1. General

The Company was established as a joint stock company with limited liability in the People's Republic of China (the "PRC"). The Company's H shares are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") as from 11th March, 2004. The addresses of registered office and principal place of business of the Company are disclosed in the corporate information section in the annual report.

The consolidated financial statements are presented in Renminbi, which is the functional currency of the Company.

The principal activities of the Group are the manufacture and sale of diesel engines and related parts. The principal activities of its associate and subsidiaries are set out in notes 19 and note 37 respectively.

2. Application of New and Revised Hong Kong Financial Reporting Standards ("HKFRs")

In the current year, the Group has applied, for the first time, a number of new standard, amendments and interpretations ("new HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), which are either effective for accounting periods beginning on or after 1st December, 2005 or 1st January, 2006. The adoption of the new HKFRSs had no material effect on how the results and the financial position for the current or prior accounting years have been prepared and presented. Accordingly, no prior year adjustment has been required.

The Group has not early applied the following new standard, amendment and interpretations that have been issued but are not yet effective. The Directors of the Company anticipate that the application of these standard, amendment or interpretations will have no material impact on the financial statements of the Group.

HKAS 1 (Amendment)	Capital Disclosures[1]
HKFRS 7	Financial Instruments: Disclosures[1]
HKFRS 8	Operating Segments[2]
HK(IFRIC)-INT 7	Applying the Restatement Approach under HKAS29 Financial Reporting in Hyperinflationary Economies[3]
HK(IFRIC)-INT 8	Scope of HKFRS 2[4]
HK(IFRIC)-INT 9	Reassessment of Embedded Derivatives[5]
HK(IFRIC)-INT 10	Interim Financial Reporting and Impairment[6]
HK(IFRIC)-INT 11	HKFRS 2 — Group and Treasury Share Transactions[7]
HK(IFRIC)-INT 12	Service Concession Arrangements[8]

1 Effective for annual periods beginning on or after 1st January, 2007.

2 Effective for annual periods beginning on or after 1st January, 2009.

3 Effective for annual periods beginning on or after 1st March, 2006.

4 Effective for annual periods beginning on or after 1st May, 2006.

2. Application of New and Revised Hong Kong Financial Reporting Standards ("HKFRs") (Continued)

[5] Effective for annual periods beginning on or after 1st June, 2006.

[6] Effective for annual periods beginning on or after 1st November, 2006.

[7] Effective for annual periods beginning on or after 1st March, 2007.

[8] Effective for annual periods beginning on or after 1st January, 2008.

3. Significant Accounting Policies

The consolidated financial statements have been prepared on the historical cost basis, as explained in the accounting policies set out below.

The consolidated financial statements have been prepared in accordance with Hong Kong Fiancial Reporting Standards issued by the HKICPA. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on the Stock Exchange and the Hong Kong Companies Ordinance.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities (including special purpose entities) controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Minority interests in the net assets of consolidated subsidiaries are presented separately from the Group's equity therein. Minority interests in the net assets consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

3. Significant Accounting Policies (Continued)

Business combinations

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under *HKFRS 3 Business Combinations* are recognised at their fair values at the acquisition date.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

For business combination involves more than one exchange transaction through successive share purchases. Each exchange transaction are treated separately, using the cost of the transaction and fair value information at the date of each exchange transaction, to determine the amount of any goodwill associated with that transaction. Any adjustments to those fair values relating to previously held interests is accounted for as increase in revaluation reserve.

Interest in an associate

An associate is an entity over which the investor has significant influence and that is neither a subsidiary nor an interest in a jointly venture.

The results and assets and liabilities of associates are incorporated in these consolidated financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of net assets of the associates, less any identified impairment loss. When the Group's share of losses of an associate equals or exceeds its interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate), the Group discontinues recognising its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that associate.

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of the associate recognised at the date of acquisition is recognised as goodwill. The goodwill is included within the carrying amount of the investment and is assessed for impairment as part of the investment.

Any excess of the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognised immediately in profit or loss.

Where a group entity transacts with an associate of the Group, unrealised profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

Notes to the Consolidated Financial Statements

For the year ended 31st December, 2006

3. Significant Accounting Policies (Continued)

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amount receivable for goods and services provided in the normal course of business, net of discounts and sales related taxes.

Sales of goods are recognised when goods are delivered and title has passed.

Income from repairs are recognised when services are provided.

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Property, plant and equipment

Property, plant and equipment, other than construction in progress, are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

Depreciation is provided to write off the cost of items of property, plant and equipment other than construction in progress, over their estimated useful lives and after taking into account of their estimated residual value, using the straight-line method.

Construction in progress represents property, plant and equipment in the course of construction for production or for its own use purposes. Construction in progress is carried at cost less any recognised impairment loss. Construction in progress is classified to the appropriate category of property, plant and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the consolidated income statement in the year in which the item is derecognised.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the leasee. All other leases are classified as operating leases.

Rentals payable under operating leases are charged to profit or loss on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are recognised as a reduction of rental expense over the lease term on a straight-line basis.

3. Significant Accounting Policies (Continued)

Leasehold land and building

The land and building elements of a lease of land and building are considered separately for the purpose of lease classification, leasehold land which is not expected to pass to the lessee by the end of the lease term is classified as an operating lease unless the lease payment cannot be allocated reliably between the land and building elements, in which case, the entire lease is classified as finance lease.

Borrowing costs

All borrowing costs are recognised as and included in finance costs in the consolidated income statement in the period in which they are incurred.

Foreign currencies

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in the respective functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchanges prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date.

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the period in which they arise. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity, in which cases, the exchange differences are also recognised directly in equity.

Retirement benefit costs

Payments to the state-managed retirement benefit schemes, are charged as expenses when employees have rendered service entitling them to the contributions.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax base used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

3. Significant Accounting Policies (Continued)

Taxation (Continued)

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Intangible assets

Intangible assets acquired separately

Intangible assets acquired separately and with finite useful lives are carried at costs less accumulated amortisation and any accumulated impairment losses. Amortisation for intangible assets with finite useful lives is provided on a straight-line basis over their estimated useful lives. Alternatively, intangible assets with indefinite useful lives are carried at cost less any subsequent accumulated impairment losses (see the accounting policy in respect of impairment losses below).

Gains or losses arising from derecognition of an intangible asset are measured at the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the consolidated income statement when the asset is derecognised.

