PMC 上海集优 SHANGHAI PRIME

SHANGHAI PRIME MACHINERY COMPANY LIMITED

(A joint stock limited company incorporated in the People's Republic of China with limited liability)

Annual Report 2007

Content

Corporate Information

Executive Directors
Liu Zhenduo
(Appointed on 26 October 2007)
Zhou Zhiyan
(Resigned on 26 October 2007)
Yan Qi
Hu Kang
Chen Hui
Xia Sicheng
Huang Wennong

Independent Non-Executive Directors
Chan Chun Hong (Thomas)
Zhou Feida
Liu Huangsong

Supervisors
Chen Jiaming
Hu Peiming
Lin Guanhong

Company Secretary
Li Wai Chung
(Certified Public Accountant)

Audit Committee
Chan Chun Hong (Thomas)
Zhou Feida
Liu Huangsong

Remuneration Committee
Zhou Feida
Chan Chun Hong (Thomas)
Liu Huangsong

Authorized Representatives
Hu Kang
Chen Hui

Alternative Authorized Representatives
Chan Chun Hong (Thomas)
Li Wai Chung

Qualified Accountant
Li Wai Chung
(Certified Public Accountant)

International Auditor
Ernst & Young

Legal Advisers
As to Hong Kong, New York U.S. Federal Law
Freshfields Bruckhaus Deringer
As to PRC Law
Jun He Law Offices

Compliance Adviser
Evolution Watterson Securities Limited

H-share Registrar and Transfer Office
Tricor Investor Services Limited
26th Floor, Tesbury Centre,
28 Queen's Road East, Wanchai,
Hong Kong

Investor and Media Relations Consultant
iPR Ogilvy Ltd

Principal Bankers
China Construction Bank
Bank of Communications

Statutory Chinese Name
上海集優機械股份有限公司

Statutory English Name
Shanghai Prime Machinery Company Limited

Registered Address
Room 1501, Jidian Edifice,
600 Heng Feng Road,
Shanghai, China
Postal Code: 200070

Principal Place of Business in Hong Kong
2901, 29th Floor,
Tower One, Lippo Center,
89 Queensway, Hong Kong

Stock Exchange on which H shares are listed:
The Stock Exchange of Hong Kong Limited
Abbreviation of H shares: Shanghai Prime
H share stock code: 2345
Website: www.pmcsh.com
Email: pmcservice@pmcsh.com
Telephone: +86 (21) 6472 9900
Fax: +86 (21) 6472 9889

Financial Summary

RMB(Million)	**2003**	**2004**	**2005**	**2006**	**2007**
Revenue and Profit					
Revenue	626	851	1,425	2,867*	3,272*
Profit before tax	36	92	201	336*	344*
Tax	(1)	(27)	(56)	(98)*	(112)*
Profit for the year	35	65	145	238	232
Attributable to:					
Equity holders of the Company	33	64	135	231	225
Minority interests	2	1	10	7	7
Dividends - Proposed final	-	-	-	58	56
Earnings per share attributable to equity holders of the Company					
-Basic (RMB cents)	4.43	8.52	18.04	18.98	15.65
Assets and Liabilities					
Non-current assets	554	684	845	1,017	1,241
Current assets	526	539	954	2,249	2,048
Current liabilities	553	601	933	776	701
Net current assets/(liabilities)	(27)	(62)	21	1,473	1,347
Total assets less current liabilities	527	622	866	2,490	2,588
Non-current liabilities	317	328	51	61	49
Net assets	210	294	815	2,429	2,539
Equity attributable to equity holders of the Company	177	253	744	2,357	2,527
Minority interests	33	41	71	72	12

* Revenue, profit before tax of 2006 and 2007 include those figures of a discontinued operation, which have been seperately disclosed in note 12 to the financial statements.

Performance Highlights

- Revenue (including both the continuing operations and a discontinued operation) for the year ended 31 December 2007 was RMB3,272 million, representing an increase of 14% over 2006.

- Profit attributable to equity holders of the Company for the year ended 31 December 2007 was RMB225 million (2006: RMB231 million). After the deduction of each year's exceptional income*, profit attributable to the equity holders represented an increase of 13% over the corresponding period last year.

- Basic earnings per share for the year ended 31 December 2007 was RMB15.65 cents. The Board of Directors proposed a final dividend for 2007 of RMB3.88 cents per share.

- Shanghai Prime Machinery Company Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") adopted a strategy in the development of high-end turbine blades that focuses on the research and development of high precision blades. A significant breakthrough was achieved in the self-production of 1,000 MW ultra-super-critical power generation turbine blades in 2007, whose sales for the year was RMB26 million.

- The Group's railway bearing business maintained positive momentum under strong market demand. Sales for the year reached RMB197 million, representing an increase of 37% over 2006.

- Benefiting from its brand name and stable product quality, turnover of cutting tools business achieved further growth. Among the product lines, the sales of threading tools amounted to RMB93 million (2006: RMB66 million), representing an increase of 41% over 2006.

* Please refer to page 6 for details.

Corporate Structure

Shanghai Prime Machinery Company Limited

- **Turbine Blade Business**
  - Wuxi Turbine Blade Company Limited — **100%**
- **Bearing Business**
  - Shanghai Tian An Bearing Company Limited — **99%**
  - Shanghai United Bearings Company Limited — **90%**
  - Shanghai General Bearing Company Limited — **40%**
  - Shanghai Bearing Import & Export Company Limited — **30%**
  - Shanghai Electric Bearings Company Limited — **100%**
- **Cutting Tool Business**
  - Shanghai Tool Works Company Limited — **100%**
- **Fastener Business**
  - Shanghai Biaowu High Tensile Fasteners Company Limited — **100%**
- **Other Business**
  - Shanghai Morgan Carbon Crucible Company Limited — **30%**
  - Shanghai Morganite Electrical Carbon Company Limited — **30%**

Chairman's Statement

Liu Zhenduo Chairman

Dear Shareholders,

On behalf of the Board of Directors (the "Board"), I am pleased to announce the annual results of the Group for the year ended 31 December 2007. The Group's results have been audited by Ernst & Young. I am honored to present to you the accomplishments achieved by the Group last year and to share with you my vision of sustainable development of the Group.

Business Review

The inflation pressure was mounting in 2007. The price surge of steel, which is one of our major raw materials, made an impact on the growth of operating profit of the Group. Under the leadership of the Board of Directors and the management, the five major business segments of the Group, though achieved a relatively slow growth, have basically accomplished targets set for 2007. Among these segments, profit recorded by the fastener business dropped slightly as compared with 2006 under the pressure brought by the appreciation of Renminbi ("RMB") and the reduction of export tax refund rate. However, our performance is more encouraging when focusing on the overall results of the Group. With the support of the dedicated staff, our manufacturing business has demonstrated a steady growth throughout the whole year in 2007. When comparing with the results in 2006 after deducting the exceptional income, our segment results and sales income have both showed an upward trend.

Turnover of the Group (including both the continuing operations and a discontinued operation) for 2007 was RMB3,272 million (2006: RMB2,867 million), representing an increase of 14% over 2006. Profit attributable to the equity holders of the Company was RMB225 million in 2007 (2006: RMB231 million). After the deduction of each year's exceptional income, profit attributable to the equity holders represented an increase of 13% over last year. The exceptional income in 2007 was the net gain on disposal of a subsidiary of RMB14 million. The exceptional income in 2006 was RMB45 million, which represented the net interest income from over-subscription funds and the net gain from debt restructuring. Total assets amounted to RMB3,289 million (2006: RMB3,266 million).

Outlook and Prospects

The government of the People's Republic of China (the "PRC") will further tighten its macro-control in 2008. Through the influence of the tax policy, the government encourages enterprises to use renewable resources and clean energy and put much emphasis on energy conservation and consumption reduction. Demand of industrial machinery products arising from the development of the related industries will give fresh impetus to the machinery manufacturing industry and such factor will encourage enterprises to put more resources to initiate innovation and produce high-value added products to meet market demand.

In addition, Shanghai has given priority to the development of modern service industry and advanced manufacturing industry. Under such strategic development plan, Shanghai will "speed up its pace for structural adjustment of the service industry and establish an industrial structure with service economy enjoying a dominant role" and this development trend will also accelerate the growth momentum of suppliers of industrial parts and components who play a complementary role in the development of the main equipment manufacturing industry. On the other hand, the Group will also encounter new challenges. The government will adopt a tight monetary policy in 2008, under which restriction will be placed on the volume of bank lending. The continual appreciation of RMB will exert pressure on the export trade of the Group. Furthermore, the price-hike of raw materials, energy and other materials should not be overlooked. In particular, the implementation of the new Law of the PRC on employment contracts will increase the production costs of enterprises. Being an international and publicly listed company, the Group shall take seriously into consideration all the macro-control policies adopted by the government and strictly comply with the relevant laws and regulations issued by the government in order to safeguard the interests of the shareholders, customers and staff.

Looking into 2008, by upholding the corporate belief of "diligently serve customers and partners, wholeheartedly strive for better returns to the shareholders and investors" and by following the operating standards of "producing top-quality products and offering excellent services", the Group will try to achieve further growth through the following initiatives:

Speed up the research and development of high technology and high value-added products. In 2008, the Group will continue to increase spending in the research and development of proprietary and innovative products and accelerate the restructuring of product portfolio by cooperating with products research institutions. The Group will concentrate on the development of precise and advanced products with high added-values, study global development trend of similar products in order to fasten the pace of domestic production to replace imported products, particularly on the auxiliary products used in environmental protection projects supported by the government, and on the increase of the share of high technology and high value-added products in the overall production. The Group will also build up its experience and gradually develop its own core technology with a view to enhance its capacity in developing middle-end and high-end products independently.

Enlarge the scale of operation. In 2008, the investment projects funded with the Group's Initial Public Offerings proceeds will begin yielding investment returns. In the meantime, the Group will set off to plan, launch and implement various significant key investment projects, particularly the project of building the manufacturing base for 1,000 MW extra large nuclear power generation turbine blades and technology upgrades for manufacturing

Chairman's Statement

aviation blade forgings, to optimize the economies of scale and overall strength of the Group. In addition, the Group will actively seek additional investment opportunities and conduct mergers and acquisitions as appropriate with a view to improve the Group's development potential and competitive strength as supplier and service provider in the industrial parts and components manufacturing industry.

Explore new model of business development. In 2008, the manufacturing of technologically advanced industrial parts and components will become the fundamental and major operation of the Group. Oriented by modern manufacturers' services such as trading and logistics, the Group will establish a brand new supply chain management services platform with information technology, which enables the Group to provide quality and effective products and services of industrial parts and components. To achieve the target of becoming a leading domestic and international product and service provider of industrial parts and components, the Group will increase the level of efficient use of internal resource by trying to structure the organisation based on the idea of Group operation and exploring the new operating model featuring "end-user service, chain operation, e-commerce and distribution of branded products".

Finally, I would like to take this opportunity to thank all the directors, supervisors, members of the management and the entire staff for their contributions and devotion to the Group's development in 2007. In the coming year, the Group will strive for long-term and sustainable profit growth for all shareholders by facing new challenges and seizing the good investment opportunities in return for their trust and ceaseless support.

Liu Zhenduo
Chairman
Shanghai, PRC
28 March 2008

Management Discussion and Analysis

Performance Overview

2007 was a challenging year for the Group. The Group successfully mitigated the impacts of macroeconomic factors such as price-hike of raw materials, continuous appreciation of RMB and reduction in export tax refund rate. In addition, the long-term stable development of the Group was secured by the implementation of investment projects using fund-raising proceeds, introduction of innovative management and the persistent improvement in technology. With the ceaseless efforts paid by the management and the entire staff, the Group is developing into a product and service supplier of industrial parts and components that excels both domestically and internationally.

For 2007, the Group's revenue (including both the continuing operations and a discontinued operation) was RMB3,272 million (2006: RMB2,867 million), representing an increase of 14% over the last year. Profit attributable to the equity holders of the Company was RMB225 million in 2007 (2006: RMB231 million). After the deduction of each year's exceptional income, profit attributable to the equity holders represented an increase of 13% over last year. The exceptional income in 2007 was the net gain on disposal of a subsidiary of RMB14 million. The exceptional income in 2006 was RMB45 million, which represented the net interest income from over-subscription funds and the net gain from debt restructuring. Basic earnings per share attributable to ordinary equity holders of the Company was RMB15.65 cents (2006: RMB18.98 cents).

As at 31 December 2007, total assets of the Group amounted to RMB3,289 million (2006: RMB3,266 million) while total liabilities amounted to RMB750 million (2006: RMB837 million). Total equity of the Group was RMB2,539 million (2006: RMB2,429 million), of which RMB2,527 million (2006: RMB2,357 million) was attributable to the equity holders of the Company. Net assets attributable to equity holders of the Company per share amounted to RMB1.76 (2006: RMB1.64).

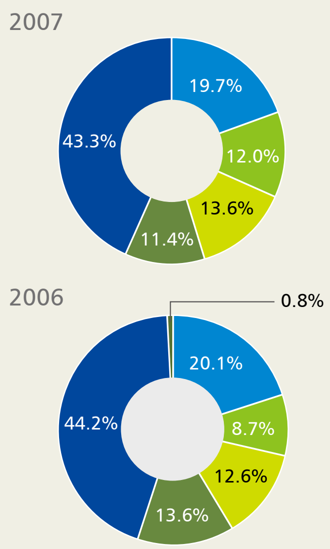
Operation Analysis

Accelerated the implementation of investment projects and streamlined the business structure. In 2007, the Group sped up the implementation of its investment projects. As at the end of 2007, four of its investment projects using its fund-raising proceeds, namely the project of increase in export of high precision turbine blades, phase 1 of project of the technology upgrades for the production and development of numerically-controlled cutting tools, project of technology upgrades for logistic systems and expansion in production capacity as well as the project of technology upgrades for its speed-lifting railway bearings for 80 tons heavy cargo trains, were approaching completion. The Company has completed the acquisition of 40% foreign-owned equity interest in Shanghai United Bearings Company Limited ("United Bearings") and 30% equity interest in Shanghai Morganite Electrical Carbon Company Limited ("Shanghai Morganite"), of the remaining relevant assets of Shanghai Tongqiang Fastener Company Limited ("Tongqiang") and the entire equity interest of Shanghai Electric Bearings Company Limited ("Electric Bearings") as well as made the capital contribution to Electric Bearings. In the meantime, the Company has also completed the sale of 60% equity interest in Shanghai Nanyang Electric Motor Company Limited ("Nanyang Motor") . Through the implementation of these investment projects and acquisition and disposal of equity interests, the Group's production capacity and the profitability have been increased, which provides a sound foundation for its long-term development.

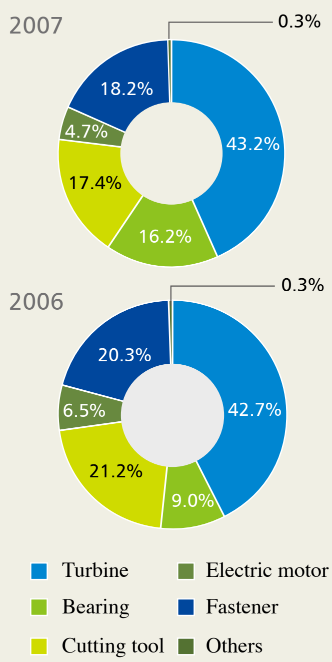
Management Discussion and Analysis

Introduced innovative management and improved control and governance. The Group has strictly complied with the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and operated prudently and soundly in 2007. The Company perfected the cash pool management system and strengthened the centralized control over funds. The Group tightened the the supervision of investment projects and strengthened the remuneration evaluation system by introducing the total value-added (TVA) appraisal method. Last but not least, it has refined its management information system. Through such effective management initiatives, the Company mitigated its operating risks and secured steady growth.

Revenue



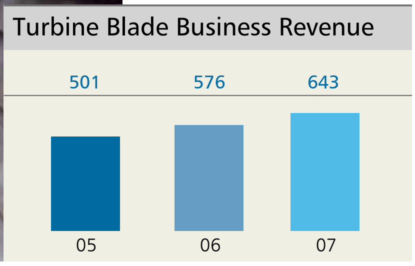
Segment Results



Persisted in upgrading technology and enhanced proprietary development ability. In 2007, the Group increased its investment in research and development and sped up the hiring process of high-end research and development talents. The Group achieved significant breakthrough in key technologies. For example, the turbine blades business has independently developed new technologies such as laser quenching as well as forging and heat treatment techniques for high temperature alloy materials, the cutting tools business has established a joint laboratory and a parameter data bank for the production of cutting tools under a cooperation with Shanghai Jiao Tong University, and the Group has completed several key research projects on aerospace bearings. Through the development and application of the above new products, techniques and technologies, the core competitiveness of the Group has been strengthened.

Set out below are the Revenue and Segment Results of each business segment:

	Revenue		Segment Results	
RMB (Million)	2007	2006	2007	2006
Turbine blade	643	576	147	137
Percentage of total	19.7%	20.1%	43.2%	42.7%
Bearing	394	248	55	29
Percentage of total	12.0%	8.7%	16.2%	9.0%
Cutting tool	446	362	59	68
Percentage of total	13.6%	12.6%	17.4%	21.2%
Electric motor	372	390	16	21
Percentage of total	11.4%	13.6%	4.7%	6.5%
Fastener	1,417	1,268	62	65
Percentage of total	43.3%	44.2%	18.2%	20.3%
Others (Intra-group transactions eliminated)	-	23	1	1
Percentage of total	-	0.8%	0.3%	0.3%
Total	3,272	2,867	340	321



TURBINE BLADE BUSINESS

The Group is a leading specialized provider of turbine blades for power station turbines in the PRC and is primarily engaged in the manufacturing of long turbine blades and precision turbine blades, which require higher level of technical sophistication compared to other turbine blade products. In 2007, the Group was well aware of the continuous expansion of the domestic turbine blade market and therefore adopted an active strategy to strengthen its position in the domestic market and develop high-end turbine blade products. In addition, the Group achieved breakthrough in the development of new products such as MW-capacity large nuclear power generation turbine blades, 1,000 MW ultra-super-critical large last stage steam turbine blades and titanium long turbine blades, which laid the foundation for the Group's expansion into domestic and overseas high precision large turbine blade markets and helped to realise fully domestic production of turbine blades used in 1,000 MW ultra supercritical power generators. In support of the Group's expansion plan, the Group entered into an agreement with the Committee of Wuxi Huishan Economic Development Zone (無錫惠山經濟開發區委員會) to acquire a land in Wuxi Huishan Economic Development Zone at a consideration of RMB65 million to build the plant and accommodate machineries and equipments of Wuxi Turbine Blade Company Limited ("WuXi Turbine Blade"). For 2007, revenue of the turbine blade business amounted to RMB643 million (2006: RMB576 million), representing an increase of 12% over the last year. The segment results amounted to RMB147 million (2006: RMB137 million), representing a year-on-year growth of 7%.

