product mix adjustment and establishment of new sales system and upgrade of technology for products, and raise its operation capability. The Group will undergo business and assets reorganisation in respect of loss-making products and businesses, by introducing strategic partners and system reform, and raise asset quality and profitability.

Consolidating the leading position of non-road engine machinery: The Group will speed up co-operation with international research institutes and promote upgrade of engine machinery products for higher better functions, higher economic efficiency and lower gas emission. While accommodating the needs of main products such as high horsepower tractors and consolidating the leading position of engine machinery business in ancillary agricultural machinery market in the PRC, the Group will accelerate the research and development of heavy power duty diesel machine so as to explore the market of business vehicles.

Utilising on financial resources: In 2007, the Group will utilise the financial resources of China First Tractor Group Finance Co., Ltd.. On one hand, the Group will seek to explore businesses of buyer credit and credit lease for the products of the Group, which provides strong support to its business development. On the other hand, the Group, through cooperation with other financial institutions, will broaden its business scope and improve its performance.

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International market and international cooperation

In addition to enhancing its export of large wheeled tractors, the Group will focus on the expansion of international market for medium wheeled tractors and road roller. The Group will speed up the construction of international marketing network and channels in order to improve its capability to explore international market. The Group will also actively advance its joint venture with internationally renowned corporations while continuously deepening and broadening the cooperation in terms of products, technology and capital and to enhance the Group's competitiveness and its influence internationally.

ACKNOWLEDGEMENT

I hereby wish to thank all Directors and staff of the Group for their dedications to the Group's growth in the previous year. On behalf of the Board, I would also like to express my sincere gratitude to all Shareholders, all walks of life and friends for their support and care for the Group's growth, give heartfelt thanks to all dedicated employees of the Group.

By order of the Board

Liu Dagong

Chairman

Luoyang, the PRC
20 April 2007