Research and development expenditures

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

The amount initially recognised for internally-generated intangible asset is the sum of the expenditure incurred from the date when the intangible asset first meets the recognition criteria. Where no internally generated intangible asset can be recognised, development expenditure is charged to profit or loss in the year in which it is incurred.

Subsequent to initial recognition, internally-generated intangible asset is reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets acquired separately.

Impairment

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually by comparing their carrying amounts with their recoverable amounts, irrespective of whether there is any indication that they may be impaired. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediate.

3. Significant Accounting Policies (Continued)

Intangible assets (Continued)

Impairment (Continued)
When an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years.

Intangible assets with finite useful lives are tested for impairment when there is an indication that an asset may be impaired (see the accounting policies in respect of impairment losses for tangible and intangible assets below).

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the weighted average method.

Financial instruments

Financial assets and financial liabilities are recognised on the balance sheet when a group entity becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

Financial assets
The Group's financial assets are classified into loans and receivables and available-for-sale financial assets. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace. The accounting policies adopted in respect of financial assets are set out below.

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. At each balance sheet date subsequent to initial recognition, loans and receivables (including trade and bills receivables, deposits, other receivables, pledged bank deposits and bank balances and cash) are carried at amortised cost using the effective interest method, less any identified impairment losses. An impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. Impairment losses are reversed in subsequent periods when an increase in the asset's recoverable amount can be related objectively to an event occurring after the impairment was recognised, subject to a restriction that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Notes to the Consolidated Financial Statements

For the year ended 31st December, 2006

3. Significant Accounting Policies (Continued)

Financial instruments (Continued)

Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated or not classified as financial assets at fair value through profit or loss, loans and receivables or held-to-maturity investments.

For available-for-sale equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments, they are measured at cost less any identified impairment losses at each balance sheet date subsequent to initial recognition. An impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired. The amount of the impairment loss is measured as the difference between the carrying amount of the asset and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment losses will not reverse in profit or loss in subsequent periods.

Financial liabilities and equity

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

An equity instrument is any contract that evidences a residual interest in the assets of the group after deducting all of its liabilities. The Group's financial liabilities are generally classified as other financial liabilities. The accounting policies adopted in respect of financial liabilities and equity instruments are set out below.

Other financial liabilities

Other financial liabilities including trade and bills payables, other payables, amount due to a related party and unsecured bank borrowings are subsequently measured at amortised cost, using the effective interest rate method.

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and the cumulative gain or loss that had been recognised directly in equity is recognised in profit or loss.

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

3. Significant Accounting Policies (Continued)

Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the Directors' best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material.

Impairment loss (other than goodwill, intangible assets with indefinite useful lives (see the accounting policies in respect of goodwill and intangible assets above))

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

Where an impairment loss is subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

4. Critical Accounting Judgements and Key Sources of Estimation Uncertainty

Critical Judgement in Applying the Entity's Accounting Policies

In the process of applying the entity's accounting policies, which are described in note 3, management has made the following judgments that have the most significant effect on the amounts recognised in the financial statements (apart from those involving estimations, which are dealt with below.)

Intangible assets with indefinite useful lives

As detailed in note 17, trademarks with a carrying amounts of RMB108,892,000 have a legal life up to 2012 but are renewable every 10 years at minimal costs. The Directors of the Company considered that these trademarks for all practical purposes have an indefinite useful life and therefore they will not be amortised until their useful life is determined to be finite and they will be tested for impairment annually.

Key Sources of Estimation Uncertainty

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

Estimated carrying amounts of intangible assets

Determining whether intangible assets are to be impaired requires an estimation of the value in use of the cash generating units to which intangible assets have been allocated. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate the present value. As at 31st December, 2006, the carrying amount of intangible assets are approximately RMB140,003,000. Details of the recoverable amount calculation are disclosed in note 18.

4. Critical Accounting Judgements and Key Sources of Estimation Uncertainty (Continued)

Key Sources of Estimation Uncertainty (Continued)

Warranty expenses

The Group offers a six month to one year warranty for its products, during which free warranty service for the repair and maintenance of parts or components under normal usage is provided to the customers. Warranty expenses are accrued with reference to historical cost data for repairs and maintenance, and units of products sold.

5. Financial Instruments

The Group's major financial instruments include trade and bills receivables, deposits, other receivables, pledged bank deposits, bank balances and cash, trade and bills payables, other payables, borrowings, discounted bills with recourse and amount due to a related party. Details of these financial instruments are disclosed in respective notes. The risks associated with these financial instruments and the policies on how to mitigate these risks are set out below. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

Market risk

Currency risk

The Group has foreign currency purchases, which expose the Group to foreign currency risk. Certain trade payables of the Group are denominated in foreign currencies. The Group currently does not have a foreign currency hedging policy. However, the management monitors foreign exchange exposure and will consider hedging significant foreign currency exposure should the need arises.

Fair value interest rate risk

The Group is exposed to fair value interest rate risk relating to pledged bank deposits and fixed rate bank borrowings. The Group currently does not have any interest rate hedging policy. The interest rates and terms of repayment of bank borrowings of the Group are disclosed in notes 24 and 26.

Cash flow interest rate risk

The Group's cash flow interest rate risk relates primarily to cash and cash equivalents and variable-rate bank borrowings (see Notes 24 and 26 for details of these items). It is the Group's intention to keep its borrowings at floating rate of interests so as to minimise the cash flow interest rate risk.

Credit risk

The Group's maximum exposure to credit risk in the event of the counterparties failure to perform their obligations as at 31st December, 2006 in relation to each class of recognised financial assets is the carrying amount of those assets as stated in the consolidated balance sheet. In order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade debt at each balance sheet date to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the Directors of the Company consider that the Group's credit risk is significantly reduced.

5. Financial Instruments (Continued)

Market risk (Continued)

Credit risk (Continued)
The Group has a number of counterparties and customers, however, credit risk of the Group is concentrated on certain major customers. At 31st December, 2006, the five largest receivable balances accounted for approximately 81% of the trade receivable balances. The management considers the credit risk involved is acceptable/properly managed in view of the strong financial background and good credit standing of these customers.

The credit risk on liquid funds is limited because the counterparties are banks in the PRC with high credit rating.