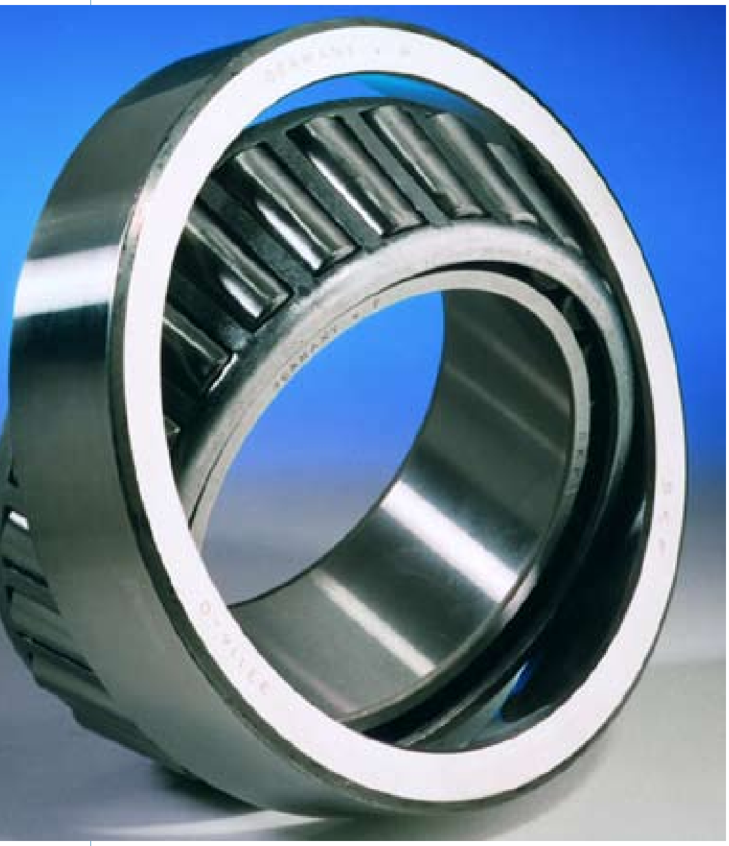
While consolidating our development in the domestic turbine blade market, the Group further expanded into the overseas market and formed five new strategic foreign trade partnerships with General Electric of the U.S., Siemens Power Generation of Germany, etc. In 2007, export sales of turbine blades amounted to RMB97 million, accounting for 15% of the total revenue generated from the turbine blade business.

Management Discussion and Analysis

BEARING BUSINESS

In 2007, except for the railway bearing, the Group focused on the development of high-end products such as precision miniature bearings with a bore diameter of less than 1mm and four-point touch ball miniature bearings. For the year, the revenue of bearing business was RMB394 million (2006: RMB248 million), representing an increase of 59% over the last year. The sales of railway bearings reached RMB197 million, representing an increase of 37% over the last year.

The Group adopted a diversified marketing strategy that is engaging in both the domestic and overseas markets. The export sales of bearings for this year was RMB72 million, accounting for 18% of the total revenue generated from the bearing business.



CUTTING TOOL BUSINESS

Being a leading enterprise with more than 50 years experience in the PRC cutting tool industry, the Group took advantage of the steady development of the tool market in 2007 and further developed our market network by fully utilizing the Company's brand name. The network of our distributors extended from the Yangtze River delta region and the Zhujiang delta region to Bohai Rim and the northeast industrial region. The Group has also laid emphasis on exploring the market of hard numerically-controlled cutting tools that require higher level of technical sophistication. During the year of 2007, the revenue of the cutting tool business was RMB446 million (2006: RMB362 million), representing an increase of 23% over the last year. The segment result was RMB59 million (2006: RMB68 million, including an one-time gain from debt restructuring of RMB22 million), representing an increase of 28% over the last year after deducting the one-time gain from debt restructuring in 2006.

While actively increasing the domestic cutting tools market share, the Group also endeavored to expand its overseas market with a view to increase its brand name presence in the international market. The export sales of cutting tools for 2007 was RMB77 million, accounting for 17% of the total revenue generated from the cutting tool business.

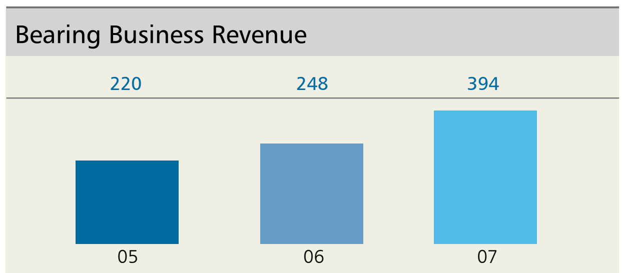
FASTENER BUSINESS

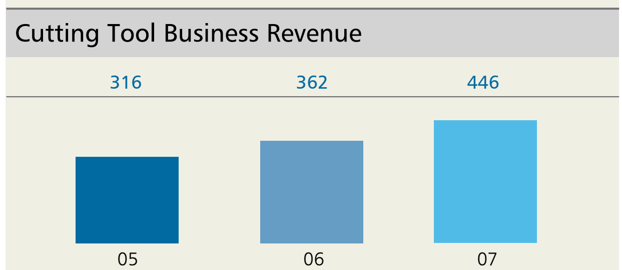
The Group is the largest fastener exporter in the PRC. As the global manufacturing industry is shifting to China, the Group focuses on the export of various types of standard and specialized fasteners. With respect to the rapid appreciation of RMB, decrease of export refund tax rate and the increase of steel and transportation prices, the Group has adopted various measures, including raising selling price in new orders, shortening the lead time of delivery and applying new technologies in its production process, which led to same quality, but lower production costs. The Group is committed to follow the strategies of providing diversified products, quick delivery and best quality as well as being the most cost-effective with a view to improve its liquidity. Since successful implementation of project of technology upgrade for the logistics system and expansion in production capacity, the Group further strengthened the its core competitiveness by establishing an automatic warehouse and improving the storage and logistics center in terms of automation and computerisation. In 2007, the sales was RMB1,417 million (2006: RMB1,268 million), representing an increase of 12% over the last year. The segment result was RMB62 million.

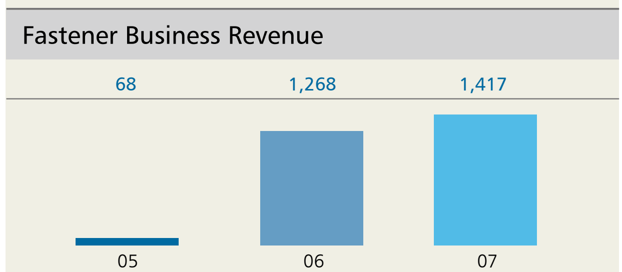
Based on the dispute submitted by European Industrial Fasteners Institute (EIFI), the European Commission undertook an anti-dumping investigation against the steel fastener manufacturing companies from the PRC in November 2007. The Company has actively responded to the investigation. By the date of this annual report, the case is still in process.

ELECTRIC MOTOR BUSINESS

Due to the fact that the price of main raw material, being copper, remained high, competitions within the electric motor industry has become more intensive. It is expected that the price of products and gross profit will decrease in the long run, therefore the Group sold its 60% equity interest in Nanyang Motor.







Management Discussion and Analysis

Review of Financial Position

Share of Profits and Losses of Associates

During the year 2007, the Group's share of profits of associates was RMB16 million (2006: RMB12 million), representing an increase of 33% over the last year.

Finance Costs

Finance costs for the year 2007 were RMB8 million (2006: RMB19 million), representing a decrease of 58% over the last year.

Profit Attributable to Equity Holders of the Company

According to the foregoing information, profit attributable to the equity holders of the Company was RMB225 million in 2007 (2006: RMB231 million). After the deduction of each year's exceptional income, profit attributable to the equity holders represented an increase of 13% over last year. The exceptional income in 2007 was the net gain on disposal of a subsidiary of RMB14 million. The exceptional income in 2006 was RMB45 million, which represented the net interest income from over-subscription funds and the net gain from debt restructuring. Basic earnings per share was RMB15.65 cents (2006: RMB18.98 cents).

Cash Flow

As at 31 December 2007, the Group's cash and bank balances were RMB882 million (2006: RMB1,187 million), of which RMB19 million (2006: RMB660 million) were restricted deposits, representing a decrease of RMB641 million in restricted deposit from the beginning of the year. For 2007, the Group had a net cash inflow from operating activities of RMB180 million (2006: net cash inflow of RMB36 million), a net cash inflow from investing activities of RMB361 million (2006: net cash outflow of RMB1,004 million), and a net cash outflow from financing activities of RMB17 million (2006: net cash inflow of RMB1,198 million).

Assets and Liabilities

As at 31 December 2007, the Group had total assets of RMB3,289 million (2006: RMB3,266 million), representing an increase of RMB23 million or 1% as compared with the beginning of the year, of which total current assets amounted to RMB2,048 million (2006: RMB2,249 million), accounting for 62% of the total assets, representing a decrease of RMB201 million as compared with the beginning of the year. Total non-current assets were RMB1,241 million (2006: RMB1,017 million), accounting for 38% of the total assets and representing an increase of RMB224 million as compared with the beginning of the year.

As at 31 December 2007, the total liabilities of the Group were RMB750 million (2006: RMB837 million), representing a decrease of RMB87 million or 10% as compared with the beginning of the year, of which total current liabilities amounted to RMB701 million (2006:RMB776 million), accounting for 93% of total liabilities and representing a decrease of RMB75 million as compared with the beginning of the year. Total non-current liabilities amounted to RMB49 million (2006: RMB61 million), accounting for 7% of total liabilities and representing a decrease of RMB12 million as compared with the beginning of the year.

As at 31 December 2007, the net current assets of the Group were RMB1,347 million (2006: RMB1,473 million), representing a decrease of RMB126 million or 9% as compared with the beginning of the year whereas current ratio increased from 2.90 to 2.92.

Sources of Funding and Indebtedness

As at 31 December 2007, the Group had an aggregate bank and other borrowings of RMB92 million (2006: RMB107 million), representing a decrease of RMB15 million or 14% as compared with the beginning of the year. Borrowings repayable by the Group within one year were RMB75 million (2006: RMB90 million), representing a decrease of RMB15 million from the beginning of the year, whereas borrowings repayable after one year were RMB17 million (2006: RMB17 million).

As at 31 December 2007, all bank and other borrowings of the Group were interest bearing at fixed rates.

Gearing Ratio

As at 31 December 2007, the gearing ratio of the Group, which represents the ratio of interest-bearing bank and other borrowings to total shareholders' equity, was 4% (2006: 5%).

Pledges of Assets

As at 31 December 2007, bank deposits of RMB19 million (2006: RMB7 million) of the Group were pledged to banks.

Contingent Liabilities

As at 31 December 2007, the Group had total contingent liabilities of RMB2 million (2006: RMB56 million).

Capital Expenditure

The total capital expenditure of the Group for the year was approximately RMB535 million (2006: RMB230 million), which was principally invested in the upgrading of production technologies and equipment, and the expansion of production capacity.

Risk of Foreign Exchange

The Group uses RMB as the reporting currency. General view of the market expects that the measures adopted by the PRC government may cause faster increase in exchange rate in the future. Appreciation of RMB will result in higher prices for exported products, and may result in a negative impact on the Group's export sales but a positive influence on the Group's materials and equipments import.

As at 31 December 2007, the Group's deposits comprised of HK$0.2 million, US$0.8 million and JPY12.6 million. Save as disclosed above, the Group was not exposed to any significant risks related to foreign exchange fluctuations.

Significant Events

On 16 August 2007, the Company entered into an agreement with Shanghai Electric (Group) Corporation ("Shanghai Electric Corporation"), being the controlling shareholder of our Company in respect of the transfer of its 60% equity interest in Nanyang Motor and the gain on disposal was RMB14 million.

The Company and its subsidiary Shanghai Biaowu High Tensile Fasteners Company Limited ("Biaowu Fasteners") are participating in an anti-dumping investigation on Chinese companies manufacturing carbon steel fasteners initiated by the European Commission on 9 November 2007. The Company and Biaowu Fasteners are requesting for Market Economy Treatment ("MET"). Whether the Company and Biaowu Fasteners could obtain the MET will greatly impact the duty that will apply to exports to the European Union of fasteners manufactured by the Company and Biaowu Fasteners. The investigation is under way and it is expected to be completed in February 2009. The on-going anti-dumping investigation is not a litigation. It is an administrative investigation by the European Commission on whether Chinese companies manufacturing carbon steel fastenters, including the Company and Biaowu Fasteners, are dumping their products on the EU market. There is no legal liability arising from the investigation. Save as disclosed above, the Group did not have any other significant disclosable events during the year.

Employees

As at 31 December 2007, the Group had approximately 3,307 employees (2006: 4,182). The Group has implemented all statutory pension schemes required by the PRC government as well as incentive schemes and training programs to stimulate staff and assist them in their self-development.

Biographical Details of Directors, Supervisors and Senior Management

The following table sets forth certain information concerning our Directors, Supervisors and Senior Management.

Name	Age	Position
Liu Zhenduo	60	Executive Director and Chairman
Yan Qi	42	Executive Director and Vice Chairman
Hu Kang	44	Executive Director and Chief Executive Officer
Chen Hui	39	Executive Director and Vice President
Xia Sicheng	44	Executive Director and Vice President
Huang Wennong	59	Executive Director and Vice President
Chan Chun Hong (Thomas)	44	Independent Non-executive Director
Zhou Feida	68	Independent Non-executive Director
Liu Huangsong	39	Independent Non-executive Director
Chen Jiaming	46	Supervisor and Chairman of the supervisory committee
Hu Peiming	50	Supervisor
Lin Guanhong	57	Supervisor
Zhu Weiming	37	Vice President
Wang Pin	34	Chief Financial Officer
Li Wai Chung	30	Qualified Accountant and Company Secretary

Directors

Liu Zhenduo, aged 60, is a senior economist. He was appointed as Executive Director and Chairman of the Company in October 2007. Mr. Liu joined Shanghai Electric Corporation in 1986 and has been Vice President of the Parent Group of the Company since 1997, general manager and director of Shanghai Mechanical & Electrical Industry Company Limited since 2005. Mr. Liu has also been the president of Shanghai Electric Assets Management Company Limited since 2007. Mr. Liu graduated from East China Normal University Postgraduate Class in 2000. He also holds a master degree of Business Administration conferred by Asia International Open University (Macao) in 2003.

Yan Qi, aged 42, is a senior engineer. He was appointed as Executive Director of the Company and Vice Chairman of the Board in September 2005. Mr. Yan was appointed in 1997 as deputy factory director of Wuxi Turbine Blade, one of our key subsidiaries, and was promoted to the position of factory director in 2001. He was president and executive director of Wuxi Turbine Blade since 2005, and was elected as a representative of the Wuxi People's Congress in 2003. Mr. Yan graduated from Beijing Institute of Technology in 1988 with a degree in mechanical engineering and from Fudan University of Shanghai in 2000 with a MBA degree. In 2007, he graduated from Southeast University with a doctorate degree in management.

Hu Kang, aged 44, is a senior economist. He was appointed as Executive Director and President of the Company in September 2005. He joined the Shanghai Electric Corporation in 1982. Since 1996, he has been factory director of Shanghai Zhenhua Bearing Head Works, vice president of Shanghai Bearing (Group) Co., Ltd, president of Shanghai Shanglin Electrics Company, Ltd., all of which are part of the Parent Group, and president of the second management department of Shanghai Electric Assets Management Company Limited, one of our Promoters. Mr. Hu graduated from Shanghai University of Finance & Economics in 1988 with a degree in statistics, and graduated from the Shanghai College of the Chinese

Communist Party in 1998 specializing in management. In 2001, he obtained a MBA degree from Macau University of Science and Technology.

Chen Hui, aged 39, is an engineer and a senior economist. He was appointed as Executive Director and Vice President of the Company in September 2005. He joined the Parent Group of the Company in 1987. From 2002 to 2004, Mr. Chen was one of the factory directors and was responsible for the management of the bearing business division of Shanghai Electric Corporation prior to the Reorganization. Mr. Chen was also president of Electric Bearings, a holding company of our bearing subsidiaries prior to the Reorganization from 2004 to 2005. Mr. Chen graduated from Shanghai University with a degree specailizing in mechanical automation, and graduated from the Central College of the Communist Party in 2001 with a bachelor degree in management, and later obtained a master degree from Macau University of Science and Technology in 2002.

Xia Sicheng, aged 44, was appointed as Executive Director and Vice President of the Company in September 2005. He joined the Parent Group of the Company in 1982. From 2000 to 2003, Mr. Xia was one of the factory directors and was responsible for the management of the cutting tool business division of Shanghai Electric Corporation prior to its reorganization. Since 2003, Mr. Xia has been director and president of Shanghai Tool Works Company Limited, one of our key subsidiaries. Mr. Xia graduated from the Central College of the Communist Party in 2002 with a bachelor's degree in economics and management.

Huang Wennong, aged 59, is a senior economist. He was appointed as Executive Director and Vice President of the Company in September 2005. He graduated from Shanghai Jiao Tong University with a bachelor degree in business management. He joined the Parent Group of the Company in 1968. Since 1991, Mr. Huang has been Vice President of Shanghai Standard Component Corporation, President of Shanghai Shang Biao (Group) Co., Ltd, and President of Shanghai Standard Component Import and Export Company Limited, a subsidiary of the Parent Group, the entire business of which was subsequently transferred to one of our key subsidiaries, Biaowu Fasteners. Mr. Huang graduated from Shanghai Jiao Tong University in 1985 with a bachelor degree in enterprise management.

Chan Chun Hong (Thomas), aged 44, is a qualified accountant and a fellow of The Association of Chartered Certified Accountants. He was appointed as Independent Non-executive Director of the Company in November 2005. Mr. Chan holds directorships in various companies listed in Hong Kong and is currently managing director of Wang On Group Limited and Wai Yuen Tong Medicine Holdings Limited, where he is responsible for the overall corporate management and supervision of the Wang On Group and Wai Yuen Tong Group. Mr. Chan graduated from Hong Kong Polytechnic University with a bachelor degree.

Zhou Feida, aged 68, is an engineer. He was appointed as Independent Non-executive Director of the Company in November 2005. Mr. Zhou was factory director of Shanghai Turbine Works Company Limited from 1985 to 1994, and chief executive officer of Shanghai Electric Corporation from 1994 to 2001. Mr. Zhou graduated from Xi'an Jiao Tong University with a bachelor degree in July 1963 and later with a master degree in 1966, both in mechanical engineering.

Liu Huangsong, aged 39, was appointed as Independent Non-executive Director of the Company in November 2005. Between 1996 and 2001, he held the position of deputy manager of Shanghai Worldbest Group Co., Ltd, assistant to the chief executive officer of China Worldbest Group Co., Ltd, director of Changzhou Worldbest Radici Co., Ltd and counselor of the Shanghai Economic Review. He has been financial consultant of the Pudong New Area Trade Union since 2003. Mr. Liu is currently serving at the Shanghai Academy of Social Sciences and has

Biographical Details of Directors, Supervisors and Senior Management

been independent non-executive director of Shanghai Xinyu Hengdeli Holdings Limited. Mr. Liu graduated from Fudan University in 1989 with a bachelor degree in management, and later obtained a doctorate degree in the School of Economics of Fudan University in 2005.

Supervisors

Chen Jiaming, aged 46, is a senior engineer. He was appointed as Supervisor and Chairman of the supervisory committee of the Company in November 2005. Mr. Chen was deputy head of the heavy machinery department of Shanghai Electric Corporation from 2001 to 2004 and chairman of Shanghai Construction Road and Bridge Mechanical Equipment Co., Ltd, which is a subsidiary of the Parent Group, from 2002 to 2004. Mr. Chen is currently general manager of the first department of Shanghai Electric Assets Management Company Limited, one of our Promoters. Mr. Chen graduated from Tongji University in 1988 specializing in automation.

Hu Peiming, aged 50, was appointed as Supervisor of the Company in November 2005. Ms. Hu was vice president and chairwoman of the employee committee of Shanghai Standard Component Import and Export Company Limited, which is a subsidiary of the Parent Group, from 1988 to 2005. Ms. Hu graduated from the Shanghai College of Electromechanics of the Chinese Communist Party in 1986, specializing in politics and management.