Liquidity risk
In managing liquidity risk, the Group monitors and maintains a level of cash and cash equivalents deemed adequate by the management to finance the Group's operations and mitigate the effects of fluctuations in cash flows. The management monitors the utilisation of bank borrowings and ensures compliance with loan covenants.

In addition to the above, risks relating to financial instruments, the Group is exposed to the commodity price risk such as steel and metal (major components of the Group's raw materials). The Group currently does not have any commodity futures to hedge the price risk exposure of its raw material purchases.

6. Business and Geographical Segments

The Group was principally engaged in the manufacture and sale of diesel engines and related parts and over 90% of the Group's turnover and operating results were derived from the PRC and accordingly, no analysis of business and geographical segment is presented.

Notes to the Consolidated Financial Statements

For the year ended 31st December, 2006

7. Other Income

	2006 RMB'000	2005 RMB'000
Other income includes:		
Gain on sale of scrap and other materials	**11,832**	32,402
Sales and warranty period repair services fee income	**16,330**	21,025
Bank interest income	**10,780**	10,246
Warehouse uploading and logistic services fee income	**8,524**	630
Write back of bad debt provision	**29,387**	—
Gain on disposal of property, plant and equipment	**879**	—
Compensation from China Heavy Duty Track Group Co. Ltd. ("CHDTGL") (note 21)	**13,540**	—
Others	**8,057**	5,660
	99,329	69,963

8. Finance Costs

	2006 RMB'000	2005 RMB'000
Interest on:		
Bank borrowings wholly repayable within five years	**53,841**	30,843
Imputed interest expense on amount due to a related party	**9,319**	12,135
	63,160	42,978

9. Profit Before Taxation

	2006 RMB'000	2005 RMB'000
Profit before taxation has been arrived at after charging (crediting):		
Directors' and Supervisors' emoluments (note 11)	**3,606**	3,874
Staff costs excluding Directors' and Supervisors' emoluments	**328,954**	236,995
Retirement benefits scheme contributions excluding amounts included in Directors' and Supervisors' emoluments	**29,816**	27,328
Total staff costs	**362,376**	268,197
Depreciation of property, plant and equipment	**193,662**	109,597
Release of prepaid lease payments (included in administrative expenses)	**1,278**	1,278
Amortisation of intangible assets (included in administrative expenses)	**62,223**	62,223
Auditors' remuneration	**5,000**	3,000
Impairment loss on trade receivables	**—**	15,272
Cost of inventories recognised as expense	**4,742,383**	4,096,408
Share of tax of an associate (included in share of results of an associate)	**27,383**	(311)
Loss on disposal of property, plant and equipment	**—**	489

Included in the total staff costs is an amount of approximately RMB36,000,000 (2005: RMB3,000,000) relating to bonus accrued for the Group's senior management including directors and supervisors. However, the amounts allocated to each individual have not been determined.

10. Income Tax Expense

	2006 RMB'000	2005 RMB'000
PRC Enterprise Income Tax:		
Current year	**168,736**	106,379
Under(over)provision in prior years	**246**	(203)
Tax credit	**—**	(10,407)
	168,982	95,769
Deferred tax (note 29)	**12,117**	(1,850)
	181,099	93,919

PRC Enterprise Income companies in the PRC comprising Tax is calculated at the statutory income tax rate of 33% (2005: 33%) of the assessable profit of the Group, except that the assessable profit derived from the production in the high technology development zone is taxed at a preferential rate of 15% (2005: 15%) pursuant to the following governmental notices:

(i) Notice of Ministry of Finance and the State Administration of Taxation concerning certain preferential policies on enterprise income tax (財政部、國家稅務總局《關於企業所得稅若干優惠政策的通知》); and

(ii) Notice of the State Administration of Taxation concerning proper implementation of the continuing administrative work after the cancellation delegation of the examination and approval procedure for enterprise income tax (國家稅務總局《關於做好已取消和下放管理的企業所得稅審批項目後續管理工作的通知》).

Pursuant to the notice issued by Jiang Jing Municipal Tax Bureau, the Company's Chongqing branch is also subject to PRC Enterprise Income Tax at a preferential rate of 15% (2005: 15%).

The Company's Hong Kong branch is subject to Hong Kong Profits Tax at 17.5% (2005: 17.5%) on its estimated assessable profit. No provision for Hong Kong Profits Tax has been made as the branch had no assessable profit for the year.

Pursuant to the notices issued by Weifang Municipal Tax Bureau and Chongqing Municipal Tax Bureau, the Group was entitled to a total income tax credit of approximately RMB10,407,000 for the year ended 31st December, 2005 in respect of eligible additions of domestic machinery and equipment for production use. No tax credit has been granted for the year.

According to 《山東省人民政府國有資產監督管理委員會》 (魯國資分配函(2006)45號), the Company has received an approval for 工效掛鈎方案 in respect of its eligible deduction on salaries.

10. Income Tax Expense (Continued)

The taxation charge for the year can be reconciled to the profit before taxation per the income statement as follows:

	2006 RMB'000	2005 RMB'000
Profit before taxation	**889,109**	410,602
Tax at PRC Enterprise Income Tax rate of 33% (2005: 33%)	**293,406**	135,499
Tax effect of share of results of an associate	**(10,591)**	(311)
Tax effect of expenses not deductible for tax purpose	**51,727**	11,310
Effect of tax exemption and concession granted to the Company	**(130,733)**	(26,803)
Effect of different tax rate for the Company's Chongqing branch	**(22,956)**	(15,166)
Under(over)provision in prior years	**246**	(203)
Tax credit	**—**	(10,407)
	181,099	93,919

11. Directors' and Supervisors' Emoluments

The remuneration paid or payable to each of the 16 (2005: 16) Directors and 3 (2005: 3) Supervisors were as follows:

2006

	Tan Xuguang RMB'000	Xu Xinyu RMB'000	Sun Shaojun RMB'000	Zhang Quan RMB'000	Yeung Sai Hong RMB'000	Chen Xue Jian RMB'000	Yao Yu RMB'000	Li San Yim RMB'000	Liu Huisheng RMB'000	Zhang Fusheng RMB'000	Julius G. Kiss RMB'000	Han Xiaoqun RMB'000	Tong Jingen RMB'000	Zhang Xiaoyu RMB'000	Koo Fook Sun, Louis RMB'000	Fang Zhongchang RMB'000	Sun Chengping RMB'000	Wang Yong RMB'000	Jiang Jianfang RMB'000	Total RMB'000
Fees	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
Other emoluments																				
Salaries and other benefits	380	300	300	300	50	50	50	50	50	50	50	50	25	100	138	100	50	108	50	2,251
Retirement benefits scheme contribution	3	3	3	3	–	–	–	–	–	–	–	–	–	–	–	–	–	3	–	15
Performance related incentive payments	228	278	278	278	–	–	–	–	–	–	–	–	–	–	–	–	–	278	–	1,340
Total emoluments	611	581	581	581	50	50	50	50	50	50	50	50	25	100	138	100	50	389	50	3,606

2005

	Tan Xuguang RMB'000	Xu Xinyu RMB'000	Sun Shaojun RMB'000	Zhang Quan RMB'000	Yeung Sai Hong RMB'000	Chen Xue Jian RMB'000	Yao Yu RMB'000	Li San Yim RMB'000	Tong Jingen RMB'000	Zhang Fusheng RMB'000	Julius G. Kiss RMB'000	Han Xiaoqun RMB'000	Feng Gang RMB'000	Koo Fook Sun, Louis RMB'000	Zhang Xiaoyu RMB'000	Fang Zhongchang RMB'000	Sun Chengping RMB'000	Wang Yong RMB'000	Jiang Jianfang RMB'000	Total RMB'000
Fees	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
Other emoluments																				
Salaries and other benefits	380	250	250	250	50	50	50	50	50	50	50	2	48	146	100	100	50	60	50	2,036
Retirement benefits scheme contribution	76	50	50	50	–	–	–	–	–	–	–	–	–	–	–	–	–	12	–	238
Performance related incentive payments	500	300	300	300	–	–	–	–	–	–	–	–	–	–	–	–	–	200	–	1,600
Total emoluments	956	600	600	600	50	50	50	50	50	50	50	2	48	146	100	100	50	272	50	3,874

Note: The performance related incentive payment is determined as a percentage of the Group's profit for the each of the two years ended 31st December, 2006.

12. Employees' Emoluments

Of the five individuals with the highest emoluments in the Group, four (2005: four) were Executive Directors of the Company whose emoluments are included in the disclosures in note 11 above. The emoluments of the remaining one (2005: one) individual was as follows:

	2006 RMB'000	2005 RMB'000
Salaries and allowances	**1,900**	1,352
Retirement benefits scheme contributions	**12**	12
	1,912	1,364

No emoluments were paid by the Group to the Directors, Supervisors or the five highest paid individuals as an inducement to join or upon joining the Group or as a compensation for loss of office. None of the Directors nor any of the Supervisors waived any emoluments for either 2005 or 2006.

13. Dividends

	2006 RMB'000	2005 RMB'000
Final, paid — 2005: RMB0.165 (2004: RMB0.15) per share	**54,450**	49,500
Interim, paid — 2006: RMB0.20 (2005: RMB0.165) per share	**66,000**	54,450
	120,450	103,950

The Board has resolved that it will not propose a final dividend for the Company for 2006 until the Merger (as defined in note 19) is completed. After the completion of the Merger, the Board will meet again to consider proposing a final dividend (if any) for the Company for 2006 for the consideration and approval by the 2006 annual general meeting of the Company.

14. Basic Earnings Per Share

The calculation of basic earnings per share attributable to the equity holders of the Company is based on the profit for the year attributable to equity holders of the Company of approximately RMB702,695,000 (2005: RMB315,203,000) and on 330,000,000 (2005: 330,000,000) ordinary shares in issue during the year.

No diluted earnings per share has been presented as there is no potential ordinary share issue during both years.

15. Property, Plant and Equipment

	Construction in progress RMB'000	Buildings RMB'000	Plant and machinery RMB'000	Computer, equipment and fixtures RMB'000	Motor vehicles RMB'000	Total RMB'000
COST						
At 1st January, 2005	473,795	75,150	388,891	33,636	34,431	1,005,903
Additions	801,634	—	148	4,849	612	807,243
Transfer	(967,196)	276,724	622,223	30,155	38,094	—
Disposals	—	—	(1,086)	(109)	(274)	(1,469)
At 31st December, 2005	308,233	351,874	1,010,176	68,531	72,863	1,811,677
Additions	520,909	—	3,161	2,708	640	527,418
Transfer	(191,285)	36,985	130,037	9,594	14,669	—
Disposals	—	—	(66)	(392)	(2,350)	(2,808)
At 31st December, 2006	637,857	388,859	1,143,308	80,441	85,822	2,336,287
DEPRECIATION						
At 1st January, 2005	—	8,404	69,143	8,604	7,819	93,970
Charged for the year	—	12,462	77,860	9,247	10,028	109,597
Eliminated on disposals	—	—	(505)	(79)	(146)	(730)
At 31st December, 2005	—	20,866	146,498	17,772	17,701	202,837
Charged for the year	—	19,976	145,737	16,508	11,441	193,662
Eliminated on disposals	—	—	(36)	(278)	(2,074)	(2,388)
At 31st December, 2006	—	40,842	292,199	34,002	27,068	394,111
CARRYING VALUE						
At 31st December, 2006	637,857	348,017	851,109	46,439	58,754	1,942,176
At 31st December, 2005	308,233	331,008	863,678	50,759	55,162	1,608,840

The above items of property, plant and equipment, other than construction in progress, are depreciated over their estimated useful lives and after taking into account of their estimated residual value, using the straight-line method at the following rates per annum:

Buildings	20 years
Plant and machinery	5 to 10 years
Computer, equipment and fixtures	5 years
Motor vehicles	5 years

All buildings are erected on land held under medium-term land use rights in the PRC.

16. Prepaid Lease Payments

The Group's prepaid lease payments represented land in the PRC held under medium-term land use rights.