Lin Guanhong, aged 57, was appointed as Supervisor of the company in November 2005. Mr. Lin was a senior officer of the human resources department of Shanghai Electric Machinery (Group) Co., Ltd from 1994 to 2003. He was vice president of Shanghai United Electric Machinery (Group) Co., Ltd from 2003 to 2005 and is currently director and chairman of the supervisory committee of Nanyang Motor. All of these companies are part of the Parent Group. Mr. Lin graduated from Shanghai University of Finance & Economics in 1986 with a degree in industrial economics and Fudan University in 1995 with a degree in management and administration.

Senior Management

Zhu Weiming, aged 37, is an engineer. Mr. Zhu was appointed as Vice President of the Company in August 2007. Mr. Zhu was product designer of the Research Institute of Shanghai Punching & Shearing Machine Works, deputy manager of Shanghai Punching & Shearing Machine Works, deputy general manager of Shanghai Li Da Pressing Machines Company Limited as well as director and deputy general manager of Shanghai Ri Yong-JEA Gate Electric Co., Ltd. between 1993 and 2008. Mr. Zhu graduated from Shanghai Polytechnic University in 1993 with a bachelor degree in machine design and manufacturing. He also obtained the qualification of First Class Chinese Professional Managers in 2005.

Wang Pin, aged 34, is a Certified Public Accountant in the PRC and a member of the Chinese Institute of Certified Public Accountants. He was appointed as Chief Financial Officer of the Company in February 2006. He joined Shanghai Gong Xin Zhong Nan Accounting Firm since 1996 and took the role of lead auditor in auditing annual accounts for our bearing subsidiaries in 2001. Mr. Wang graduated from Shanghai University in 1996 with a bachelor degree in accounting.

Li Wai Chung, aged 30, is a member of Hong Kong Institute of Certified Public Accountants, the Association of Chartered Certified Accountants and the Institute of Chartered Accountants in England and Wales. He was appointed as Qualified Accountant and Company Secretary in April 2006. Prior to joining the Company, Mr. Li worked as auditing manager in Deloitte Touche Tohmatsu Huayong Certified Public Accountants and Deloitte Touche Tohmatsu in Hong Kong. Mr. Li graduated from the University of Hong Kong with a bachelor degree (majoring finance and accounting).

Corporate Governance Report

Corporate Governance Practices

The Board of the Company believes that good corporate governance is fundamental to the success of the Company. The Company has accordingly adopted various measures to emphasize a high quality Board, effective internal control, strict compliance with relevant regulatory requirements and operation transparency.

From 1 January 2007 to 31 December 2007 (the "Period"), the Board believes that the Company was fully compliant with all code provisions of the Code on Corporate Governance Practices (the "CG Code") as set out in Appendix 14 of the Listing Rules.

The Board reviews and monitors the corporate governance practices on a regular manner with the aim of promoting a good standard of corporate governance practices.

Model Code for Securities Transactions by Directors

The Board adopted the Model Code for Securities Transactions by Directors of Listed Issuer (the "Model Code") as set out in Appendix 10 of the Listing Rules as the Group's code of conduct for Directors' securities transactions. All directors and supervisors of the Company confirmed that they complied with the Model Code in their securities transactions throughout the Period covered by this annual report.

The Board

The Board is responsible for formulating the overall development strategy of the Group, monitoring its financial performance and overseeing the management of the business. The Board aims at maximising shareholders' value in the process of discharging its duties and responsibilities. When determining the Group's business objectives and development direction, the Board takes into account the latest economic and market situations. Daily operations and management of the Group are entrusted to the management team. The division of power and responsibilities between the Board and senior management is in strict compliance with the Articles of Association of the Company. Other duties of the Board include deciding on the Group's investment scheme, preparing the Group's profit distribution and loss recovery proposals, formulating the Group's capital operation proposals, and implementing resolutions approved at shareholders' meeting.

On 26 October 2007, Mr. Liu Zhenduo was elected as the director and appointed as the chairman of the Board. As at the date of this annual report, the Board consists of nine directors, including six executive directors and three independent non-executive directors.

Executive Directors
Mr. Liu Zhenduo (Chairman)
Mr. Yan Qi
Mr. Hu Kang
Mr. Chen Hui
Mr. Xia Sicheng
Mr. Huang Wennong

Independent Non-Executive Directors
Mr. Chan Chun Hong (Thomas)
Mr. Zhou Feida
Mr. Liu Huangsong

All independent non-executive directors have confirmed their independence to the Company as required under Rule 3.13 of the Listing Rules. The Company is of the view that all the independent non-executive directors are independent in accordance with the terms of the independence guidelines set out in Rule 3.13 of the Listing Rules.

The Board convened five Board meetings during the Period. The attendance of each director is summarized as follows:

Directors	Number of meetings	Actual attendance
Mr. Liu Zhenduo	2	2
Mr. Yan Qi	5	5
Mr. Hu Kang	5	5
Mr. Chen Hui	5	5
Mr. Xia Sicheng	5	5
Mr. Huang Wennong	5	5
Mr. Chan Chun Hong (Thomas)*	5	5
Mr. Zhou Feida*	5	5
Mr. Liu Huangsong*	5	5

*Independent Non-Executive Directors

Mr. Zhou Zhiyan no longer served as the director and chairman of the Board as of 26 October 2007. During the Period, he attended three Board meetings in total.

Each Board member is offered to submit resolution proposals before the regular Board meeting. The Board meeting notification is sent out to all the directors at least 14 days before the regular meeting, which gives them sufficient time to review the resolution proposals. Draft and final versions of minutes of the Board meetings are sent to all the directors in a timely manner for their comments and records respectively after the meeting is held.

Each Board member has the right to inspect minutes of the Board meetings, to consult the Company Secretary on regulatory and compliance matters and to seek external professional advice when necessary. The Company Secretary continuously advises all directors on continuing obligations under the Listing Rules and other applicable laws and regulations to ensure the Company's compliance with such requirements and to ensure an excellent corporate governance of the Company.

Nomination of Directors

As of the date of this annual report, the Nomination Committee has not been established. All current directors were nominated by the promoters. Before the Nomination Committee is established, the Board is responsible for the nomination of new directors and the re-election of existing directors. All nominations need to be approved by General Meeting of Shareholders.

During the Period, the Board nominated Mr. Liu Zhenduo as the director and his nomination was approved by the Extraordinary General Meeting of Shareholders held on 26 October 2007.

Chairman and Chief Executive Officer

Pursuant to the CG Code provision A2.1, roles of the chairman and chief executive officer should be segregated and should not be performed by the same individual. The division of responsibilities between the chairman and chief executive officer should be clearly established and set out in writing. The Chairman of the Board is responsible for ensuring that the directors perform their duties and discuss all important matters on a timely basis, and for ensuring that the Board operates effectively. The Chairman is also responsible for conducting interview individually with each independent non-executive director to understand his opinion and advice on the operation of the Group and the duties of the Board. At present, Mr. Liu Zhenduo is the chairman of the Board. Mr. Hu Kang is the chief executive officer of the Company, who is fully responsible for the day to day operations of the Group and execution of instructions from the Board. The Company is of the opinion that duties and responsibilities between the Board and the management team have been well separated and there exists no problem of over-centralization of management power on any particular person.

Tenure of Independent Non-Executive Directors

All current independent non-executive directors of the Company were appointed with tenure of three years, and can be re-elected and re-appointed with office tenure extended accordingly.

Remuneration of Directors

With written terms of reference as suggested under the CG Code, the remuneration committee is mainly responsible for determining the policies in relation to the overall compensation policy and structure for directors, supervisors and senior management of the Company. Executive Directors, however, do not participate in determination relating to their own remuneration. Pursuant to the Articles of Association of the Company, the remuneration package must be approved by General Meeting of Shareholders.

The committee is currently consisted of three Independent Non-executive Directors. It is chaired by Mr. Zhou Feida and with Mr. Chan Chun Hong, Thomas and Mr. Liu Huangsong as members.

Directors	Number of meetings	Actual attendance
Mr. Zhou Feida	1	1
Mr. Chan Chun Hong (Thomas)	1	1
Mr. Liu Huangsong	1	1

During the Period, Remuneration Committee reviewed and approved the proposed 2007 remuneration package of Board members and key management personnel of the Company. The remuneration of Directors and senior executives is determined with reference to the performance and profitability of the Group as well as remuneration benchmarks from other domestic and international companies and prevailing market conditions.

Audit Committee

The Board established an audit committee in compliance with the CG Code. The committee is required, amongst other things, to oversee the relationship with the external auditors, to review the Group's reviewed and audited interim and annual financial statements, to monitor compliance with statutory requirements, and to review the scope, extent and effectiveness of the Group's internal control function.

Corporate Governance Report

Audit Committee currently comprises three independent non-executive directors, namely Mr. Chan Chun Hong (Thomas), Mr. Zhou Feida and Mr. Liu Huangsong. The audit committee held four meetings during the Period with 100% attendance.

Directors	Number of meetings	Actual attendance
Mr. Chan Chun Hong (Thomas)	4	4
Mr. Zhou Feida	4	4
Mr. Liu Huangsong	4	4

During the meetings, the Audit Committee approved the audited consolidated financial report of 2006 and unaudited interim condensed consolidated financial statements of 2007 of the Group, discussed with external auditor regarding the legitimacy of the applied accounting principles and practices and reviewed the list of the internal control findings discovered during the engagement.

Auditors' Remuneration

During the Period, remuneration to the auditors of the Company, Ernst & Young and its affiliate, is summarised as follows:

For services provided	Amount paid/payable (*RMB in million*)
Auditing Service	4.5
Non-Auditing Service	0.25

Directors' Responsibilities for Accounts

The directors acknowledge their responsibilities for the preparation of accounts for each financial period which gives a true and fair view of the state of affairs of the Group and of the operating results and cash flows for that period. In preparing these accounts for the year ended 31 December 2007, the directors have selected suitable accounting policies and applied them consistently; have made judgements and estimates that are prudent and reasonable; and have prepared the accounts on a going concern basis. The directors are responsible for keeping proper accounting records with reasonable accuracy at any time.

Auditors' Reporting Responsibilities

The responsibilities of the auditors are set out on page 36 to page 37.

Internal Control and Risk Management

The Board has overall responsibility for the Group's system of internal control and the assessment and management of the risks.

In meeting its responsibility, the Board has set up an internal control department underneath the Audit Committee to help to monitor and improve the internal control policies and procedures put in place for risk identification, aversion and management. The Group's system of internal control including a defined management and organizational structure with operating policies and procedures, limits of responsibility and delegated authority, is designed to safeguard corporate assets, to maintain proper accounting records, to ensure the compliance with relevant laws and regulations or to manage and control various risks of the Group. Rather than to completely eliminate the risk of failure in operations and achievements of the business objectives of the Group, the system is designed to provide reasonable, but not absolute assurance against material misstatement of the operating results, financial information, losses or fraud.

The Board, through the Audit Committee, has conducted an annual review of the effectiveness of the system of the internal control of the Company and its subsidiaries. During the Period, the internal control department completed the follow-up evaluation of the improvements of business process policies and procedures which suggested in the letters to the managements of subsidiaries and standardised internal control process by regulating seven control circles that covers the areas of sales, purchasing, inventory, fixed assets, investment, human resource and financial reporting. All of the work performed by internal audit department is conformed to the guidelines described under the framework of the Committee of Sponsoring Organizations of the Treadway Commission. In addition, an upper-lower interactive structure of the internal control system has been put into place to ensure the effective monitor of the daily operation of the headquarter and subsidiaries. As a result, the Board is aware of the current condition of the internal control of the Company and its subsidiaries and believes that the internal control is effective at the date of this annual report.

The internal control department continues to strengthen the Group's business process level control policies and procedures. Depending on the nature of business and risk exposure of individual business segment, the scope of work performed by the internal control department will expand to strategic plan review, fraud investigation and productivity efficiency review.

Information Disclosure and Investor Relationship

The Company has endeavored to keep the transparency of the Group on a high level and has regularly communicated with investors and shareholders through different channels since the IPO.

Through Company's website (http://www.pmcsh.com), the investors can obtain the latest news regarding Company's development, announcements and press releases.

An investor relationship team has been established to handle the phone inquiry, meeting and factory visit from the investors, it also organised annual investment conferences and road shows abroad. During the Period, the involvement of the senior management allows investors to have a better understanding of Company's strategy and development plans.

In the future, the Company will strive to provide better service for investment industry by enhancing current investor relation activities.

By order of the Board
Liu Zhenduo
Chairman
Shanghai, PRC
28 March 2008

Other Information

Share Capital Structure

	Number of shares	Approximate percentage of total issued share capital (%)
Domestic Shares	678,576,184	47.18
H Shares	759,710,000	52.82
Total	1,438,286,184	100

Disclosure of Interests

Substantial shareholders' and other persons' interests and short positions in shares and underlying shares

As at 31 December 2007, interests and short positions in shares and underlying shares of substantial shareholders (other than the directors, chief executives and supervisors of the Company) who were entitled to exercise or control the exercise of 5% or more of the voting power at any general meeting of the Company required to be recorded in the register required to be maintained pursuant to Section 336 of the Securities and Futures Ordinance ("SFO") are as follows:

Name of Substantial Shareholder	Class of Shares	No. of Shares	Note	Capacity	Nature of Interest	Percentage of total number of Domestic Shares/H Shares in issue (%)	Percentage of total number of Shares in issue (%)
Shanghai Electric Corporation	Domestic	652,328,857		Beneficial owner	Long position	96.13	45.36
	Domestic	26,247,327	(1)	Interest of controlled corporation	Long position	3.87	1.82
		678,576,184				100.00	47.18
State-owned Assets Supervision and Administration Commission of Shanghai Municipal Government	Domestic	678,576,184	(1)	Interest of controlled corporation	Long position	100.00	47.18
Templeton Asset Management Ltd.	H Shares	106,386,000		Investment manager	Long position	14.00	7.40
Government of Singapore Investment Corporation Pte Ltd	H Shares	63,432,000		Investment manager	Long position	8.35	4.41
Atlantis Investment Management Ltd	H Shares	61,000,000		Investment manager	Long position	8.03	4.24
The Hamon Investment Group Pte Limited	H Shares	40,026,000	(2)	Investment manager	Long position	5.27	2.78

Notes:

(1) Shanghai Electric Corporation held interests in 26,247,327 shares of the Company by virtue of its control over the following corporations which held direct interests in the Company:

Name of controlled corporation	Percentage of ownership in controlled corporation (%)	No. of shares
Shanghai Electric Industrial Corporation	100	23,519,451
Shanghai Electric Assets Management Company Limited	100	909,292
Shanghai Electric Group Assets Operation Company Limited	100	909,292
Shanghai General Machinery (Group) Corporation	100	909,292

Shanghai Electric Corporation was wholly owned by State-owned Assets Supervision and Administration Commission of Shanghai Municipal Government and its interests in 678,576,184 shares of the Company were deemed to be the interests of State-owned Assets Supervision and Administration Commission of Shanghai Municipal Government.

(2) The Hamon Investment Group Pte Limited held a long position in 40,026,000 shares of the Company by virtue of its control over the following corporations which held direct interests in the Company:

Name of controlled corporation	Percentage of ownership in controlled corporation (%)	No. of shares
Hamon Asset Management Limited	100	3,922,000
Hamon U.S. Investment Advisors Limited	100	34,398,000
Hamon Investment Management Limited	100	1,706,000

Save as disclosed above, the Company is not aware of any other person (other than the directors, chief executives and supervisors of the Company) having any interests or short positions in the shares and underlying shares of the Company as at 31 December 2007 as recorded in the register required to be kept by the Company pursuant to Section 336 of the SFO.

Directors' and Supervisors' Interests and Short Position in Shares and Underlying Shares

As at 31 December 2007, none of the directors, supervisors or chief executives of the Company or their respective associates held or was deemed to hold interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (as defined in Part XV of the SFO) which were required to be recorded in the register as required to be kept under Section 352 of the SFO.

As at 31 December 2007, none of the directors, supervisors or chief executives of the Company or their respective associates held or was deemed to hold interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (as defined in Part XV of the SFO) which were required to be notified to the Company and The Stock Exchange of Hong Kong Limited ("the Stock Exchange") pursuant to the Model Code set out in Appendix 10 of the Listing Rules, nor have they been granted the right to acquire any interests in shares or debentures of the Company or any of its associated corporations.

Report of the Directors

The directors present the report and the audited financial statements of the Company and the Group for the year ended 31 December 2007.

Principal activities

The principal activities of the Group are the design, manufacturing and sale of turbine blades, bearings, cutting tools, electric motors, fasteners and others, the provision of related technical services, domestic trade, the provision of manpower service, industrial investment, entrepot trade of goods and technical services. Details of the principal activities of the subsidiaries are set out in note 19 to the financial statements. During the year, the Board announced its decision to sell the Group's electric motor business, Shanghai Nanyang Electric Motor Company Limited ("Nangyang Motor").

Results and dividends

The Group's profit for the year ended 31 December 2007 and the state of affairs of the Company and the Group at that date are set out in the financial statements on pages 38 to 116.

The directors proposed the payment of a final dividend of RMB3.88 cents per ordinary share in respect of the year to shareholders on the register of members on 21 May 2008. This recommendation has been incorporated in the financial statements as an allocation of retained profits within the equity section of the balance sheet.

Use of proceeds from the Company's initial public offering

The proceeds from the Company's issues of new shares at the time of its listing on the Hong Kong Stock Exchange in April 2006, after deduction of related issuance expenses, amounted to approximately RMB1.4 billion. The proceeds of RMB724 million have been applied during the years ended 31 December 2006 and 2007 in accordance with the proposed applications set out in the Company's listing prospectus, as follows:

- approximately RMB196 million was used for the turbine blade business for expansion of overseas markets and technology upgrades of high precision turbine blades;

- approximately RMB103 million was used for the cutting tool business for technology upgrades of manufacturing facilities of numerically-controlled carbide and PCD cuttings tools;

- approximately RMB81 million was used for the bearing business for the acquisition of 40% equity interests in United Bearings and the entire equity interest in Electric Bearings, as well as technology upgrades of production facilities;

- approximately RMB182 million was used for the fastener business for upgrades of logistic system and facilities and improvement of productivity;

- approximately RMB2 million was used to reform and upgrade the management and control systems; and

- approximately RMB160 million was applied as additional working capital of the Group.

The remaining net proceeds of RMB658 million as at 31 December 2007 were placed as interest-bearing bank deposits. The Company shall apply the remaining proceeds to the intended uses as set out in the listing prospectus.

Summary of financial information

A summary of the published results and assets, liabilities and minority interests of the Group for the last five financial years, as extracted from the audited financial statements, is set out on page 3 of the annual report. This summary does not form part of the audited financial statements.

Property, plant and equipment

Details of movements in the property, plant and equipment of the Company and the Group during the year are set out in note 15 to the financial statements, respectively.

Share capital

There were no movements in either the Company's authorised or issued share capital during the year, the detail of which are set out in note 35 to the financial statements.

Pre-emptive rights

There are no provisions for pre-emptive rights under the Company's Articles of Association or the laws of The People's Republic of China (the "PRC") which would oblige the Company to offer new shares on a pro rata basis to existing shareholders.

Purchase, redemption or sale of listed securities of the Company

Neither the Company, nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the year.

Reserves

Details of movements in the reserves of the Company and the Group during the year are set out in note 36 to the financial statements and in the consolidated statement of changes in equity, respectively.

Distributable reserves

At 31 December 2007, the Company's reserves available for distribution, calculated in accordance with the relevant regulations, amounted to RMB55,812,000, of which RMB55,806,000 has been proposed as a final dividend for the year. In addition, the Company's share premium account, in the amount of RMB691,217,000, may be distributed in the form of fully paid bonus shares.

Charitable contributions

During the year, the Group made charitable contributions totalling RMB630,000.

Major customers and suppliers

In the year under review, sales to the Group's five largest customers accounted for less than 30% of the total sales for the year. Purchases from the Group's five largest suppliers also accounted for less than 30% of the total purchases for the year.

Directors

The directors of the Company during the year were set out on page 16.

The independent non-executive directors are appointed for a period of three years.

Report of the Directors

The Company has received annual confirmations of independence from Mr. Zhou Feida, Mr. Chan Chun Hong (Thomas) and Mr. Liu Huangsong, and as at the date of this report, the Company still considers them to be independent.

Directors', supervisors' and senior management's biographies

Biographical details of the Directors, supervisors and senior management of the Company are set out on page 16 to 18 of this report.

Directors' service contracts

Mr. Liu Zhenduo, the Director of the Company, has entered into a service contract with the Company on 26 October 2007 while other Directors of the Company have entered into service contracts with the Company on 28 September 2005. According to the terms of the service contracts, each of the executive directors agreed to be appointed as the Company's executive director until 28 September 2008. These contracts are renewable in accordance with the Company's articles of association and the Listing Rules and terminable at the option of the Company and the executive directors by giving three months' notice in writing or according to the terms of the contract prior to the expiry of the contract.

Apart from the foregoing, no director has a service contract with the Company which is not terminable by the Company within one year without payment of compensation, other than statutory compensation.

Directors' remuneration

The directors' fees are determined and resolved by the Remuneration Committee subject to shareholders' approval at general meetings. Other emoluments are determined by the Remuneration Committee of the Company with reference to directors' duties, responsibilities and performance and the results of the Group.

Directors' and supervisors' interests in contracts

No director or supervisor had a material interest, either directly or indirectly, in any contract of significance to the business of the Group to which the Company, its holding company, or any of its subsidiaries or fellow subsidiaries was a party during the year.

Directors' interests and short positions in shares and underlying shares

As at 31 December 2007, none of the directors had registered an interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations that was required to be recorded pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code.

Directors' rights to acquire shares or debentures

At no time during the year were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any director or their respective spouse or minor children, or were any such rights exercised by them; or was the Company, its holding company, or any of its subsidiaries or fellow subsidiaries a party to any arrangement to enable the directors to acquire such rights in any other body corporate.

Contract of significance

The Company has entered into various contracts of significance with its ultimate holding company, Shanghai Electric Corporation, and the subsidiaries of Shanghai Electric Corporation. Further details of the transactions are set out in the section "Connected transactions and continuing connected transactions" below.

Substantial shareholders' and other persons' interests in shares and underlying shares

At 31 December 2007, the following interests of 5% or more of the issued share capital of the Company were recorded in the register of interests required to be kept by the Company pursuant to Section 336 of the SFO:

Long positions:

Name	Capacity and nature of interest	Number of ordinary shares held	Percentage of the Company's issued share capital (%)	Category of ordinary shares
Shanghai Electric Corporation	Directly beneficially owned	678,576,184	47.18	Domestic
Templeton Asset Management Ltd.	Directly beneficially owned	106,386,000	7.40	H

Save as disclosed above, as at 31 December 2007, no person had registered an interest or short position in the shares or underlying shares of the Company that was required to be recorded pursuant to Section 336 of the SFO.

Connected transactions and continuing connected transactions

During the year, the Company and the Group had the following connected and continuing connected transactions, certain details of which are disclosed in compliance with the requirements of Chapter 14A of the Listing Rules.

Connected Transactions

On 13 April 2007, the Company entered into an equity purchase agreement with Shanghai Electric Industrial Corporation ("Shiye"). As Shiye was a promoter upon listing as well as a substantial shareholder of the Company, Shiye and its associates as defined under the Listing Rules are connected persons of the Group under Chapter 14A of the Listing Rules. Pursuant to the equity purchase agreement, the Company agreed to acquire 30% equity interest in Shanghai Morganite from Shiye for a consideration of RMB18.47 million. The acquisition consideration was determined with reference to the audited net asset value of Shanghai Morganite of approximately RMB54.88 million (or approximately RMB16.46 million attributable to the 30% interests to be acquired by the Company) as at 31 December 2006, and with reference to the appraised value of Shanghai Morganite of approximately RMB61.57 million (or approximately RMB18.47 million attributable to the 30% interest to be acquired by the Company) as set out in a valuation report prepared by Orient Appraisal Co., Ltd., an independent certified valuer in the PRC. On 10 May 2007, the Company entered into a Share Transfer Agreement with Shiye, pursuant to which the results of Shanghai Morganite for the period from 31 December 2006 to the date of final issuance of an updated business license of Shanghai Morganite is attributable to Shiye in proportion to its then shareholding, which amounted to a net profit of RMB2.32 million. Based on negotiation, the net payable amount was RMB1.52 million as an adjustment to the purchase consideration. The acquisition has been completed as at 31 December 2007.

On 13 April 2007, Biaowu Fasteners, a wholly-owned subsidiary of the Company, entered into a property purchase agreement with Tongqiang, a subsidiary of Shanghai Electric Corporation, to acquire a property from

Tongqiang for a consideration of RMB97.97 million. As Shanghai Electric Corporation is one of the promoters and the substantial shareholder of the Company, Shanghai Electric Corporation and its associates as defined under the Listing Rules are connected persons of the Group pursuant to chapter 14A of the Listing Rules. The acquisition consideration was determined with reference to a valuation carried out by an independent certified valuer in the PRC. The acquisition has been completed as at 31 December 2007.

On 16 August 2007, the Company entered into a share transfer agreement with Shanghai Electric Corporation to sell 60% equity interest in Nanyang Motor, representing the entire equity interest owned by the Company, for a consideration of RMB122.57 million. The disposal consideration was determined with reference to the appraised net asset value of Nanyang Motor of approximately RMB204.28 million (or approximately RMB122.57 million attributable to the 60% interest to be disposed by the Company) on 31 May 2007, as set out in the valuation report dated 29 June 2007 issued by Orient Appraisal Co., Ltd., a certified valuer in the PRC who is independent of the Group. On 11 November 2007, the Company entered into a supplementary share transfer agreement with Shanghai Electric Corporation, pursuant to which the results of Nanyang Motor for the period from 31 May 2007 to the date of final issuance of an updated business license of Nanyang Motor is attributable to the Company in proportion to its then shareholding, which amounted to a net profit of RMB6.32 million as an adjustment to the sales consideration. The disposal had been completed as at 31 December 2007.

On 30 August 2007, Biaowu Fasteners entered into an agreement with Shanghai Fasteners Import and Export Company Limited, a subsidiary of Shanghai Electric Corporation, to sell 16% equity interest in Tongqiang to Shanghai Fasteners Import and Export Company Limited for a consideration of RMB6.42 million. The consideration for the share transfer was determined with reference to a valuation carried out by an independent certified valuer in the PRC. The disposal has been completed as at 31 December 2007.

On 30 August 2007, the Company entered into an equity purchase agreement with Shanghai Electric Corporation to acquire the entire equity interest in Electric Bearings from Shanghai Electric Corporation for a consideration of RMB32.49 million. The acquisition consideration was determined with reference to a valuation carried out by an independent certified valuer in the PRC. The acquisition has been completed as at 31 December 2007.

Continuing connected transactions

Wuxi Land Lease Agreement

On 31 March 2006, Wuxi Turbine Blade entered into a land lease agreement with Shanghai Electric Corporation. Under the Wuxi land lease agreement, Shanghai Electric Corporation agrees to sub-lease a parcel of land that it leases from the Wuxi government with a total area of approximately 106,121.6 square meters to Wuxi Turbine Blade for industrial use. The term of the sub-lease is 10 years, which is the same as the term of the lease between the Wuxi government and Shanghai Electric Corporation. The annual cap, representing the agreed rental payable due to Shanghai Electric Corporation, is RMB3.7 million per year for the first three years of the agreement and is to be reviewed every three years, taking into account market conditions, and should not be higher than the rent applicable to a third party tenant. The rental payment term is also the same as the lease between the Wuxi government and Shanghai Electric Corporation.

In 2006, Wuxi Turbine Blade obtained an approval from the Wuxi government for a waiver of the rental for three years starting from November 2005 and a 50% reduction in the rental for two years thereafter (the "Waiver"). Shanghai Electric Corporation has agreed on the Waiver.

Accordingly, no rental payment was payable by Wuxi Turbine Blade to Shanghai Electric Corporation for the year ended 31 December 2007. In the financial statements for the year ended 31 December 2007, Wuxi Turbine Blade has recognised rental expense payable to Shanghai Electric Corporation of RMB2.2 million, which is the apportionment of total rental payable evenly throughout the 10-year lease period.

Framework Property Lease Agreement

On 31 March 2006, the Company entered into a framework property lease agreement with Shanghai Electric Corporation, pursuant to which Shanghai Electric Corporation agreed to lease (either by itself or through its subsidiaries, excluding Shanghai Electric Group Company Limited and its subsidiaries (collectively referred to as "Shanghai Electric Company")) certain properties with a total area of approximately 89,115 square meters to the Group. The term of each lease granted under the framework property lease agreement is 20 years. Under the agreement, the Company has the right, at its discretion, to terminate the lease term of any premises at any time prior to its expiry. The rental payable under the framework property lease agreement is to be reviewed every three years, taking into account market conditions, and should not be higher than the rent applicable to a third party tenant.

The proposed annual caps, representing the maximum aggregate rental payable as agreed between the parties for the years of 2006, 2007 and 2008 are RMB25 million, RMB30 million and RMB30 million, respectively. The actual rental payable to Shanghai Electric Corporation for the year ended 31 December 2007 was RMB21.0 million.

Framework Processing Agreement with Shanghai Electric Corporation

On 31 March 2006, the Company entered into a framework processing agreement with Shanghai Electric Corporation, pursuant to which Shanghai Electric Corporation (either by itself or through its subsidiaries, excluding Shanghai Electric Company) agrees to provide to the Group processing services.

Pursuant to the framework processing agreement, Biaowu Fasteners will provide the raw materials for certain fasteners to Shanghai Electric Corporation and its subsidiaries, excluding the Group and Shanghai Electric Company (collectively referred to as the "Parent Group") for processing and receiving finished fasteners products from the Parent Group.

The fees payable by the Group under the framework processing agreement shall be:

- such prices as may be stipulated by the PRC government (if any); and if there are no such stipulated prices,
- prices not exceeding any pricing guidelines or pricing recommendations set by the PRC government (if any); and if there are no such pricing guidelines or recommendations,
- prices not exceeding market price; and if there is no market price for a particular type of service,
- an agreed price consisting of the actual or reasonable cost incurred by the Parent Group in providing that services plus a reasonable profit.

The term of the framework processing agreement is three years, renewable at the option of the Company for another term of three years by giving at least three months' notice prior to its expiry of the initial term. Either party may terminate the framework processing agreement at any time by giving at least three months' notice.

The proposed annual caps, representing the maximum aggregate processing fees payable as agreed between the parties for the years of 2006, 2007 and 2008 are RMB8.5 million, RMB9.3 million and RMB10.1 million, respectively. There were no processing fees payable to the Parent Group incurred for the year ended 31 December 2007.

Framework Sales Agreement and Supplementary Framework Sales Agreement with Shanghai Electric Corporation

The Company entered into a framework sales agreement dated 31 March 2006 with Shanghai Electric Corporation, pursuant to which the Group has agreed to sell, on a non-exclusive basis, products from its bearing and cutting tool businesses, both finished and semi-finished, to the Parent Group.

The prices of the products sold to Shanghai Electric Corporation under the framework sales agreement shall be:

- such prices as may be stipulated by the PRC government (if any); and if there are no such stipulated prices,
- prices not exceeding any pricing guidelines or pricing recommendations set by the PRC government (if any); and if there are no such pricing guidelines or recommendations,
- prices not exceeding market price; and if there is no market price for a particular product,
- an agreed price consisting of the actual or reasonable cost incurred by the Group in supplying the product plus a reasonable profit.

Under the framework sales agreement, the proposed annual caps for the years of 2006, 2007 and 2008 were RMB12.1 million, RMB14.5 million, RMB17.4 million, respectively.

The Company entered into a supplementary framework sales agreement dated 13 April 2007 with Shanghai Electric Corporation, pursuant to which both parties have agreed that the proposed annual caps for the years of 2006, 2007 and 2008 shall be adjusted to RMB12.1 million, RMB41.0 million and RMB50.8 million, respectively.

The term of the framework sales agreement and the supplementary framework sales agreement are three years and two years, respectively, renewable at the option of the Company for another term of three years by giving at least three months' notice prior to its expiry of the initial term. Either party can terminate the framework sales agreement by giving at least three months' notice.

The Group's actual sale to Shanghai Electric Corporation for the year ended 31 December 2007 amounted to RMB28.8 million.

Framework Purchase Agreement with Shanghai Electric Corporation

The Company entered into a framework purchase agreement dated 31 March 2006 with Shanghai Electric Corporation, pursuant to which the Group has agreed to purchase (on a non-exclusive basis) raw materials and component parts from the Parent Group, and the Parent Group has agreed to supply (on a non-exclusive basis) such raw materials and component parts to the Group.

The prices of raw materials and components supplied under the framework purchase agreement shall be:

- such prices as may be stipulated by the PRC government (if any); and if there are no such stipulated prices,
- prices not exceeding any pricing guidelines or pricing recommendations set by the PRC government (if any); and if there are no such pricing guidelines or recommendations,
- prices not exceeding market price; and if there is no market price for a particular product,
- an agreed price consisting of the actual or reasonable cost incurred by the Parent Group in supplying the product plus a reasonable profit.

The term of the framework purchase agreement is three years, renewable at the option of the Company for another term of three years by giving at least three months' notice prior to its expiry of the initial term. Either party may terminate the framework purchase agreement by giving at least three months' notice.

The proposed annual caps, representing the maximum aggregate purchase price as agreed between the parties for the years of 2006, 2007 and 2008 are RMB45.2 million, RMB53.9 million and RMB64.4 million, respectively. The Group's actual purchases from the Parent Group for the year ended 31 December 2007 amounted to RMB4.1 million.

Framework Sales Agreement and Supplementary Framework Sales Agreement with Shanghai Electric Company

The Company entered into a framework sales agreement dated 31 March 2006 with Shanghai Electric Company, pursuant to which the Group has agreed to sell, on a non-exclusive basis, products from its turbine blade and cutting tool businesses, both finished and semi-finished, to Shanghai Electric Company.

Shanghai Electric Company is a subsidiary and therefore an associate of Shanghai Electric Corporation as defined under the Listing Rules. As such, any transaction entered or to be entered into between the Group and Shanghai Electric Company would constitute connected transactions pursuant to Chapter 14A of the Listing Rules.

The prices of the products sold to Shanghai Electric Company under the framework sales agreement shall be:

- such prices as may be stipulated by the PRC government (if any); and if there are no such stipulated prices,
- prices not exceeding any pricing guidelines or pricing recommendations set by the PRC government (if any); and if there are no such pricing guidelines or recommendations,
- prices not exceeding market price; and if there is no market price for a particular product,
- an agreed price consisting of the actual or reasonable cost incurred by the Group in supplying the product plus a reasonable profit.

Under the framework sales agreement, the proposed annual caps for the years of 2006, 2007 and 2008 were RMB230.0 million, RMB282.6 million and RMB345.1 million, respectively.

The Company entered into a supplementary framework sales agreement dated 13 April 2007 with Shanghai Electric Company, pursuant to which both parties have agreed that the proposed annual caps for the years of 2006, 2007 and 2008 shall be adjusted to RMB230.0 million, RMB321.8 million and RMB390.7 million, respectively.

The term of the framework sales agreement and the supplementary framework sales agreement are three years and two years, respectively, renewable at the option of either party for another term of three years by giving at least three months' notice prior to its expiry of its initial term. Either party may terminate the framework sales agreement by giving at least three months' notice.

The Group's actual sales to Shanghai Electric Company for the year ended 31 December 2007 amounted to RMB208.9 million.

The independent non-executive directors of the Company have reviewed the continuing connected transactions set out above and in note 43 to the financial statements and have confirmed that these continuing connected transactions were entered into:

1. in the ordinary and usual course of business of the Group;
2. on normal commercial terms or on terms no less favourable to the Group than terms available to or from independent third parties; and
3. in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

Sufficiency of public float

Based on information that is publicly available to the Company and within the knowledge of the directors, at least 25% of the Company's total issued share capital was held by the public as at the date of this report.

Post balance sheet events

Details of the significant post balance sheet events of the Group are set out in note 46 to the financial statements.

Auditors

Ernst & Young retire and a resolution for their reappointment as auditors of the Company will be proposed at the forthcoming annual general meeting.

By order of the Board
Liu Zhenduo
Chairman
Shanghai, PRC
28 March 2008

Report of the Supervisory Committee

Dear Shareholders,

During the reporting period, the Supervisory Committee of Shanghai Prime Machinery Company Limited held three Supervisory Committee meetings in accordance with relevant provisions of the Company Law of the PRC, Securities Law of the PRC, Articles of Association of the Company and the Listing Rules, and has actively and effectively performed its duties in compliance with the Standing Order of the Supervisory Committee passed in the Annual General Meeting. The Committee has carried out all its duties with diligence and prudence, and has supervised all operating and management activities of the Company in a legal, timely and effective manner, practically protected the interests of our shareholders and the Company.

During the reporting period, the Supervisory Committee reviewed the interim results, financial accounts, financial budgets and profit distribution of the Company, as well as participated in the review of the auditor's report and proposed reasonable advice to Board meetings through attending two general meetings and five Board meetings, conducting on-the-spot inspections and convening meetings of the Supervisory Committee. The business expertise of the Committee members was given full play in performing their duties.

With respect to annual progress of the Company in 2007, the Supervisory Committee has the following views:

- The Supervisory Committee has examined details of the implementation of financial management system and financial reports of the Company. It confirms that the budget report, financial report and interim report are true and reliable and the auditing opinions presented by the auditors engaged by the Company produced objective and fair opinions.

- The Supervisory Committee has supervised the operating activities of the Company. It believes that the Company has established a relatively mature internal control system and an internal control management structure, and has made great efforts to improve and execute the system and structure, which mitigated various operating risks of the Company.

- The Supervisory Committee has examined the use of proceeds of the Company. It confirms that the use of proceeds of the Company is in concert with those disclosed in the listing prospectus of the Company. The projects are substantially completed.

- The Supervisory Committee has supervised the connected transactions of the Company. It believes that the connected transactions between the Company and Shanghai Electric Corporation, its controlling shareholder, and Shanghai Electric Company during the reporting period are fair and impartial without damaging the interests of other shareholders and the Company. In 2007, all continuing connected transactions were conducted for amounts within their respective caps for exemption.

- The Supervisory Committee has supervised duty fulfillment of the directors and management of the Company. It confirms that the directors, chief executive officer and other senior management have exercised every rights granted by shareholders and discharged every duties in strict compliance with the principle of diligence and good faith. The Committee is not aware of any abuse of authority which impairs our shareholders' interests and the legitimate rights of our employees as of the date of this report.

In 2008, all members of the Supervisory Committee will continue to comply with relevant provisions of the Company law of the PRC, Securities Law of the PRC, Articles of Association of the Company and the Listing Rules. With dedication to protect the interests of the Company and its shareholders, the Committee will endeavor to perform its supervising duties for the benefits of all shareholders.