	2006 **RMB'000**	2005 RMB'000
Analysed for reporting purposes as:		
Current	**1,278**	1,278
Non-current	**59,213**	60,491
	60,491	61,769

17. Intangible Assets

	Trademarks RMB'000 (Note i)	**Technologies** RMB'000 (Note ii)	**Total** RMB'000
COST			
At 1st January, 2005, 31st December, 2005 and 31st December, 2006	119,264	222,965	342,229
AMORTISATION			
At 1st January, 2005	10,372	67,408	77,780
Charge for the year	—	62,223	62,223
At 31st December, 2005	10,372	129,631	140,003
Charge for the year	—	62,223	62,223
At 31st December, 2006	10,372	191,854	202,226
CARRYING VALUE			
At 31st December, 2006	108,892	31,111	140,003
At 31st December, 2005	108,892	93,334	202,226

17. Intangible Assets (Continued)

Notes:

(i) The trademarks have a legal life up to 2012 but are renewable every 10 years at minimal cost. The Directors of the Company are of the opinion that the Group has both the intention and ability to renew the trademarks continuously. As a result, the useful life of the trademarks is considered by the management of the Group as having an indefinite because it is expected to contribute to net cash inflows indefinitely. The trademarks will not be amortised until its useful life is determined to be finite. Instead it will be tested for impairment annually and whenever there is an indication that it may be impaired. Particulars of the impairment testing are disclosed in note 18.

(ii) The cost of technologies is amortised on a straight-line basis over 4.5 years.

18. Impairment Testing on Trademarks with Indefinite Useful Lives

As explained in note 6, the Group was principally engaged in the business of manufacture and sale of diesel engines and related parts, which is the Group's only cash generating unit (CGU). For the purposes of impairment testing, trademarks with indefinite useful lives at 31st December, 2006 set out in note 17 are fully allocated to this unit.

During the year ended 31st December, 2006, management of the Group determines that there are no impairment of its CGU containing trademarks with indefinite useful lives.

That calculation uses cash flow projections based on financial budgets approved by management for the next five years and a discount rate of 12%. The cash flows for the following five years are extrapolated based on an estimated growth rate of 10% which is in line with the anticipated growth rate of the motor vehicle industry in the PRC. This rate does not exceed the average long-term growth rate for the relevant markets. Other key assumptions for the value in use calculations relate to the estimation of cash inflows/outflows which include budgeted sales and gross margin, such estimation is based on the CGU's past performance and management's expectations for the market development. Management believes that any reasonably possible change in any of these assumptions would not cause the aggregate carrying amount of the CGU to exceed the aggregate recoverable amount of the CGU.

19. Interest in an Associate

	2006 RMB'000	2005 RMB'000
Cost of investment in associate (Note):		
Listed in the PRC	**1,046,872**	—
Unlisted in the PRC	**—**	560,250
Share of post-acquisition profit	**20,859**	941
	1,067,731	561,191

At 31st December, 2005, the Group held 45% in Weichai Power (Weifang) Investment Co., Limited ("Weifang Investment") which is an investment company established in the PRC whose principal asset is 28.12% interest in TAGC (as defined below) in the form of domestic shares. On 30th June, 2006, the Group completed the acquisition of the remaining 55% interest in Weifang Investment not already owned by it. Accordingly, Weifang Investment became a wholly-owned subsidiary of the Group and TAGC became a direct associate of the Group. TAGC is a company established in the PRC with its A shares listed on Shenzhen Stock Exchange.

On 12th November, 2006, the Company entered into an agreement ("Merger Agreement") with TAGC for the purpose of merging the Company and TAGC and the issue of new A Shares by the Company (which will be listed on the Shenzhen Stock Exchange upon Completion of the merger) ("Weichai A Shares") to the shareholders of TAGC (other than Weifang Investments) at the ratio of one Weichai A Share to 3.53 of TAGC held by such shareholders of TAGC ("Merger"). The Merger will be accompanied by a cash alternative to the shareholders of TAGC who elected not to received in whole (or in part) the Weichai A shares at the rate of RMB5.05 per TAGC. The Company itself will not be a cash alternative provider and it shall be arranged by the sponsor to the listing of the Weichai A share.

After the completion of the Merger, (i) the shares of TAGC will be cancelled; (ii) TAGC's assets will be absorbed into and its liabilities assumed by the Company; (iii) TAGC will be deregistered and will cease to exist; and (iv) the Weichai A shares will be listed on the Shenzhen Stock Exchange while the H shares of the Company continue to be listed on the Stock Exchange. The shareholder of A shares and H shares shall bear the same rights. The proposed merger is expected to be completed in the second quarter of 2007.

Note:

Included in the cost of investment in associate is goodwill of approximately RMB599,552,000 (2005: RMB278,286,000) attributable to the acquisitions of TAGC. The movement of goodwill is set out below.

	RMB'000
COST	
Arising on acquisition of Weifang Investment during the year ended 31st December, 2005	278,286
Arising on acquisition of remaining interest in Weifang Investment in 2006 (note 30)	321,266
At 31st December, 2006	599,552

19. Interest in an Associate (Continued)

Further details of the Group's associate at 31st December, 2006 are as follow:

Name of entity	Form of business structure	Country of registration/ Principal place of operation	Paid up registered capital RMB	Proportion of registered capital held by the Group	Principal activity
Torch Automobile Group Co., Ltd. ("TAGC") (湘火炬汽車集團股份有限公司)	Incorporated	The PRC	RMB936,287,000	28.12%	Manufacture and sale of heavy trucks and related parts and components

The summarised financial information is set out below:

	TAGC 2006 RMB'000	Weifang Investment 2005 RMB'000
As at 31st December		
Total assets	**10,280,493**	1,247,714
Total liabilities	**(6,713,704)**	(623)
Group's share of net assets of the associate	**468,179**	282,905
For the year ended 31st December		
Revenue	**11,221,963**	4,052
Profit for the year attributable to equity holders of the associate	**191,791**	2,091
Group's share of results of associate for the year	**32,094**	941

20. Available-for-sale Financial Assets

Available-for-sale financial assets at the balance sheet date represented an investment in 5.71% (2005: 5.71%) of the registered capital of 福田雷沃國際重工股份有限公司 ("福田雷沃") (formerly known as 山東福田重工股份有限公司), a private entity established in the PRC. These are measured at cost less impairment at each balance sheet date because the range of reasonable fair value estimates is significant and the Directors of the Company are of the opinion that the fair value cannot be measured reliably.

21. Deposits Paid for Acquisition of Property, Plant and Equipment

At the balance sheet date, the amount represented deposits paid to certain vendors for the acquisition of property, plant and equipment. Details of the related capital commitments are set out in note 31.

At 31st December, 2005, included in the balance was a refundable deposit of RMB80,000,000 paid to CHDTGL in relation to a framework agreement dated 27th September, 2004 for the Group to acquire certain assets of Hangzhou Motor Engine Factory, a wholly-owned subsidiary of CHDTGL.