By order of the Supervisory Committee
Chen Jiaming
Chairman of the Supervisory Committee
Shanghai, PRC
28 March 2008

Independent Auditors' Report

To the shareholders of Shanghai Prime Machinery Company Limited

(Incorporated in the People's Republic of China as a joint stock company with limited liability)

We have audited the financial statements of Shanghai Prime Machinery Company Limited set out on pages 38 to 116, which comprise the consolidated and company balance sheets as at 31 December 2007, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the financial statements

The directors of the Company are responsible for the preparation and the true and fair presentation of these financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. Our report is made solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2007 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Ernst & Young
Certified Public Accountants
Hong Kong
28 March 2008

Consolidated Income Statement

Year ended 31 December 2007

	Notes	2007 RMB'000	2006 RMB'000
CONTINUING OPERATIONS			
REVENUE	5	2,900,397	2,476,847
Cost of sales		(2,362,416)	(2,013,716)
Gross Profit		537,981	463,131
Other income and gains	5	69,372	91,844
Selling and distribution costs		(78,615)	(52,097)
Administrative expenses		(140,364)	(149,424)
Other expenses		(70,324)	(31,106)
Finance costs	7	(3,885)	(15,593)
Share of profits and losses of associates		16,486	11,931
PROFIT BEFORE TAX	6	330,651	318,686
Tax	10	(110,829)	(97,899)
PROFIT FOR THE YEAR FROM CONTINUING OPERATIONS		219,822	220,787
DISCONTINUED OPERATION			
Profit for the year from a discontinued operation	12	11,836	17,459
PROFIT FOR THE YEAR		231,658	238,246
Attributable to:			
Equity holders of the Company	14	225,094	231,116
Minority interests		6,564	7,130
		231,658	238,246
DIVIDENDS			
Proposed final	13	55,806	57,531
EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY			
Basic (RMB cents)			
– For profit for the year	14	15.65	18.98
– For profit from continuing operations	14	15.16	18.12

Consolidated Balance Sheet

31 December 2007

	Notes	2007 RMB'000	2006 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment	15	1,026,084	771,232
Prepaid land premiums/land lease payments	16	56,212	45,860
Goodwill	17	8,818	-
Other intangible assets	18	3,362	19,002
Investments in associates	20	96,155	70,402
Available-for-sale investments	21	1,072	6,263
Long-term prepayments		15,636	57,470
Deferred tax assets	22	33,898	47,036
Total non-current assets		1,241,237	1,017,265
CURRENT ASSETS			
Inventories	23	553,571	529,691
Trade receivables	24	337,868	336,487
Bills receivable	25	81,529	71,983
Prepayments, deposits and other receivables	26	113,328	107,788
Loan receivable	27	-	14,139
Held-to-maturity investment	28	80,000	-
Derivative financial instruments	29	-	1,615
Restricted deposits	30	18,833	659,805
Cash and cash equivalents	30	863,303	527,318
Total current assets		2,048,432	2,248,826
CURRENT LIABILITIES			
Trade payables	31	360,879	412,673
Bills payable	32	50,460	11,800
Tax payable		102,488	72,758
Other payables and accruals	33	112,528	188,722
Interest-bearing bank and other borrowings	34	75,000	90,000
Total current liabilities		701,355	775,953
NET CURRENT ASSETS		1,347,077	1,472,873
TOTAL ASSETS LESS CURRENT LIABILITIES		2,588,314	2,490,138

Consolidated Balance Sheet (continued)

31 December 2007

	Notes	2007 RMB'000	2006 RMB'000
TOTAL ASSETS LESS CURRENT LIABILITIES		2,588,314	2,490,138
NON-CURRENT LIABILITIES			
Interest-bearing bank and other borrowings	34	17,000	17,000
Government grants		21,286	24,519
Other long-term payables		3,465	6,309
Deferred tax liabilities	22	7,211	13,422
Total non-current liabilities		48,962	61,250
Net assets		2,539,352	2,428,888
EQUITY			
Equity attributable to equity holders of the Company			
Issued capital	35	1,438,286	1,438,286
Reserves	36	1,033,279	861,030
Proposed final dividends	13	55,806	57,531
		2,527,371	2,356,847
Minority interests		11,981	72,041
Total equity		2,539,352	2,428,888

Director ....Liu Zhenduo........ Director ....Hu Kang........

Consolidated Statement of Changes in Equity

Year ended 31 December 2007

		Attributable to equity holders of the Company								
	Notes	Issued capital RMB'000	Capital reserve RMB'000	Contributed surplus RMB'000	Surplus reserves RMB'000	Retained profits RMB'000	Proposed final dividends RMB'000	Total RMB'000	Minority interests RMB'000	Total equity RMB'000
At 1 January 2006		747,640	17,005	(58,756)	13,116	24,863	-	743,868	70,911	814,779
Profit for the year		-	-	-	-	231,116	-	231,116	7,130	238,246
Total income and expense for the year		-	-	-	-	231,116	-	231,116	7,130	238,246
Issue of shares	35	690,646	691,217	-	-	-	-	1,381,863	-	1,381,863
Appropriation to surplus reserves		-	-	-	29,733	(29,733)	-	-	-	-
Transfer to capital reserve		-	50,627	-	-	(50,627)	-	-	-	-
Dividends from a subsidiary		-	-	-	-	-	-	-	(6,000)	(6,000)
Proposed final 2006 dividends	13	-	-	-	-	(57,531)	57,531	-	-	-
At 31 December 2006 and 1 January 2007		1,438,286	758,849	(58,756)	42,849	118,088	57,531	2,356,847	72,041	2,428,888
Profit for the year		-	-	-	-	225,094	-	225,094	6,564	231,658
Total income and expense for the year		-	-	-	-	225,094	-	225,094	6,564	231,658
Acquisition of subsidiaries	37	-	2,295	-	-	-	-	2,295	5,296	7,591
Capital injection by minority interests		-	-	-	-	-	-	-	3,692	3,692
Appropriation to surplus reserves		-	-	-	25,672	(25,672)	-	-	-	-
Adjustments of surplus reserves		-	-	-	(12,692)	12,692	-	-	-	-
Adjustments of capital reserve		-	(54,552)	-	-	54,552	-	-	-	-
Disposal of a subsidiary	38	-	(3,986)	666	(3,378)	7,364	-	666	(75,530)	(74,864)
Final 2006 dividends declared		-	-	-	-	-	(57,531)	(57,531)	-	(57,531)
Dividends paid to a minority shareholder		-	-	-	-	-	-	-	(82)	(82)
Proposed final 2007 dividends	13	-	-	-	-	(55,806)	55,806	-	-	-
At 31 December 2007		1,438,286	702,606*	(58,090)*	52,451*	336,312*	55,806	2,527,371	11,981	2,539,352

* These reserve accounts comprise the consolidated reserves of RMB1,033,279,000 (2006: RMB861,030,000) in the consolidated balance sheet.

Consolidated Cash Flow Statement

Year ended 31 December 2007

	Notes	2007 RMB'000	2006 RMB'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before tax:			
From continuing operations		330,651	318,686
From a discontinued operation	12	12,606	17,459
Adjustments for:			
Finance costs	7	7,702	18,826
Share of profits and losses of associates		(16,486)	(11,931)
Interest income from over-subscription funds	5	-	(36,772)
Interest income from loan receivable, bank balances and deposits		(29,407)	(34,420)
Dividend income from available-for-sale investments	5	(1,965)	(1,269)
Depreciation	6	86,273	71,669
Recognition of prepaid land premiums/ land lease payments	6	1,457	943
Amortisation of other intangible assets	18	2,771	2,761
Gain on disposal of a subsidiary	5	(13,518)	-
Gain on disposal of available-for-sale investments	5	(1,060)	-
Gain on disposal of financial investments	5	-	(1,715)
Fair value gains, net: derivative financial instruments	5	(4,008)	(1,615)
Foreign exchange differences, net		31,408	29,949
Gain on disposal of items of property, plant and equipment, net		(1,495)	(3,106)
Gain from debt restructuring, net		-	(28,275)
Impairment of property, plant and equipment	6	4	93
Impairment/(reversal of impairment) of receivables		437	(834)
Write-down/(reversal of write-down) of inventories to net realisable value	6	(1,425)	799
		403,945	341,248
Increase in inventories		(157,227)	(78,163)
Increase in trade receivables, bills receivable, prepayments, deposits and other receivables		(128,433)	(205,961)
(Increase)/decrease in long-term prepayments		1,014	(1,381)
Increase in trade payables, bills payable, other payables and accruals		125,618	57,650
Increase/(decrease) in other long-term payables		(2,844)	3,034
Decrease in government grants		(3,233)	(3,232)

Consolidated Cash Flow Statement (continued)

Year ended 31 December 2007

	Notes	2007 RMB'000	2006 RMB'000
Cash generated from operations		238,840	113,195
Taxes paid		(58,382)	(77,473)
Net cash inflow from operating activities		180,458	35,722
CASH FLOWS FROM INVESTING ACTIVITIES			
Interest received		38,525	34,281
Dividend income from available-for-sale investments	5	1,965	1,269
Dividends received from associates		10,721	7,309
Purchases of items of property, plant and equipment		(414,635)	(228,220)
Proceeds from disposal of items of property, plant and equipment		4,577	6,632
Proceeds from derivative financial instruments		5,623	-
Prepaid land premiums/land lease payments		(43,386)	(17,784)
Additions to other intangible assets		(2,902)	(1,170)
Acquisition of subsidiaries	37	(57,015)	-
Proceeds from disposal of available-for-sale investments		6,351	-
Disposal of a subsidiary	38	111,499	-
Acquisition of equity interests in an associate		(18,471)	-
Purchase of financial investments		-	(181,645)
Purchase of held-to-maturity investment		(80,000)	-
Proceeds from disposal of financial investments		-	183,360
(Increase)/decrease in restricted deposits		640,624	(645,464)
(Increase)/decrease in non-restricted deposits with original maturity of over three months when acquired		157,159	(162,299)
Net cash inflow/(outflow) from investing activities		360,635	(1,003,731)
CASH FLOWS FROM FINANCING ACTIVITIES			
Increase in issued capital		-	1,500,480
Share issue expenses		-	(118,617)
New bank and other borrowings		273,000	370,720
Capital injection by minority interests		3,692	-
Interest income from over-subscription funds	5	-	36,772
Repayments of bank and other borrowings		(228,000)	(566,617)
Dividends paid to minority interests		-	(6,000)
Dividends paid		(57,531)	-
Interest paid		(7,702)	(18,826)

Consolidated Cash Flow Statement (continued)

Year ended 31 December 2007

	Notes	2007 RMB'000	2006 RMB'000
Net cash inflow/(outflow) from financing activities		(16,541)	1,197,912
NET INCREASE IN CASH AND CASH EQUIVALENTS		524,552	229,903
Cash and cash equivalents at beginning of year		359,019	159,065
Effect of foreign exchange rate changes, net		(31,408)	(29,949)
CASH AND CASH EQUIVALENTS AT END OF YEAR		852,163	359,019
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balances	30	262,163	260,974
Non-restricted time deposits with original maturity of less than three months when acquired		590,000	98,045
		852,163	359,019

Balance Sheet

31 December 2007

	Notes	2007 RMB'000	2006 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment	15	7,540	5,834
Interests in subsidiaries	19	1,572,453	1,118,074
Investment in a jointly-controlled entity	37(a)	-	16,260
Investments in associates	20	92,828	68,321
Total non-current assets		1,672,821	1,208,489
CURRENT ASSETS			
Inventories	23	2,774	4,832
Trade receivables	24	156,364	147,098
Prepayments, deposits and other receivables	26	285,942	64,951
Loan receivable	27	22,000	28,278
Held-to-maturity investment	28	80,000	-
Derivative financial instruments	29	-	1,615
Restricted deposits	30	-	653,035
Cash and cash equivalents	30	414,844	384,185
Total current assets		961,924	1,283,994
CURRENT LIABILITIES			
Trade payables	31	106,820	109,512
Bills payable	32	-	10,000
Tax payable		6,493	-
Other payables and accruals	33	315,506	210,118
Total current liabilities		428,819	329,630
NET CURRENT ASSETS		533,105	954,364
TOTAL ASSETS LESS CURRENT LIABILITIES		2,205,926	2,162,853
NON-CURRENT LIABILITIES			
Deferred tax liabilities	22	5,515	9,708
Total non-current liabilities		5,515	9,708
Net assets		2,200,411	2,153,145
EQUITY			
Issued capital	35	1,438,286	1,438,286
Reserves	36(b)	706,319	657,328
Proposed final dividends	13	55,806	57,531
Total equity		2,200,411	2,153,145

Director .... Liu Zhenduo .... Director .... Hu Kang ....

Notes to Financial Statements

1. CORPORATE INFORMATION

Shanghai Prime Machinery Company Limited (the "Company") is a joint stock limited liability company incorporated in the People's Republic of China (the "PRC") on 30 September 2005. The registered office of the Company is located at Room 1501, Jidian Edifice, 600 Hengfeng Road, Shanghai, the PRC.

During the year, the Company and its subsidiaries (collectively referred to as the "Group") was principally involved in the design and sale of turbine blades, precision bearings, highly durable fasteners, numerical control machine cutting tools, small-to-medium sized electric motors and others, the provision of related technical services, domestic trade, the provision of manpower service, industrial investment, entrepot trade of goods and technical services. During the year, the board of directors announced its decision to sell the Group's electric motor business, Shanghai Nanyang Electric Motor Company Limited ("Nanyang Motor").

In the opinion of the directors, the holding company and the ultimate holding company of the Company is Shanghai Electric (Group) Corporation ("Shanghai Electric Corporation"), a wholly state-owned enterprise established in the PRC.

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which include all Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for derivative financial instruments, which have been measured at fair value. These financial statements are presented in Renminbi ("RMB") and all values are rounded to the nearest thousand except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Group for the year ended 31 December 2007. Adjustments are made to bring into line any dissimilar accounting policies that may exist. The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The acquisition of subsidiaries during the year has been accounted for using the purchase method of accounting. This method involves allocating the cost of the business combinations to the fair value of the identifiable assets acquired, and liabilities and contingent liabilities assumed at the date of the acquisition. The cost of the acquisition is measured at the aggregate of the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

Minority interests represent the interests of outside shareholders not held by the Group in the results and net assets of the Company's subsidiaries. Acquisitions of minority interests are accounted for using the parent entity extension method whereby the difference between the consideration and the book value of the share of net assets acquired is recognised as goodwill.

2.2 IMPACT OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS

The Group has adopted the following new and revised HKFRSs for the first time for the current year's financial statements. Except for in certain cases, giving rise to new and revised accounting policies and additional disclosures, the adoption of these new and revised standards and interpretations has had no material effect on these financial statements.

HKFRS 7	Financial Instruments: Disclosures
HKAS 1 Amendment	Capital Disclosures
HK(IFRIC)-Int 8	Scope of HKFRS 2
HK(IFRIC)-Int 9	Reassessment of Embedded Derivatives
HK(IFRIC)-Int 10	Interim Financial Reporting and Impairment

The principal effects of adopting these new and revised HKFRSs are as follows:

(a) HKFRS 7 Financial Instruments: Disclosures

This standard requires disclosures that enable users of the financial statements to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments. The new disclosures are included throughout the financial statements. While there has been no effect on the financial position or results of operations of the Group, comparative information has been included/revised where appropriate.

(b) Amendment to HKAS 1 Presentation of Financial Statements – Capital Disclosures

This amendment requires the Group to make disclosures that enable users of the financial statements to evaluate the Group's objectives, policies and processes for managing capital. These new disclosures are shown in note 45 to the financial statements.

(c) HK(IFRIC)-Int 8 Scope of HKFRS 2

This interpretation requires HKFRS 2 to be applied to any arrangement in which the Group cannot identify specifically some or all of the goods or services received, for which equity instruments are granted or liabilities (based on a value of the Group's equity instruments) are incurred by the Group for a consideration, and which appears to be less than the fair value of the equity instruments granted or liabilities incurred. As the Company has not issued any equity instruments to its employees, the interpretation has had no effect on these financial statements.

(d) HK(IFRIC)-Int 9 Reassessment of Embedded Derivatives

This interpretation requires that the date to assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative is the date that the Group first becomes a party to the contract, with reassessment only if there is a change to the contract that significantly modifies the cash flows. As the Group has no embedded derivative requiring separation from the host contract, the interpretation has had no effect on these financial statements.

2.2 IMPACT OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS (continued)

(e) HK(IFRIC)-Int 10 Interim Financial Reporting and Impairment

This interpretation requires that an impairment loss recognised in a previous interim period in respect of goodwill or an investment in either an equity instrument classified as available-for-sale or a financial asset carried at cost is not subsequently reversed. As the Group had no impairment losses previously reversed in respect of such assets, the interpretation has had no impact on the financial position or results of operations of the Group.

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in these financial statements.

HKAS 1 (Revised)	*Presentation of Financial Statements*[1]
HKFRS 8	*Operating Segments*[1]
HKAS 23 (Revised)	*Borrowing Costs*[1]
HK(IFRIC)-Int 11	*HKFRS 2 – Group and Treasury Share Transactions*[2]
HK(IFRIC)-Int 12	*Service Concession Arrangements*[4]
HK(IFRIC)-Int 13	*Customer Loyalty Programmes*[3]
HK(IFRIC)-Int 14	*HKAS 19 – The Limit on a Defined Benefit Assets, Minimum Funding Requirements and their Interaction*[4]

[1] Effective for annual periods beginning on or after 1 January 2009
[2] Effective for annual periods beginning on or after 1 March 2007
[3] Effective for annual periods beginning on or after 1 July 2008
[4] Effective for annual periods beginning on or after 1 January 2008

The revised HKAS 1 *Presentation of Financial Statements* becomes effective for financial years beginning on or after 1 January 2009. The Standard separates owner and non-owner changes in equity. The statement of changes in equity will include only details of transactions with owners, with all non-owner changes in equity presented as a single line. In addition, the Standard introduces the statement of comprehensive income: it presents all items of income and expense recognised in profit or loss, together with all other items of recognised income and expenses, either in one single statement, or in two linked statements. The Group is still evaluating whether it will have one or two statements.

HKFRS 8, which will replace HKAS 14 *Segment Reporting*, specifies how an entity should report information about its operating segments, based on information about the components of the entity that is available to the chief operating decision maker for the purposes of allocating resources to the segments and assessing their performance. The standard also requires the disclosure of information about the products and services

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS (continued)

provided by the segments, the geographical areas in which the Group operates, and revenue from the Group's major customers. The Group expects to adopt HKFRS 8 from 1 January 2009.

HKAS 23 has been revised to require capitalisation of borrowing costs when such costs are directly attributable to the acquisition, construction or production of a qualifying asset. As the Group's current policy for borrowing costs aligns with the requirements of the revised standard, the revised standard is unlikely to have any financial impact on the Group.

HK(IFRIC)-Int 11 requires arrangements whereby an employee is granted rights to the Group's equity instruments, to be accounted for as an equity-settled scheme, even if the Group acquires the instruments from another party, or the shareholders provide the equity instruments needed. HK(IFRIC)-Int 11 also addresses the accounting for share-based payment transactions involving two or more entities within the Group. As the Group currently has no such transactions, the interpretation is unlikely to have any financial impact on the Group.

HK(IFRIC)-Int 12 requires an operator under public-to-private service concession arrangements to recognise the consideration received or receivable in exchange for the construction services as a financial asset and/or an intangible asset, based on the terms of the contractual arrangements. HK(IFRIC)-Int 12 also addresses how an operator shall apply existing HKFRSs to account for the obligations and the rights arising from service concession arrangements by which a government or a public sector entity grants a contract for the construction of infrastructure used to provide public services and/or for the supply of public services. As the Group currently has no such arrangements, the interpretation is unlikely to have any financial impact on the Group.

HK(IFRIC)-Int 13 requires that loyalty award credits granted to customers as part of a sales transaction are accounted for as a separate component of the sales transaction. The consideration received in the sales transaction is allocated between the loyalty award credits and the other components of the sale. The amount allocated to the loyalty award credits is determined by reference to their fair value and is deferred until the awards are redeemed or the liability is otherwise extinguished.

HK(IFRIC)-Int 14 addresses how to assess the limit under HKAS 19 *Employee Benefits*, on the amount of a refund or a reduction in future contributions in relation to a defined benefit scheme that can be recognised as an asset, in particular, when a minimum funding requirement exists.

As the Group currently has no customer loyalty award credits or defined benefit scheme, HK(IFRIC)-Int 13 and HK(IFRIC)-Int 14 are not applicable to the Group and therefore are unlikely to have any financial impact on the Group.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

A subsidiary is an entity whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's interests in subsidiaries are stated at cost less any impairment losses.

Joint ventures

A joint venture is an entity set up by contractual arrangement, whereby the Group and other parties undertake an economic activity. The joint venture operates as a separate entity in which the Group and the other parties have an interest.

The joint venture agreement between the venturers stipulates the capital contributions of the joint venture parties, the duration of the joint venture entity and the basis on which the assets are to be realised upon its dissolution. The profits and losses from the joint venture's operations and any distributions of surplus assets are shared by the venturers, either in proportion to their respective capital contributions, or in accordance with the terms of the joint venture agreement.

A joint venture company is treated as:

(a) a subsidiary, if the Group has unilateral control, directly or indirectly, over the joint venture;

(b) a jointly-controlled entity, if the Group does not have unilateral control, but has joint control, directly or indirectly, over the joint venture;

(c) an associate, if the Group does not have unilateral or joint control, but holds, directly or indirectly, generally not less than 20% of the joint venture's registered capital and is in a position to exercise significant influence over the joint venture; or

(d) an equity investment accounted for in accordance with HKAS 39, if the Group holds, directly or indirectly, less than 20% of the joint venture's registered capital and has neither joint control of, nor is in a position to exercise significant influence over, the joint venture.

Jointly-controlled entities

A jointly-controlled entity is a joint venture that is subject to joint control, resulting in none of the participating parties having unilateral control over the economic activity of the jointly-controlled entity.

The Group's investment in its jointly-controlled entity is accounted for by proportionate consolidation, which involves recognising its share of the jointly-controlled entity's assets, liabilities, income and expenses with similar items in the consolidated financial statements on a line-by-line basis. Unrealised gains and losses resulting from transactions between the Group and its jointly-controlled entities are eliminated to the extent of the Group's interest in the jointly-controlled entities, except where unrealised losses provide evidence of

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Jointly-controlled entities (continued)

an impairment of the asset transferred. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

The results of the jointly-controlled entity are included in the Company's income statement to the extent of dividends received and receivable. The Company's investment in its jointly-controlled entity is treated as a non-current asset and is stated at cost less any impairment losses.

Associates

An associate is an entity, not being a subsidiary or a jointly-controlled entity, in which the Group has a long-term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence.

The Group's investments in associates are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses.The Group's share of the post-acquisition results and reserves of associates is included in the consolidated income statement and consolidated reserves, respectively. Unrealised gains and losses resulting from transactions between the Group and its associates are eliminated to the extent of the Group's interests in the associates, except where unrealised losses provide evidence of an impairment of the asset transferred. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

The results of associates are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in associates are treated as non-current assets and are stated at cost less any impairment losses.

Goodwill

Goodwill arising on the acquisition of subsidiaries, associates and jointly-controlled entities represents the excess of the cost of the business combination over the Group's interest in the net fair value of the acquirees' identifiable assets acquired, and liabilities and contingent liabilities assumed as at the date of acquisition.

Goodwill arising on acquisition is recognised in the consolidated balance sheet as an asset, initially measured at cost and subsequently at cost less any accumulated impairment losses. In the case of associates, goodwill is included in the carrying amount thereof, rather than as a separately identified asset on the consolidated balance sheet.

The carrying amount of goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. The Group performs its annual impairment test of goodwill as at 31 December. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Goodwill (continued)

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised. An impairment loss recognised for goodwill is not reversed in a subsequent period.

Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Excess over the cost of business combinations

Any excess of the Group's interests in the net fair value of the acquirees' identifiable assets, liabilities and contingent liabilities over the cost of the acquisition of subsidiaries, after reassessment, is recognised immediately in the income statement.

Impairment of non-financial assets other than goodwill

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories, deferred tax assets, financial assets and goodwill), the asset's recoverable amount is estimated. An asset's recoverable amount is the higher of the asset's or cash-generating unit's value in use and its fair value less costs to sell, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to the income statement in the period in which it arises.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, but not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation) had no impairment loss been recognised for the asset in prior years. A reversal of such impairment loss is credited to the income statement in the period in which it arises.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Related parties

A party is considered to be related to the Group if:

(a) the party, directly, or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with the Group; (ii) has an interest in the Group that gives it significant influence over the Group; or (iii) has joint control over the Group;

(b) the party is an associate;

(c) the party is a jointly-controlled entity;

(d) the party is a member of the key management personnel of the Group or its parent;

(e) the party is a close member of the family of any individual referred to in (a) or (d); or

(f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e).

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. When an item of property, plant and equipment is classified as held for sale or when it is part of a disposal group classified as held for sale, it is not depreciated and is accounted for in accordance with HKFRS 5. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment, and where the cost of the item can be measured reliably, the expenditure is capitalised as an additional cost of that asset or as a replacement.

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful life. The principal annual rates used for this purpose are as follows:

Leasehold buildings	2% to 5%
Machinery and equipment	5% to19%
Motor vehicles	8% to 19%
Office and other equipment	10% to 30%
Leasehold improvements	10% to 20%

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, plant and equipment and depreciation (continued)

Included in machinery and equipment is a spire-pressure machine (10KT-clutch mode) which is depreciated on the unit-of-production method to write off its cost to the residual value over its estimated working hours capacity.

Where parts of an item of property, plant and equipment have different useful lives, the cost of that item is allocated on a reasonable basis among the parts and each part is depreciated separately.

Residual values, useful lives and the depreciation methods are reviewed, and adjusted if appropriate, at each balance sheet date.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in the income statement in the year the asset is derecognised is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress represents property, plant and equipment under construction, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment or investment properties when completed and ready for use.

Intangible assets (other than goodwill)

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each balance sheet date.

Patents and licences

Purchased patents and licences are stated at cost less any impairment losses and are amortised on the straight-line basis over their estimated useful lives of 5 to 10 years.

Research and development costs

All research costs are charged to the income statement as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development. Product development expenditure which does not meet these criteria is expensed when incurred.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Intangible assets (other than goodwill) (continued)

Research and development costs (continued)

Deferred development costs are stated at cost less any impairment losses and are amortised using the straight-line basis over the commercial lives of the underlying products, commencing from the date when the products are put into commercial production.

Leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in non-current assets, and rentals receivable under the operating leases are credited to the income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under the operating leases net of any incentives received from the lessor are charged to the income statement on the straight-line basis over the lease terms.

Prepaid land premiums/land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms. The lease terms of prepaid land premiums range from 20 to 50 years.

Investments and other financial assets

Financial assets in the scope of HKAS 39 are classified as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments and available-for-sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

The Group assesses whether a contract contains an embedded derivative when the Group first becomes a party to it and assesses whether an embedded derivative is required to be separated from the host contract when the analysis shows that the economic characteristics and risks of the embedded derivative are not closely related to those of the host contract. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required under the contract.

The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at the balance sheet date.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments and other financial assets (continued)

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading. Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on these financial assets are recognised in the income statement. The net fair value gains or loss recognised in the income statement does not include any dividends or interest earned on these financial assets, which are recognised in accordance with the policies set out for "Revenue recognition" below.

Where a contract contains one or more embedded derivatives, the entire hybrid contract may be designated as a financial asset at fair value through profit or loss, except where the embedded derivative does not significantly modify the cash flows or it is clear that separation of the embedded derivative is prohibited.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in active market. Such assets are subsequently carried at amortised cost using the effective interest method less any allowance for impairment. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Held-to-maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Group has the positive intention and ability to hold to maturity. Held-to-maturity investments are subsequently measured at amortised cost less any allowance for impairment. Amortised cost is computed as the amount initially recognised minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initially recognised amount and the maturity amount. Gains and losses are recognised in the income statement when the investments are derecognised or impaired, as well as through the amortisation process.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets in listed and unlisted equity securities that are designated as available-for-sale or are not classified in any of the other three categories. After initial recognition, available-for-sale financial assets are measured at fair value, with gains or losses recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the income statement. Interest and dividends earned are reported as interest income and dividend income, respectively and are recognised in the income statement as "Other income" in accordance with policies set out for "Revenue recognition" below. Losses arising from the impairment of such investments are recognised in the income statements as "Impairment losses on available-for-sale financial assets" and are transferred from the available-for-sale investment revaluation reserve.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments and other financial assets (continued)

Available-for-sale financial assets (continued)

When the fair value of unlisted equity securities cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such securities are stated at cost less any impairment losses.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business at the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; a discounted cash flow analysis; and other valuation models.

Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced either directly or through the use of an allowance account. The amount of the impairment loss is recognised in the income statement. Loans and receivables together with any associated allowance are written off when there is no realistic prospect of future recovery.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. Any subsequent reversal of an impairment loss is recognised in the income statement, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

In relation to trade and other receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency or significant difficulties of the debtor and significant changes in the technological, market economic or legal environment that have an adverse effect on the debtor) that the Group will not be able to collect all of the amounts due under the original terms of an invoice. The carrying amount of the receivables is reduced through the use of an allowance account. Impaired debts are derecognised when they are assessed as uncollectible.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments and other financial assets (continued)

Assets carried at cost

If there is objective evidence that an impairment loss on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on these assets are not reversed.

Available-for-sale financial assets

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the income statement, is transferred from equity to the income statement. A provision for impairment is made for available-for-sale equity investments when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires judgement. In addition, the Group evaluates other factors, such as the share price volatility. Impairment losses on equity instruments classified as available-for-sale are not reversed through the income statement.

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Group retains the rights to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Group's continuing involvement is the amount of the transferred asset that the Group may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial liabilities at amortised cost (including interest-bearing loans and borrowings)

Financial liabilities including trade and other payables, an amount due to the ultimate holding company and interest-bearing loans and borrowings are initially stated at fair value less directly attributable transaction costs and are subsequently measured at amortised cost, using the effective interest method unless the effect of discounting would be immaterial, in which case they are stated at cost. The related interest expense is recognised within "finance costs" in the income statement.

Gains and losses are recognised in the income statement when the liabilities are derecognised as well as through the amortisation process.

Financial guarantee contracts

Financial guarantee contracts in the scope of HKAS 39 are accounted for as financial liabilities. A financial guarantee contract is recognised initially at its fair value less transaction costs that are directly attributable to the acquisition or issue of the financial guarantee contract, except when such contract is recognised at fair value through profit or loss. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount determined in accordance with HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets*; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with HKAS 18 *Revenue*.

Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference between the respective carrying amounts is recognised in the income statement.

Derivative financial instruments

The Group uses derivative financial instruments such as forward currency contracts to hedge its risks associated with foreign currency fluctuations. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

Any gains or losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are taken directly to the income statement.

The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Contracts for services

Contract revenue on the rendering of services comprises the agreed contract amount. Costs of rendering services comprise labour and other costs of personnel directly engaged in providing the services and attributable overheads.

Revenue from the rendering of services is recognised based on the percentage of completion of the transaction, provided that the revenue, the costs incurred and the estimated costs to completion can be measured reliably. The percentage of completion is established by reference to the costs incurred to date as compared to the total costs to be incurred under the transaction. Where the outcome of a contract cannot be measured reliably, revenue is recognised only to the extent that the expenses incurred are eligible to be recovered.

Provision is made for foreseeable losses as soon as they are anticipated by management.

Where contract costs incurred to date plus recognised profits less recognised losses exceed progress billings, the surplus is treated as an amount due from contract customers.

Where progress billings exceed contract costs incurred to date plus recognised profits less recognised losses, the surplus is treated as an amount due to contract customers.

Cash and cash equivalents

For the purpose of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments that are readily convertible into known amounts of cash are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the balance sheet, cash and cash equivalents comprise cash on hand and at banks, including term deposits, which are not restricted as to use.

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Provisions (continued)

When the effect of discounting is material, the amount recognised for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the income statement.

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the income statement, or in equity if it relates to items that are recognised in the same or a different period directly in equity.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except:

- where the deferred tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with interests in subsidiaries, investment in jointly-controlled entity and associates, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised, except:

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with interests in subsidiaries, investments in jointly-controlled entity and associates, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income tax (continued)

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 profit will be available to allow all or part of the deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, the fair value is credited to a deferred income account and is released to the income statement over the expected useful life of the relevant asset by equal annual instalments.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;

(b) from the rendering of services, on the percentage of completion basis, as further explained in the accounting policy for “Contracts for services” above ;

(c) rental income, on a time proportion basis over the lease terms;

(d) interest income, on an accrual basis using the effective interest method by applying the rate that discounts the estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset; and

(e) dividend income, when the shareholders’ right to receive payment has been established.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Retirement benefits

The Group, jointly-controlled entity and associates participate in a government-regulated defined contribution pension scheme, under which the Group, jointly-controlled entity and associates pay contributions to a government-regulated pension scheme at a fixed percentage of wages and salaries of the existing full-time employees in the PRC and have no further legal or constructive obligations to pay additional contributions. The contributions are charged as an expense to the income statement as incurred. Details of the government-regulated pension scheme are set out in note 6(i) below.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e. assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised.

Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained profits within the equity section of the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends have been approved by the shareholders and declared, they are recognised as a liability.

Foreign currencies

The financial records of the Group, jointly-controlled entity and associates are maintained and these financial statements are presented in RMB, which is the functional and presentation currency of the Company and its subsidiaries, jointly-controlled entity and associates.

Foreign currency transactions are initially recorded using the functional currency rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to the income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

3. SIGNIFICANT ACCOUNTING ESTIMATES

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the reporting date. However, uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amounts of the assets or liabilities affected in the future.

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.

(i) Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating units and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at 31 December 2007 was RMB8,818,000 (2006: Nil). More details are given in note 17.

(ii) Impairment of non-financial assets (other than goodwill)

The Group assesses whether there are any indicators of impairment for all non-financial assets at each reporting date. Non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable. When value in use calculations are undertaken, management must estimate the expected future cash flows from the asset or cash-generating unit and choose a suitable discount rate in order to calculate the present value of those cash flows.

(iii) Impairment of trade receivables

Impairment of trade receivables is made based on assessment of the recoverability of trade receivables and other receivables. The identification of impairment of trade receivables requires management's judgement and estimates. Where the actual outcome or expectation in future is different from the original estimate, such differences will impact the carrying value of the receivables and impairment loss/reversal of impairment in the period in which such estimate has been changed.

4. SEGMENT INFORMATION

Segment information is presented by way of two segment formats: (i) on a primary segment reporting basis, by business segment; and (ii) on a secondary segment reporting basis, by geographical segment.

The Group's operating businesses are structured and managed separately according to the nature of their operations and the products and services they provide. Each of the Group's business segments represents a strategic business unit that offers products and services which are subject to risks and returns that are different from those of the other business segments.

Summary details of the business segments are as follows:

(i) the bearing segment is engaged in the production and sale of bearings;

(ii) the turbine blade segment is engaged in the production and sale of turbine blades;

(iii) the cutting tool segment is engaged in the production and sale of cutting tools;

(iv) the fastener segment is engaged in the production and sale of fasteners;

(v) the electric motor segment is engaged in the production and sale of electric motors; and

(vi) "others" refers to investment in an associate, which is engaged in the production and sale of carbolic products, and trading activities carried out by the Company.

In determining the Group's geographical segments, revenues are attributed to the segments based on the location of the customers. No further geographical segments based on the location of the assets are presented as the Group's operations and assets are solely located in the PRC.

Inter-segment sales and transfers are transacted with reference to the selling prices used for sales made to third parties at the then prevailing market prices.

4. SEGMENT INFORMATION (continued)

Business segments

The following tables present revenue, profit and certain asset, liability and expenditure information on the Group's business segments for the years ended 31 December 2007 and 2006:

	Continuing operations							Discontinued operation	
Year ended 31 December 2007	Bearing RMB'000	Turbine blade RMB'000	Cutting tool RMB'000	Fastener RMB'000	Others RMB'000	Elimination RMB'000	Total RMB'000	Electric motor RMB'000	Consolidated RMB'000
Segment revenue:									
Sales to external customers	394,471	643,353	445,749	1,416,797	27	-	2,900,397	372,210	3,272,607
Inter-segment sales	-	-	-	-	58,005	(58,005)	-	-	-
Other revenue	10,842	17,666	10,060	13,388	-	-	51,956	4,174	56,130
Total	405,313	661,019	455,809	1,430,185	58,032	(58,005)	2,952,353	376,384	3,328,737
Segment results	55,068	147,093	58,592	62,308	313	-	323,374	16,296	339,670
Interest and dividend income and unallocated gains							17,416	127	17,543
Corporate and other unallocated expenses							(22,740)	-	(22,740)
Finance costs							(3,885)	(3,817)	(7,702)
Share of profits and losses of associates	9,255	-	225	-	7,006	-	16,486	-	16,486
Profit before tax							330,651	12,606	343,257
Tax							(110,829)	(770)	(111,599)
Profit for the year							219,822	11,836	231,658
Assets and liabilities									
Segment assets	929,310	903,748	469,564	704,231	438,911	(689,870)	2,755,894	-	2,755,894
Investments in associates	51,837	-	6,103	-	38,215	-	96,155	-	96,155
Corporate and other unallocated assets							437,620	-	437,620
Total assets							3,289,669	-	3,289,669
Segment liabilities	229,342	254,817	109,381	419,234	333,718	(689,870)	656,622	-	656,622
Corporate and other unallocated liabilities							93,695	-	93,695
Total liabilities							750,317	-	750,317
Other segment information:									
Depreciation and amortisation	9,230	35,282	16,570	14,181	1,430	-	76,693	13,808	90,501
Capital expenditure	66,515	186,553	103,327	162,746	3,190	-	522,331	12,877	535,208
Impairment losses recognised in the income statement	4	-	-	-	-	-	-	-	4
Other non-cash expenses	25	(913)	577	(636)	-	-	(947)	842	(105)

4. SEGMENT INFORMATION (continued)

Business segments (continued)

Year ended 31 December 2006	Continuing operations Bearing RMB'000	Turbine blade RMB'000	Cutting tool RMB'000	Fastener RMB'000	Others RMB'000	Elimination RMB'000	Total RMB'000	Discontinued operation Electric motor RMB'000	Consolidated RMB'000
Segment revenue:									
Sales to external customers	248,364	575,454	362,151	1,268,051	22,827	-	2,476,847	390,424	2,867,271
Inter-segment sales	-	-	-	-	23,988	(23,988)	-	-	-
Other revenue	1,513	13,502	27,075	3,186	-	-	45,276	8,868	54,144
Total	249,877	588,956	389,226	1,271,237	46,815	(23,988)	2,522,123	399,292	2,921,415
Segment results	29,364	137,463	67,476	65,396	907	-	300,606	20,524	321,130
Interest and dividend income and unallocated gains							46,568	168	46,736
Corporate and other unallocated expenses							(24,826)	-	(24,826)
Finance costs							(15,593)	(3,233)	(18,826)
Share of profits and losses of associates	8,569	-	(1,710)	-	5,072	-	11,931	-	11,931
Profit before tax							318,686	17,459	336,145
Tax							(97,899)	-	(97,899)
Profit for the year							220,787	17,459	238,246
Assets and liabilities									
Segment assets	288,496	650,788	436,113	496,946	143,940	(290,939)	1,725,344	446,941	2,172,285
Investments in associates	46,759	-	5,889	-	17,754	-	70,402	-	70,402
Corporate and other unallocated assets							1,023,404	-	1,023,404
Total assets							2,819,150	446,941	3,266,091
Segment liabilities	125,945	109,995	115,799	253,909	218,927	(290,939)	533,636	193,537	727,173
Corporate and other unallocated liabilities							35,030	75,000	110,030
Total liabilities							568,666	268,537	837,203
Other segment information:									
Depreciation and amortisation	5,726	28,437	15,401	11,752	276	-	61,592	13,781	75,373
Capital expenditure	20,420	132,451	8,936	23,498	5,837	-	191,142	38,393	229,535
Impairment losses recognised in the income statement	93	-	-	-	-	-	93	-	93
Other non-cash expenses	2,049	1,781	(6,208)	483	-	-	(1,895)	1,860	(35)

4. SEGMENT INFORMATION (continued)

Business segments (continued)

The Company and Shanghai Biaowu High Tensile Fasteners Company Limited ("Biaowu Fasteners"), a wholly-owned subsidiary of the Company, are participating in an anti-dumping investigation on Chinese companies manufacturing carbon steel fasteners initiated by the European Commission on 9 November 2007. The Company and Biaowu Fasteners are requesting for Market Economy Treatment ("MET"). Whether the Company and Biaowu Fasteners could obtain the MET will greatly impact the duty that will apply to exports to the European Union of fasteners manufactured by the Company and Biaowu Fasteners. The investigation is under way and is expected to be completed in February 2009. The on-going anti-dumping investigation is not litigation. It is an administrative investigation by the European Commission into whether Chinese companies manufacturing carbon steel fasteners, including the Company and Biaowu Fasteners, are dumping their products on the European Union market. There is no legal liability arising from the investigation.