CHDTGL was the holding company of 濰坊柴油機廠 Weifong Diesel Engine Works ("Weichai Factory") which held 23.53% interest in the Company as at 31st December, 2006. On 20th March, 2006, 山東省人民政府國有資產監督管理委員會 (State-owned Assets Supervision and Administration Commission of Shandong Province People's Government, "Shandong SASAC") issued a document approving the segregation of ownership between CHDTGL and Weichai Factory whereby CHDTGL transferred its entire ownership in Weichai Factory to Shandong SASAC for its direct holding. CHDTGL ceased to have direct or indirect interest in the Company thereafter.

On 23rd December, 2006, the Company entered into a settlement agreement with CHDTGL whereby CHDTGL would refund the above-mentioned deposit and also pay a compensation of RMB13,540,000 to the Company for the termination of the framework agreement. Accordingly, the deposit was classified as a current asset at 31st December, 2006.

22. Inventories

	2006 RMB'000	2005 RMB'000
Raw materials and consumables	**296,209**	340,362
Work-in-progress	**96,983**	81,041
Finished goods	**503,800**	224,175
	896,992	645,578

23. Trade and Bills Receivables/Deposits, Prepayments and other Receivables

Trade and bills receivables

	2006 RMB'000	2005 RMB'000
Third party customers	**43,892**	151,850
Related party and connected person customers (Note i)	**124,586**	251,128
Less: accumulated impairment	**(8,032)**	(42,584)
	160,446	360,394
Bills receivable (Note ii)	**1,236,830**	801,655
	1,397,276	1,162,049

Notes:

(i) The related party customers represented Weichai Factory, CHDTGL, 龍工(福建)機械有限公司 (Longgong Fujian Machinery Company Limited ("Longgong Fujian")) and 龍工(上海)機械有限公司 (Longgong Shanghai Machinery Company Limited ("Longgong Shanghai")) and 廣西柳工集團有限公司 ("Guangxi Liugong").

Details of the relationship with Fujian Longgong, Shanghai Longgong and Guangxi Liugong are set out in note 35(a).

(ii) The bills are non-interest bearing and have a maturity of six months.

The credit terms granted by the Group to its customers are normally in the range from 30 days to 180 days. However, customers with established trading records could be granted longer credit period. The following is an aged analysis of trade and bills receivables net of impairment losses as at the balance sheet date:

	2006 RMB'000	2005 RMB'000
Within 90 days	**1,163,198**	974,679
Between 91 to 180 days	**104,279**	180,522
Between 181 to 365 days	**30,187**	2,916
Over 365 days	**99,612**	3,932
	1,397,276	1,162,049

The carrying amounts of the Group's trade and bills receivables approximate their fair value at the balance sheet date.

Deposits, prepayments and other receivables

The carrying amount of the Group's deposits and other receivables approximate their fair values at the balance sheet date.

24. Pledged Bank Deposits/Bank Balances and Cash

Pledged bank deposits

The pledged bank deposits carry prevailing bank interest rates of 1.65% (2005: 1.10%) per annum. The pledge will be released upon the settlement of the relevant bank borrowings. The carrying amount of the bank deposits approximates its fair value at the balance sheet date.

Bank balances and cash

Bank balances and cash, which carry prevailing market interest rates ranging from 0.72% to 1.62% (2005: ranging from 0.30% to 1.10%) per annum, comprise cash held by the Group and short-term bank deposits with an original maturity of three months or less. The carrying amounts of these assets approximate their fair values at the balance sheet date.

25. Trade and Bills Payables/Other Payables and Accruals

Trade and bills payables

	2006 RMB'000	2005 RMB'000
Third party suppliers	**1,357,532**	1,184,615
Related party and connected person suppliers (Note i)	**26,227**	75,411
	1,383,759	1,260,026
Bills payable (Note ii)	**1,081,811**	551,480
	2,465,570	1,811,506

Notes:

(i) The related party suppliers represented Weichai Factory and CHDTGL.

(ii) The bills are non-interest bearing and have a maturity of six months.

Notes to the Consolidated Financial Statements

For the year ended 31st December, 2006

25. Trade and Bills Payables/Other Payables and Accruals (Continued)

Trade and bills payables (Continued)

	2006 RMB'000	2005 RMB'000
An analysis of trade and bills payables as at the balance sheet date is as follows:		
Within 90 days	**1,672,493**	1,312,896
Between 91 to 180 days	**685,237**	439,327
Between 181 to 365 days	**15,360**	13,123
Over 365 days	**92,480**	46,160
	2,465,570	1,811,506

The carrying amount of the Group's trade and bills payables approximates their carrying amount at the balance sheet date.

Other payables and accruals

The carrying amount of the Group's other payable approximates their carrying amount at the balance sheet date.

26. Unsecured Bank and Other Borrowings

	2006 RMB'000	2005 RMB'000
Unsecured bank borrowings	**348,087**	334,241
Unsecured other borrowing	**324,183**	—
	672,270	334,241
The maturity profile of the above bank borrowings is as follows:		
On demand or within one year	**198,087**	44,241
More than one year, but not exceeding two years	**474,183**	240,000
More than two years, but not exceeding three years	**—**	50,000
	672,270	334,241
Less: Amounts due within one year shown under current liabilities	**(198,087)**	(44,241)
	474,183	290,000

26. Unsecured Bank and Other Borrowings (Continued)

Unsecured bank borrowings include fixed rate borrowings of RMB270,000,000 (2005: RMB310,000,000) and variable rate bank borrowings of USD10,000,000 (equivalent to approximately RMB78,087,000) (2005: RMB24,241,000) which is denominated in currencies other than the functional currencies of the relevant group entities.

The Group's variable-rate borrowings carry interest at London Interbank Offered Rate. Interest is repriced every six months.

The ranges of effective interest rates (which are also equal to contracted interest rates) on the Group's bank borrowings are as follows:

	2006	2005
Effective interest rate per annum:		
Fixed-rate borrowings	**5.6% to 6.1%**	5.6% to 5.8%
Variable-rate borrowings	**6.5%**	5.3%

During the year, the Group obtained new loans in the amount of RMB498,029,000. The loans bear interest at market rates and will be repayable in 2008.

The carrying amount of the Group's bank borrowings approximates to the corresponding fair value at the balance sheet date.