Geographical segments

The following table presents revenue information on the Group's geographical segments for the years ended 31 December 2007 and 2006:

	2007			2006		
	PRC	Outside PRC	Total	PRC	Outside PRC	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Sales to external customers	1,756,103	1,516,504	3,272,607	1,518,588	1,348,683	2,867,271
Attributable to a discontinued operation	(372,210)	-	(372,210)	(390,424)	-	(390,424)
Revenue from continuing operations	1,383,893	1,516,504	2,900,397	1,128,164	1,348,683	2,476,847

5. REVENUE, OTHER INCOME AND GAINS

Revenue, which is also the Group's turnover, represents the net invoiced value of goods sold, after allowances for returns and trade discounts, and the value of services rendered during the year, net of sales taxes and surcharges.

An analysis of revenue, other income and gains is as follows:

	Notes	2007 RMB'000	2006 RMB'000
Revenue			
Sale of goods		2,885,751	2,465,604
Rendering of services		14,646	11,243
Attributable to continuing operations reported in the consolidated income statement		2,900,397	2,476,847
Revenue attributable to a discontinued operation	12	372,210	390,424
		3,272,607	2,867,271

5. REVENUE, OTHER INCOME AND GAINS (continued)

	Notes	2007 RMB'000	2006 RMB'000
Other income			
Dividend income from available-for-sale investments		1,965	1,269
Interest income from over-subscription funds		-	36,772
Interest income from loan receivable, bank balances and deposits		29,279	34,252
Gross rental income		1,914	2,058
Profit on sales of raw materials, spare parts and semi-finished goods		20,194	8,820
Government grants *		19,584	4,257
Compensation income		348	1,675
Others		4,395	4,712
		77,679	93,815
Gains			
Gain on disposal of items of property, plant and equipment, net		1,495	2,805
Gain on disposal of a subsidiary	38	13,518	-
Gain on disposal of available-for-sale investments		1,060	-
Gain from debt restructuring		-	21,843
Fair value gains, net: derivative financial instruments		4,008	1,615
Gain on disposal of financial investments		-	1,715
Foreign exchange differences, net		(31,407)	(29,949)
Gain on write-off of long-aged payables		3,019	-
		(8,307)	(1,971)
Attributable to continuing operations reported in the consolidated income statement		69,372	91,844
Other income and gains attributable to a discontinued operation	12	4,301	9,036
		73,673	100,880

* Various government grants have been received during the year ended 31 December 2007. There are no unfulfilled conditions or contingencies relating to these grants.

6. PROFIT BEFORE TAX

The Group's profit before tax is arrived at after charging/(crediting): #

	2007 RMB'000	2006 RMB'000
Cost of inventories sold	2,662,881	2,334,079
Cost of services provided	14,396	11,077
Depreciation	86,273	71,669
Recognition of prepaid land premiums/land lease payments	1,457	943
Amortisation of patents and licences *	2,045	2,218

6. PROFIT BEFORE TAX (continued)

	2007 RMB'000	2006 RMB'000
Amortisation of other intangible assets *	726	543
Write-down/(reversal of write-down) of inventories to net realisable value	(1,425)	799
Research and development costs: *		
Current year expenditure	48,079	16,937
Minimum lease payments under operating leases:		
Land and buildings	22,425	17,014
Plant and machinery	3,006	1,981
Vehicles	2,144	2,377
Auditors' remuneration:		
Audit services	4,623	4,869
Non-audit services	494	1,370
Employee benefits expenses (including directors' and supervisors' remuneration – note 8):		
Wages and salaries	226,872	205,590
Defined contribution pension scheme (note i)	33,620	26,722
Medical benefits (note iii)	10,655	7,968
Housing fund (note iv)	9,878	8,440
Cash housing subsidies costs	443	41
	281,468	248,761
Foreign exchange differences, net **	44,849	37,860
Impairment/(reversal of impairment) of receivables *	437	(834)
Impairment of property, plant and equipment *	4	93
Loss from debt restructuring	-	106

* These items are included in "Other expenses" on the face of the consolidated income statement of the Group.

** The net foreign exchange losses consist of an amount of RMB31,407,000 (2006: RMB29,949,000) included as "Other income and gains" (note 5) and an amount of RMB13,442,000 (2006: RMB7,911,000) included as "Other expenses".

\# The disclosures presented in this note include those amounts charged/credited in respect of the discontinued operation.

Notes:

(i) Defined contribution pension scheme

All of the Group's full-time employees in the PRC are covered by a government-regulated pension scheme and are entitled to an annual pension determined by their basic salaries upon their retirement. The PRC government is responsible for the pension liabilities to these retired employees. The Group is required to make annual contributions to the government-regulated pension scheme at 22% of the employees' basic salaries subject to a cap. The related pension costs are expensed as incurred.

6. PROFIT BEFORE TAX (continued)

Note: (continued)

(ii) Early retirement benefits

The Group implemented an early retirement plan for certain employees in addition to the benefits under the government regulated defined contribution pension scheme described above. The benefits of the early retirement plan are calculated based on factors including the remaining number of years of services from date of early retirement to normal retirement date and the salary amount on the date of early retirement of the employees.

Wuxi Turbine Blade Company Limited ("Wuxi Turbine Blade") and Shanghai Electric Corporation, the ultimate holding company, have agreed that the costs of early retirement benefits for those employees who early retired before 1 September 2005 will be borne by Shanghai Electric Corporation from 1 September 2005 onwards. Beginning from that date the related costs paid by Wuxi Turbine Blade to these employees will be fully reimbursed by Shanghai Electric Corporation. The total costs of early retirement benefits so borne by Shanghai Electric Corporation since 1 September 2005 were approximately RMB14 million, of which RMB3,810,000 (2006: RMB3,357,000) was related to the year ended 31 December 2007. There was no employee early retired under the plan subsequent to 1 September 2005.

(iii) Medical benefits

The Group contributes on a monthly basis to defined contribution medical benefit plans administrated by the PRC government. The PRC government undertakes to assume the medical benefit obligations of all existing and retired employees under these plans. Contributions to these plans by the Group are expensed as incurred. The Group has no further obligations for medical benefits for their qualified employees under these plans.

(iv) Housing fund

The Group contributes on a monthly basis to defined contribution housing fund plans administrated by the PRC government. Contributions to these plans by the Group are expensed as incurred.

7. FINANCE COSTS

	2007 RMB'000	2006 RMB'000
Interest on bank and other loans wholly repayable within five years	7,702	18,826
Attributable to a discontinued operation (note 12)	3,817	3,233
Attributable to continuing operations reported in the consolidated income statement	3,885	15,593
	7,702	18,826

8. DIRECTORS' AND SUPERVISORS' REMUNERATION

Directors' and supervisors' remuneration for the year, disclosed pursuant to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and Section 161 of the Hong Kong Companies Ordinance, is as follows:

	Directors		Supervisors	
	2007 RMB'000	2006 RMB'000	2007 RMB'000	2006 RMB'000
Fees	587	457	-	-
Other emoluments:				
Salaries, housing benefits, other allowances and benefits in kind	1,390	687	304	360
Performance related bonuses	811	1,217	45	130
Pension scheme contributions	104	83	38	34
Total	2,892	2,444	387	524

(a) Independent non-executive directors

The fees paid to independent non-executive directors during the year were as follows:

	2007 RMB'000	2006 RMB'000
Chan Chun Hong, Thomas	237	183
Zhou Feida	175	137
Liu Huangsong	175	137
	587	457

There were no other emoluments payable to the independent non-executive directors during the year.

(b) Executive directors and supervisors

	Salaries, housing benefits, other allowances and benefits in kind RMB'000	Performance related bonuses RMB'000	Pension scheme contributions RMB'000	Total RMB'000
2007				
Executive directors:				
Liu Zhenduo	-	-	-	-
Zhou Zhiyan	-	-	-	-
Yan Qi	303	219	28	550
Hu Kang	348	128	19	495
Chen Hui	258	83	19	360
Xia Sicheng	214	167	19	400
Huang Wennong	267	214	19	500
	1,390	811	104	2,305

8. DIRECTORS' AND SUPERVISORS' REMUNERATION (continued)

(b) Executive directors and supervisors (continued):

	Salaries, housing benefits, other allowances and benefits in kind RMB'000	Performance related bonuses RMB'000	Pension scheme contributions RMB'000	Total RMB'000
Supervisors:				
Chen Jiaming	-	-	-	-
Hu Peiming	141	45	19	205
Lin Guanhong	163	-	19	182
	304	45	38	387
	1,694	856	142	2,692
2006				
Executive directors:				
Zhou Zhiyan	-	-	-	-
Yan Qi	220	269	15	504
Hu Kang	125	308	17	450
Chen Hui	118	171	17	306
Xia Sicheng	85	220	17	322
Huang Wennong	139	249	17	405
	687	1,217	83	1,987
Supervisors:				
Chen Jiaming	-	-	-	-
Hu Peiming	68	130	17	215
Lin Guanhong	292	-	17	309
	360	130	34	524
	1,047	1,347	117	2,511

There was no arrangement under which a director or supervisor waived or agreed to waive any remuneration during the year.

9. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included two (2006: two) directors or supervisors, details of whose remuneration are set out in note 8 above. Details of the remuneration of the remaining three (2006: three) non-director and non-supervisor, highest paid employees for the year are as follows:

	2007 RMB'000	2006 RMB'000
Salaries, housing benefits, other allowances and benefits in kind	2,556	1,462
Pension scheme contributions	99	48
	2,655	1,510

The remuneration of each of the three non-director and non-supervisor, highest paid employees does not exceed RMB1,000,000.

10. TAX

Except for the following companies, the Group is subject to the statutory corporate income tax rate of 33% for the year under the income tax rules and regulations of the PRC:

- Shanghai United Bearings Company Limited ("United Bearings") is subject to a corporate income tax rate of 27% up to 28 February 2007 as it is located in a coastal economic and technological development area and special economic region with foreign investment in the production business in the old city area. From 1 March 2007 to 31 December 2007, United Bearings ceases to be a foreign investment enterprise and its applicable tax rate is 33%; and

- Nanyang Motor is subject to a corporate income tax rate of 27% as it was established in the Nan Xiang Industrial Zone, Jia Ding District, Shanghai.

No provision for Hong Kong profits tax has been made as the Group did not have any assessable profits arising in Hong Kong for the year.

	2007 RMB'000	2006 RMB'000
Group:		
Current – the PRC		
Charge for the year	104,455	89,307
Overprovision in prior years	(1,327)	(1,607)
Deferred (note 22) *	8,471	10,199
Total tax charge for the year	111,599	97,899
Attributable to a discontinued operation (note 12)	770	-
Attributable to continuing operations reported in the consolidated income statement	110,829	97,899
	111,599	97,899

10. TAX (continued)

* During the 5th Session of the 10th National People's Congress, which was concluded on 16 March 2007, the PRC Corporate Income Tax Law ("the New Corporate Income Tax Law") was approved and became effective on 1 January 2008. The New Corporate Income Tax Law introduces a wide range of changes which include, but are not limited to, the unification of the income tax rate for domestic-invested and foreign-invested enterprises at 25%. This change in the income tax rate will directly change the Group's effective tax rate prospectively from 2008. According to HKAS 12, deferred tax assets and deferred tax liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled. As a result, the change in the corporate income tax rate has resulted in an increase in deferred tax charge of RMB7,490,000 of the Group for the year.

A reconciliation of the tax expense applicable to profit before tax using the statutory rate of 33% to the tax expense at the effective tax rate is as follows:

	2007 RMB'000	2006 RMB'000
Profit before tax (including profit from a discontinued operation)	343,257	336,145
Tax at the statutory tax rate of 33%	113,275	110,928
Lower tax rate for specific provinces/districts or concessions	(2,454)	(4,849)
Effect of tax rate change:		
On opening deferred tax	8,062	-
On deferred tax movement during the year	(572)	-
Adjustments in respect of current tax of previous periods	(1,327)	(1,607)
Profits and losses attributable to associates	(3,839)	(2,818)
Income not subject to tax	(542)	(325)
Expenses not deductible for tax	5,620	1,659
Effect of tax incentive	(6,624)	(5,089)
Total income tax charge for the year	111,599	97,899
Represented by:		
Tax charge attributable to a discontinued operation (note 12)	770	-
Tax charge attributable to continuing operations reported in the consolidated income statement	110,829	97,899
	111,599	97,899
The Group's effective income tax rate	32.5%	29.1%

The share of tax attributable to associates amounting to RMB3,128,000 (2006: RMB2,897,000) is included in "Share of profits and losses of associates" on the face of the consolidated income statement.

11. PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

The consolidated profit attributable to equity holders of the Company for the year ended 31 December 2007 includes a profit of RMB104,797,000 (2006: RMB24,335,000) which has been dealt with in the financial statements of the Company (note 36(b)).

12. DISCONTINUED OPERATION

On 30 November 2007, the Company disposed its entire 60% equity interest in Nanyang Motor. Nanyang Motor engages in the production and sale of electric motors and accessories, and is a separate business segment that is part of the Group's operations. The Group has ceased its electric motors business because of the expected changes in the market conditions.

The results of Nanyang Motor are presented below:

	For 11 months ended 30 November 2007 RMB'000	For 12 months ended 31 December 2006 RMB'000
Revenue	372,210	390,424
Other income and gains	4,301	9,036
Total revenue	376,511	399,460
Expenses	(360,088)	(378,768)
Finance costs	(3,817)	(3,233)
Profit before tax from the discontinued operation	12,606	17,459
Tax	(770)	-
Profit for the year from the discontinued operation	11,836	17,459

The net cash flows incurred by Nanyang Motor are as follows:

	For 11 months ended 30 November 2007 RMB'000	For 12 months ended 31 December 2006 RMB'000
Operating activities	(19,305)	8,037
Investing activities	(11,392)	(39,709)
Financing activities	22,569	36,767
Net cash inflow/(outflow)	(8,128)	5,095
Earnings per share:		
Basic (RMB cents), from the discontinued operation	0.49	0.86

The calculations of basic earnings per share from the discontinued operation are based on:

	For 11 months ended 30 November 2007	For 12 months ended 31 December 2006
Profit attributable to equity holders of the Company from the discontinued operation (RMB'000)	7,102	10,475
Weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculation (Number of shares)	1,438,286,184	1,217,559,141

13. DIVIDENDS

	2007 RMB'000	2006 RMB'000
Proposed final – RMB3.88 cents (2006: RMB4 cents) per ordinary share	55,806	57,531

The proposed final dividends for the year is subject to the approval of the Company's shareholders at the forthcoming annual general meeting.

14. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY

The calculation of basic earnings per share amounts is based on the profit for the year attributable to ordinary equity holders of the Company, and the weighted average number of ordinary shares in issue during the year.

No diluted earnings per share amounts have been presented for the years ended 31 December 2007 and 2006 as no diluting events existed during these years.

The calculation of basic earnings per share is based on:

	2007 RMB'000	2006 RMB'000
Earnings		
Profit attributable to ordinary equity holders of the Company		
From continuing operations	217,992	220,641
From a discontinued operation	7,102	10,475
	225,094	231,116

	Number of shares	
	2007	2006
Shares		
Weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculation	1,438,286,184	1,217,559,141

15. PROPERTY, PLANT AND EQUIPMENT

Group

	Notes	Leasehold buildings RMB'000	Machinery and equipment RMB'000	Motor vehicles RMB'000	Office and other equipment RMB'000	Construction in progress RMB'000	Leasehold improvements RMB'000	Total RMB'000
31 December 2007								
Cost:								
At 1 January 2007		169,565	906,546	27,317	18,979	107,119	3,896	1,233,422
Additions		51,490	9,764	1,064	2,564	382,235	3,648	450,765
Acquisition of subsidiaries	37	1,140	37,331	4,055	746	15,414	567	59,253
Disposals		(25)	(16,430)	(3,022)	(111)	(908)	-	(20,496)
Disposal of a subsidiary	38	(96,274)	(63,751)	(4,739)	(2,975)	(9,233)	-	(176,972)
Transfers		488	282,157	1,109	1,392	(293,265)	8,119	-
At 31 December 2007		126,384	1,155,617	25,784	20,595	201,362	16,230	1,545,972
Accumulated depreciation and impairment:								
At 1 January 2007		38,498	401,140	12,006	8,015	294	2,237	462,190
Depreciation		6,818	69,575	4,192	3,932	-	1,756	86,273
Impairment recognised		-	-	4	-	-	-	4
Acquisition of subsidiaries	37	513	16,772	2,682	562	295	274	21,098
Disposals		(24)	(14,275)	(2,857)	(95)	(163)	-	(17,414)
Disposal of a subsidiary	38	(10,883)	(17,725)	(2,242)	(1,413)	-	-	(32,263)
At 31 December 2007		34,922	455,487	13,785	11,001	426	4,267	519,888
Net book value:								
At 31 December 2007		91,462	700,130	11,999	9,594	200,936	11,963	1,026,084
31 December 2006								
Cost:								
At 1 January 2006		159,540	817,987	22,127	20,063	40,948	3,896	1,064,561
Additions		568	6,235	5,630	2,376	195,772	-	210,581
Disposals		(766)	(30,679)	(3,896)	(4,331)	(2,048)	-	(41,720)
Transfers		10,223	113,003	3,456	871	(127,553)	-	-
At 31 December 2006		169,565	906,546	27,317	18,979	107,119	3,896	1,233,422
Accumulated depreciation and impairment:								
At 1 January 2006		32,649	372,324	10,556	9,499	1,589	1,491	428,108
Depreciation		6,122	59,472	3,081	2,248	-	746	71,669
Impairment recognised		-	-	3	-	90	-	93
Disposals		(273)	(30,656)	(1,634)	(3,732)	(1,385)	-	(37,680)
At 31 December 2006		38,498	401,140	12,006	8,015	294	2,237	462,190
Net book value:								
At 31 December 2006		131,067	505,406	15,311	10,964	106,825	1,659	771,232

15. PROPERTY, PLANT AND EQUIPMENT (continued)

Company

	Motor vehicles RMB'000	Office and other equipment RMB'000	Construction in progress RMB'000	Leasehold improvements RMB'000	Total RMB'000
31 December 2007					
Cost:					
At 1 January 2007	1,285	2,897	1,961	-	6,143
Additions	322	1,602	966	359	3,249
Disposals	-	(14)	-	-	(14)
Transfers	-	960	(2,927)	1,967	-
At 31 December 2007	1,607	5,445	-	2,326	9,378
Accumulated depreciation and impairment:					
At 1 January 2007	28	281	-	-	309
Depreciation provided	257	928	-	349	1,534
Disposals	-	(5)	-	-	(5)
At 31 December 2007	285	1,204	-	349	1,838
Net book value:					
At 31 December 2007	1,322	4,241	-	1,977	7,540
31 December 2006					
Cost:					
At 1 January 2006	-	-	-	-	-
Additions	1,285	2,897	1,961	-	6,143
At 31 December 2006	1,285	2,897	1,961	-	6,143
Accumulated depreciation and impairment:					
At 1 January 2006	-	-	-	-	-
Depreciation provided	28	281	-	-	309
At 31 December 2006	28	281	-	-	309
Net book value:					
At 31 December 2006	1,257	2,616	1,961	-	5,834

The details of the Group's property, plant and equipment pledged for interest-bearing bank and other borrowings granted to the Group are set out in note 34.