27. Warranty Provision

	RMB'000
At 1st January, 2005	12,996
Additional provision in the year	195,851
Utilisation of provision	(190,288)
At 31st December, 2005	18,559
Additional provision in the year	
Utilisation of provision	233,474
At 31st December, 2006	(204,868)
	47,165

The warranty provision represents management's best estimate of the Group's liability under six-month to one-year warranty granted on products, based on past experience for defective products.

Notes to the Consolidated Financial Statements

For the year ended 31st December, 2006

28. Share Capital

The Company's share capital structure at the balance sheet date is as follows:

	Number of shares		Registered, issued and fully paid
	Domestic shares	H shares	
	'000	'000	RMB'000
At 1st January, 2005, 31st December, 2005 and 31st December, 2006	203,500	126,500	330,000

Each share has a par value of RMB1.

29. Deferred Taxation

The following are the major deferred tax liabilities and assets recognised and movements thereon during the current and prior years:

	Trademarks	Others	Total
	RMB'000	RMB'000	RMB'000
Charge (credit) to income statement for the year ended 31st December, 2005 and at 31st December, 2005	5,133	(6,983)	(1,850)
Charge to income statement for the year	5,134	6,983	12,117
At 31st December, 2006	10,267	—	10,267

30. Acquisition of a Subsidiary

On 30th June, 2006, the Group acquired 55% further equity interest in Weifang Investment for a cash consideration of RMB684,750,000. Prior to the acquisition, Weifang Investment was owned as to 45% by the Group. Following the acquisition, Weifang Investment became a wholly-owned subsidiary of the Company. This transaction has been accounted for using the purchase method of accounting.

30. Acquisition of a Subsidiary (Continued)

The net assets acquired in the transaction are as follows:

	Acquiree's carrying amount before combination RMB'000	Fair value adjustment RMB'000	Fair value RMB'000
Net assets acquired:			
Interest in an associate	439,017	8,303	447,320
Other receivables	215,874	—	215,874
Bank balances and cash	8	—	8
Other payables	(1,842)	—	(1,842)
	653,057	8,303	661,360
The Group's share of net assets of Weifang Investment at 30th June, 2006			(294,140)
Fair value adjustment attributable to the Group's 45% interest in Weifang Investment			(3,736)
			363,484
Goodwill (note 19)			321,266
Total consideration			684,750
Satisfied by:			
Cash consideration paid			684,750
Net cash outflow arising on acquisition:			
Cash consideration paid			(684,750)
Cash and cash equivalents acquired			8
			(684,742)

The goodwill arising on the acquisition of Weifang Investment is attributable to the anticipated future operating synergies from the combination of TAGC with the Group.

The acquisition of Weifang Investment contributed RMB17,775,000 million to the Group's profit for the period between the date of acquisition and the balance sheet date.

30. Acquisition of a Subsidiary (Continued)

Had the acquisition been completed on 1st January, 2006, the Group's revenue for the year would have no material impact and profit for the year would have been increased to RMB730.1 million. The pro forma information is for illustrative purposes only and is not necessarily an indication of revenue and results of operations of the Group that actually would have been achieved had the acquisition been completed on 1st January, 2006, nor is it intended to be a projection of future results.

31. Capital Commitments

	2006 RMB'000	2005 RMB'000
Capital expenditure in respect of acquisition of property, plant and equipment contracted for but not provided in the financial statements	**57,230**	234,912
Capital expenditure in respect of the acquisition of property, plant and equipment authorised but not contracted for	**249,221**	—

32. Operating Lease Commitments

The Group as lessee

	2006 RMB'000	2005 RMB'000
Minimum lease payments paid under operating leases during the year:		
Plant and machinery	**30,117**	30,117
Premises	**26,595**	20,522
	56,712	50,639

32. Operating Lease Commitments (Continued)

The Group as lessee (Continued)

At the balance sheet date, the Group had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	2006 RMB'000	2005 RMB'000
Within one year	**49,634**	50,355
In the second to fifth year inclusive	**24,235**	73,218
	73,869	123,573

Operating lease payments represent rentals payable by the Group for certain of its plant and machinery and premises. Leases are negotiated for a term ranging from 1 year to 5 years and rent is fixed over the lease term.

33. Pledged of Assets

At 31st December, 2006, bank deposits of approximately RMB459,653,000 (2005: RMB371,670,000) were pledged to banks to secure bills payable issued and bills receivables discounted by the Group.

At 31st December, 2006, bills receivable of approximately RMB34,300,000 (2005: nil) were pledged to banks to secure bills payable issued by the Group.

34. Post Balance Sheet Events

The following significant events took place subsequent to the balance sheet date:

(a) On 23rd January, 2007, the Company issued short term debentures in an aggregate principal amount of RMB900 million in the PRC (the "Debentures"). The Debentures, being zero coupon with a face value of RMB100 each, were priced and issued at a discount at RMB96.31 each with maturing on 25th January 2008. The proceeds from the Debentures will be used as working capital of the Company for its production and operational needs.

35. Connected and Related Parties Disclosure

(a) During the year, the Group had the following significant transactions with related parties and connected persons:

	2006 RMB'000	2005 RMB'000
Connected persons and related parties		
Weichai Factory (Note i):		
Sales of diesel engines and related parts	**275,107**	306,056
Purchases of materials	**111,146**	48,137
General services fee paid	**8,131**	15,588
Utility services fee paid	**90,071**	113,850
Sales and warranty period repair services fee income	**16,057**	21,025
Purchases of property, plant and equipment	**418**	145
Disposal of property, plant and equipment	**39**	71
Warehouse uploading and logistic services fee income	**796**	—
Rental paid for certain premises, machinery and equipment	**42,814**	42,814
Chongqing Weichai Factory (Note ii):		
Sales of diesel engines and related parts	**39,276**	48,673
Purchase of materials	**6,232**	8,121
General services fee paid	**7,172**	7,983
Utility services fee paid	**14,012**	15,322
Processing services fee paid	**63,070**	60,042
Rental paid for certain premises, machinery and equipment	**3,404**	3,404
Connected persons		
Longgong Fujian (Note iii):		
Sales of diesel engines and related parts	**97,355**	81,714
Longgong Shanghai (Note iii):		
Sales of diesel engines and related parts	**429,983**	268,060
Guangxi Liugong Group (Note iv):		
Sales of diesel engines and related parts	**320,075**	266,338
Related parties, other than connected persons		
CHDTGL (prior to 20th March, 2006, see note 22):		
Sales of diesel engines and related parts	**57,764**	1,452,069
Purchases of materials	**3,904**	72,610
Purchases of finished diesel engines	**—**	409,791
TAGC and its subsidiaries:		
Sales of diesel engines and related parts	**547,666**	—

35. Connected and Related Parties Disclosure (Continued)

Notes:

(i) At 31st December, 2006, Weichai Factory was interested in 23.53% in the Company and is the single largest shareholder of the Company. Mr. Tan Xuguang, the Chairman of the Board of Directors and the general manger of Weichai Factory was interested in the transaction.

(ii) Chongqing Weichai Factory is wholly owned by Weichai Factory.

(iii) Longgong Fujian and Longgong Shanghai are wholly owned subsidiaries of China Infrastructure Machinery Holdings Limited ("CIMHL") a listed company in Hong Kong, in which Mr. Li San Yim, a non-executive director and Ms. Ni Yingying, the wife of Mr. Li Sau Yim, both have beneficial interest in CIMHL and the Company.

(iv) Shanghai Longgong is owned as to 39.49% by Mr. Li San Yim, a non-executive director and as to 60.51% by Ms. Ni Yingying, the wife of Mr. Li San Yim, both have significant influence in Fujian Longgong.

(v) Guangxi Liugong is a promoter of the Company and holds 1.36% interest in the Company at 31st December, 2006. Guangxi Liugong together with its affiliates are collectively referred as the "Guangxi Liugong Group".

(b) Compensation of key management personnel

The remuneration of Directors and other members of key management during the year was as follows:

	2006 RMB'000	2005 RMB'000
Short-term benefits	**5,265**	3,636
Post-employment benefits	**24**	238
	5,289	3,874

(c) Details of the trading balance with related parties are set out in notes 23 and 25. These trading balances arose from the transactions set out in 35(a).

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35. Connected and Related Parties Disclosure (Continued)

(d) Details of the non-trade balances with related party are as follows:

(i) *Name of related company*

	2006 RMB'000	2005 RMB'000
Amount due to a related party:		
Weichai Factory	**127,739**	186,865

The amount is unsecured and interest-free.

Note: As at 31st December, 2006, included in the above balance was an amount of approximately RMB127,739,000 (2005: approximately RMB182,719,000) which represented the balance of the consideration payable by the Company for the acquisition of technologies and trademarks from Weichai Factory. The amount is repayable as follows:

	2006 RMB'000	2005 RMB'000
Within one year	**66,229**	59,126
In the second year	**61,510**	62,083
In the third to fifth year inclusive	**—**	61,510
	127,739	182,719
Less: Amount due for settlement within one year (including under current liabilities)	**(66,229)**	(59,126)
	61,510	123,593

The effective interest rate for the amount due to a related party of RMB127,739,000 is approximately 5% per annum.

At 31st December, 2006, the fair value of the amount due to a related part was approximately RMB127,739,000, determined based on the present value of the estimated future cash outflows discounted using the prevailing market rate at the balance sheet.

(ii) Details of a refundable deposit of RMB80,000,000 (2005: RMB80,000,000) payable to CHDTGL at 31st December, 2005 are set out in note 21.

35. Connected and Related Parties Disclosure (Continued)

(e) Transactions/balances with other state-controlled entities in the PRC

The Group operates in an economic environment currently predominated by entities directly or indirectly owned or controlled by the PRC government ("state-controlled entities"). In addition, the Group itself is part of a larger group of companies under Weichai Factory which is controlled by the PRC government. Apart from the transactions with Weichai Factory and fellow subsidiaries and other related parties disclosed in sections (a) to (d) above, the Group also conducts business with other state-controlled entities. The Directors consider those state-controlled entities are independent third parties so far as the Group's business transactions with them are concerned.

In establishing its pricing strategies and approval process for transactions with other state-controlled entities, the Group does not differentiate whether the counter-party is a state-controlled entity or not.

Material transactions/balances with other state-controlled entities are as follows:

	2006 **RMB'000**	2005 RMB'000
Trade sales	**2,093,558**	1,394,513
Trade purchases	**1,074,915**	598,002
Amounts due to other state-controlled entities	**277,649**	121,652
Amounts due from other state-controlled entities	**12,036**	140,659

In addition, the Group has entered into various transactions, including deposits placements, borrowings and other general banking facilities, with certain banks and financial institutions which are state-controlled entities in its ordinary course of business. In view of the nature of those banking transactions, the Directors are of the opinion that separate disclosure would not be meaningful.

Except as disclosed above, the Directors are of the opinion that transactions with other state-controlled entities are not significant to the Group's operations.

Notes to the Consolidated Financial Statements

For the year ended 31st December, 2006

36. Retirement Benefits

Defined contribution plans

The employees of the Group are members of a state-managed retirement benefit scheme operated by the government in the PRC. The Group is required to contribute a fixed percentage of payroll costs to the retirement benefit scheme to fund the benefits. The only obligation of the Group with respect to the retirement benefit scheme is to make the specified contributions.

37. Particulars of Subsidiaries

The following table lists the subsidiaries of the Group as at 31st December, 2006:

Name of subsidiary	Form of business structure	Country of registration/ Principal place of operation	Paid up registered capital	Proportion of registered capital held by the Company directly	Principal activities
			RMB		
濰柴動力(濰坊)備品資源有限公司	Incorporated	The PRC	45,795,918	51%	Trading of spare parts of diesel engine to group companies
濰柴動力(濰坊)油品有限公司	Incorporated	The PRC	5,200,000	52%	Trading of lubricant oil products to group companies
濰柴動力(濰坊)集約配送有限公司	Incorporated	The PRC	10,400,000	52%	Provision of warehouse management services to group companies
濰柴動力(濰坊)投資有限公司	Incorporated	The PRC	1,245,000,000	100%	Investment holding in 28.12% equity interest in TAGC which is principally engaged in the manufacture and sale of heavy duty trucks and vehicle parts
濰柴動力(上海)投資有限公司	Incorporated	The PRC	47,500,000	95%	Inactive
濰柴動力(濰坊)鑄鍛有限公司	Incorporated	The PRC	20,000,000	100%	Inactive

None of the subsidiaries had any debt securities outstanding at the end of the year or at any time during the year.