As at 31 December 2007, the Group had not obtained real estate certificates or building ownership certificates for certain buildings with a net book value of approximately RMB3,909,000 (2006: RMB5,638,000).

16. PREPAID LAND PREMIUMS/LAND LEASE PAYMENTS

Group

	Note	2007 RMB'000	2006 RMB'000
At cost:			
At beginning of year		47,821	30,037
Additions		43,386	17,784
Disposal of a subsidiary	38	(32,514)	-
At end of year		58,693	47,821
Accumulated amortisation:			
At beginning of year		993	50
Recognised		1,457	943
Disposal of a subsidiary	38	(1,192)	-
At end of year		1,258	993
Net book value:			
At end of year		57,435	46,828
Of which:			
Current portion included in prepayments, deposits and other receivables (note 26)		1,223	968
Non-current portion		56,212	45,860
		57,435	46,828

The Group's leasehold lands are all situated in the PRC and are held under the following lease terms:

	2007 RMB'000	2006 RMB'000
At cost:		
Medium-term leases	58,693	32,514
Long-term leases	-	15,307
	58,693	47,821

17. GOODWILL

Group

	2007 RMB'000	2006 RMB'000
Cost at 1 January 2007	-	-
Acquisition of subsidiaries (note 37)	8,818	-
Cost and net carrying amount at 31 December 2007	8,818	-

Impairment testing of goodwill

Goodwill acquired through business combinations has been allocated to the bearing cash-generating unit, which is a reportable segment, for impairment testing.

The recoverable amount of the cash-generating unit has been determined based on a value in use calculation, using cash flow projections based on financial budgets covering a five-year period. The discount rate applied to the cash flow projections is 10% and cash flows beyond the five-year period are assumed to be stable.

Key assumptions were used in the value in use calculation of bearing cash-generating unit for 31 December 2007. The following describes each key assumption on which management has based its cash flow projections to undertake impairment testing of goodwill:

Budgeted gross margins — The basis used to determine the value assigned to the budgeted gross margins is the average gross margins achieved in the year immediately before the budget year, increased for expected efficiency improvements and expected market development.

Discount rates — The discount rates used are before tax and reflect specific risks relating to the relevant units.

18. OTHER INTANGIBLE ASSETS

Group

	Note	Patents and licences RMB'000	Others RMB'000	Total RMB'000
31 December 2007				
At cost:				
At 1 January 2007		22,181	2,911	25,092
Additions		-	2,902	2,902
Disposal of a subsidiary	38	(20,861)	(2,276)	(23,137)
At 31 December 2007		1,320	3,537	4,857

18. OTHER INTANGIBLE ASSETS (continued)

Group (continued)

	Note	Patents and licences RMB'000	Others RMB'000	Total RMB'000
Accumulated amortisation:				
At 1 January 2007		5,375	715	6,090
Amortisation provided		2,045	726	2,771
Disposal of a subsidiary	38	(7,156)	(210)	(7,366)
At 31 December 2007		264	1,231	1,495
Net book value:				
At 31 December 2007		1,056	2,306	3,362
31 December 2006				
At cost:				
At 1 January 2006		22,181	1,741	23,922
Additions		-	1,170	1,170
At 31 December 2006		22,181	2,911	25,092
Accumulated amortisation:				
At 1 January 2006		3,157	172	3,329
Amortisation provided		2,218	543	2,761
At 31 December 2006		5,375	715	6,090
Net book value:				
At 31 December 2006		16,806	2,196	19,002

19. INTERESTS IN SUBSIDIARIES

Company

	2007 RMB'000	2006 RMB'000
Unlisted investments, at cost	1,506,967	1,064,963
Due from a subsidiary	65,486	53,111
	1,572,453	1,118,074

19. INTERESTS IN SUBSIDIARIES (continued)

Company (continued)

The Company's other receivables, trade payables and other payables and accruals with subsidiaries are disclosed in notes 26, 31 and 33. The amount due from a subsidiary included in the interests in subsidiaries above aggregating RMB65,486,000 (2006: RMB53,111,000) is in respect of non-trade balance, which is unsecured, non-interest-bearing and has no fixed terms of repayment and is therefore classified as non-current. In the opinion of the Company's directors, these advances are considered as quasi-equity loans to the subsidiary. The carrying amount of the balance approximates its fair value.

Particulars of the subsidiaries are as follows:

Name	Place of incorporation/ registration and operations	Registered capital (in '000)	Percentage of equity attributable to the Company Direct	Indirect	Principal activities
Shanghai Tian An Bearing Company Limited 上海天安軸承有限公司	PRC	US$13,103	99%	-	Production and sale of precision and other bearings and ancillary appliances
Wuxi Turbine Blade Company Limited 無錫透平葉片有限公司	PRC	RMB380,460	99.49%	0.51%	Production and sale of turbine blades
Shanghai Tool Works Company Limited 上海工具廠有限公司	PRC	RMB265,113	99.74%	0.26%	Production and sale of cutting tools and accessories
Shanghai Biaowu High Tensile Fasteners Company Limited 上海標五高強度緊固件有限公司	PRC	RMB233,100	98.93%	1.07%	Production and sale of high tensile fasteners and related equipment
Shanghai Tool Works Sales Company Limited 上海工具廠銷售有限公司	PRC	RMB8,140	-	92.81%	Sale of tools, measures and hardware
Shanghai United Bearings Company Limited 上海聯合滾動軸承有限公司	PRC	US$12,670	90%	-	Production and sale of bearings and related specific equipment
Shanghai Electric Bearings Company Limited 上海電气軸承有限公司	PRC	RMB100,000	100%	-	Production and sale of bearing products

During the year, the Group acquired an additional 40% interest in United Bearings and the entire equity interest in Shanghai Electric Bearings Company Limited ("Electric Bearings"). Further details of these acquisitions are included in note 37 to the financial statements.

20. INVESTMENTS IN ASSOCIATES

Group

	2007 RMB'000	2006 RMB'000
Share of net assets	96,155	70,402

The Group's balances of trade receivables, prepayments, deposits and other receivables and trade payables with its associates are disclosed in notes 24, 26 and 31.

Particulars of the associates of the Group are as follows:

Name	Place of incorporation/ registration and operations	Registered capital (in '000)	Percentage of ownership interest attributable to the Group	Principal activities
Shanghai General Bearing Company Limited i, ii 上海通用軸承有限公司	PRC	US$8,750	40%	Production and sale of bearings and spare parts
Shanghai Bearing Import & Export Company Limited ii 上海軸承進出口有限公司	PRC	RMB3,000	30%	Import and export of commodities and technology
Shanghai Morgan Carbon Crucible Company Limited i, ii 上海摩根碳制品有限公司	PRC	US$7,972	30%	Production and sale of carbolic products
S.U. Machine Tool (Shanghai) Company Limited i 上優機床工具(上海)有限公司	PRC	EUR2,500	40%	Design, production and sale of numerical control machine tools with three dimensions and above, and related tools
Shanghai Morganite Electrical Carbon Co., Ltd. i, ii 上海摩根耐特電碳有限公司	PRC	US$8,013	30%	Production and sale of various carbon products

i. Sino-foreign equity joint ventures

ii. The equity interests of these companies are directly owned by the Company.

The following table illustrates the summarised financial information of the Group's associates:

	2007 RMB'000	2006 RMB'000
Assets	440,526	406,023
Liabilities	(167,525)	(197,195)
Revenue	641,566	648,932
Profit	47,657	36,105

20. INVESTMENTS IN ASSOCIATES (continued)

Company

	2007 RMB'000	2006 RMB'000
Unlisted investments, at cost	92,828	68,321

21. AVAILABLE-FOR-SALE INVESTMENTS

	2007 RMB'000	2006 RMB'000
Unlisted investments, at cost	1,072	6,263

All the available-for-sale investments are located in the PRC. Unlisted equity investments are stated at cost because the range of reasonable fair value estimates is so significant that the directors are of the opinion that their fair value cannot be measured reliably.

22. DEFERRED TAX

The movements in deferred tax assets and liabilities during the year are as follows:

Group

Deferred tax assets

	Losses available for offset against future taxable profit RMB'000	Impairment of assets RMB'000	Depreciation in excess of related depreciation allowance RMB'000	Others RMB'000	Total RMB'000
At 1 January 2007					
Per balance sheet					47,036
Offset by deferred tax liabilities					533
Before offset	533	37,837	3,996	5,203	47,569
Effect of tax rate change					
- on opening deferred tax	(129)	(8,532)	(978)	(1,254)	(10,893)
- on deferred tax movement during the year	129	990	67	336	1,522
Acquisition of subsidiaries (note 37)	-	3,909	(57)	67	3,919
Disposal of a subsidiary (note 38)	-	(373)	-	(472)	(845)
Charged to the income statement during the year	(533)	(5,615)	(223)	(1,003)	(7,374)
At 31 December 2007	-	28,216	2,805	2,877	33,898

22. DEFERRED TAX (continued)

Group (continued)

Deferred tax liabilities

	Fair value adjustments arising from: Derivative financial instruments RMB'000	Fair value adjustments arising from: Acquisition of a subsidiary RMB'000	Interest income from oversubscription funds RMB'000	Unremitted earnings RMB'000	Total RMB'000
At 1 January 2007					
Per balance sheet					13,422
Offset by deferred tax assets					533
Before offset	533	1,440	9,708	2,274	13,955
Effect of tax rate change					
- on opening deferred tax	(129)	(349)	(2,353)		(2,831)
- on deferred tax movement during the year	129	234	587		950
Acquisition of subsidiaries (note 37)	-	1,530	-	-	1,530
Credited to the income statement during the year	(533)	(1,159)	(2,427)	(2,274)	(6,393)
At 31 December 2007	-	1,696	5,515	-	7,211

Deferred tax assets

	Losses available for offset against future taxable profit RMB'000	Impairment of assets RMB'000	Depreciation in excess of related depreciation allowance RMB'000	Others RMB'000	Total RMB'000
At 1 January 2006	391	39,380	2,758	3,756	46,285
Credited/(charged) to the income statement during the year	142	(1,543)	1,238	1,447	1,284
Gross deferred tax liabilities at 31 December 2006	533	37,837	3,996	5,203	47,569
Offset by deferred tax liabilities					(533)
Net deferred tax assets at 31 December 2006					47,036

22. DEFERRED TAX (continued)

Group (continued)

Deferred tax liabilities

	Fair value adjustments arising from				
	Derivative financial instruments RMB'000	Acquisition of a subsidiary RMB'000	Interest income from oversubscription funds RMB'000	Unremitted earnings RMB'000	Total RMB'000
At 1 January 2006	-	1,603	-	869	2,472
Charged/(credited) to the income statement during the year	533	(163)	9,708	1,405	11,483
Gross deferred tax liabilities at 31 December 2006	533	1,440	9,708	2,274	13,955
Offset by deferred tax assets					(533)
Net deferred tax liabilities at 31 December 2006					13,422

The Group has no unrecognised tax losses arising in the PRC at each balance sheet date.

Company

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

The Company's deferred tax liabilities as at each balance sheet date relates to the interest income from over-subscription funds.

23. INVENTORIES

Group

	2007 RMB'000	2006 RMB'000
Raw materials	154,796	140,963
Work in progress	170,083	139,588
Finished goods	228,692	249,140
	553,571	529,691

23. INVENTORIES (continued)

Company

	2007 RMB'000	2006 RMB'000
Raw materials	2,475	4,832
Finished goods	299	-
	2,774	4,832

24. TRADE RECEIVABLES

Group

	2007 RMB'000	2006 RMB'000
Trade receivables	394,886	413,429
Impairment	(57,018)	(76,942)
	337,868	336,487

The Group's trading terms with its customers are mainly on credit, except for new customers, where payment in advance or cash on delivery is normally required. The credit period is generally for a period of less than three months. In view of the aforementioned and the fact that the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. Trade receivables are non-interest-bearing.

An ageing analysis of trade receivables as at the balance sheet date, based on the invoice date, and net of provisions, is as follows:

	2007 RMB'000	2006 RMB'000
Within 3 months	311,678	307,106
Over 3 months but within 6 months	21,758	15,800
Over 6 months but within 1 year	3,593	10,258
Over 1 year but within 2 years	804	3,278
Over 2 years	35	45
	337,868	336,487

24. TRADE RECEIVABLES (continued)

Group (continued)

The movements in provision for impairment of trade receivables are as follows:

	2007 RMB'000	2006 RMB'000
At 1 January	76,942	77,594
Impairment losses recognised	7,301	6,680
Acquisition of subsidiaries	4,531	-
Impairment losses reversed	(7,071)	(7,332)
Disposal of a subsidiary	(2,508)	-
Amount written off as uncollectible	(22,177)	-
	57,018	76,942

The above provision for impairment of trade receivables of the Group is provision for both individually and collectively impaired trade receivables with a carrying amount of RMB60,486,000 (2006: RMB77,705,000). The individually impaired trade receivables relate to customers that were in financial difficulties and only a portion of the receivables is expected to be recovered. The Group does not hold any collateral or other credit enhancements over these balances.

The aged analysis of the trade receivables that are not considered to be impaired as follows:

	2007 RMB'000	2006 RMB'000
Neither past due nor impaired	249,533	224,890
Less than 3 month past due	84,695	98,311
3 to 6 months past due	92	7,754
6 to 9 months past due	80	1,579
9 to 12 months past due	-	6
1 to 2 years past due	-	3,184
	334,400	335,724

Receivables that were neither past due nor impaired relate to a large number of diversified customers for whom there was no recent history of default.

Receivables that were past due but not impaired relate to a number of independent customers that have a good track record with the Group. Based on past experience, the directors of the Company are of the opinion that no provision for impairment is necessary in respect of these balances as there has not been a significant change in credit quality and the balances are still considered fully recoverable. The Group does not hold any collateral or other credit enhancements over these balances.

24. TRADE RECEIVABLES (continued)

Group (continued)

The amounts due from a jointly-controlled entity, associates, the related companies over which Shanghai Electric Corporation is able to exert control or significant influence ("SEC group companies") and other related companies included in the above can be analysed as follows:

	2007 RMB'000	2006 RMB'000
Due from a jointly-controlled entity	-	8,627
Due from associates	-	115
Due from SEC group companies	8,208	2,548
Due from other related companies	-	596
	8,208	11,886

Company

	2007 RMB'000	2006 RMB'000
Within 3 months	151,590	142,886
Over 3 months but within 6 months	4,104	4,212
Over 6 months but within 9 months	670	-
	156,364	147,098

The Group's and Company's balances with related parties are unsecured, non-interest-bearing and are repayable on similar credit terms to those offered to the major customers of the Group.

25. BILLS RECEIVABLE

The maturity profiles of the bills receivable of the Group are as follows:

	2007 RMB'000	2006 RMB'000
Within 3 months	64,143	31,153
Over 3 months but within 6 months	17,386	40,830
	81,529	71,983

Included in the above balance are bills of RMB800,000 (2006: RMB7,375,000) issued by SEC group companies.

The balances are unsecured, non-interest-bearing and are repayable as the bills fall due.

26. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

Group

	2007 RMB'000	2006 RMB'000
Prepayments as purchase deposits	74,186	32,008
Receivables for sales of non-trade assets	82	755
Deposits	977	3,996
Prepaid land premiums/land lease payments (note 16)	1,223	968
Value-added tax refundables and prepaid value-added tax	14,294	29,126
Other receivables	10,108	17,236
Due from a jointly-controlled entity	-	10,308
Due from associates	-	1,183
Due from ultimate holding company	10,135	3,357
Due from SEC group companies	2,323	3,374
Due from other related companies	-	5,477
	113,328	107,788

Company

	2007 RMB'000	2006 RMB'000
Prepayments as purchase deposits	14,449	3,763
Deposits	567	-
Other receivables	1,073	40,166
Value-added tax refundables and prepaid value-added tax	14,083	-
Due from a jointly-controlled entity	-	20,615
Due from ultimate holding company	6,325	-
Due from SEC group companies	1,069	-
Due from subsidiaries	248,376	407
	285,942	64,951

The Group's and Company's balances with related parties are unsecured, non-interest-bearing and are repayable on demand or within one year.

None of the above assets is either past due or impaired. The financial assets included in the above balances relate to receivables for which there was no recent history of default.

27. LOAN RECEIVABLE

The balance of RMB22,000,000 (2006: RMB28,278,000) represents an entrusted loan provided by the Company to United Bearings through China Construction Bank. The loan is unsecured, bearing an interest rate of 6.32% (2006: 5.58%) per annum and for a period of one year beginning from 28 September 2007 (2006: 27 October 2006). The carrying amount of the loan approximates to its fair value.

28. HELD-TO-MATURITY INVESTMENT

The balance represents an investment in the money market for a period of 40 days commencing 11 December 2007 which bears an expected interest rate of 3.8% per annum.

29. DERIVATIVE FINANCIAL INSTRUMENTS

Balance at 31 December 2006 represented various forward currency contracts entered into by the Company to manage its exchange rate exposures which did not meet the criteria for hedge accounting. Changes in the fair value of non-hedging currency derivatives amounting to RMB1,615,000 were credited to the income statement during the year ended 31 December 2006.

30. CASH AND CASH EQUIVALENTS AND RESTRICTED DEPOSITS

Group

	2007 RMB'000	2006 RMB'000
Cash and bank balances	262,163	260,974
Time deposits	619,973	926,149
	882,136	1,187,123
Less: Restricted deposits	18,833	659,805
Cash and cash equivalents	863,303	527,318

The restricted deposits can be analysed as follows:

	2007 RMB'000	2006 RMB'000
Pledged bank balances and time deposits secured for:		
Bank loans	-	2,941
Trade finance facilities	18,833	3,829
Restricted bank balances and time deposits not allowed to be withdrawn before maturity	-	653,035
	18,833	659,805

30. CASH AND CASH EQUIVALENTS AND RESTRICTED DEPOSITS (continued)

Group (continued)

The Group's cash and bank balances are denominated in RMB at each balance sheet date, except for the followings:

	2007		2006	
	Original currency in'000	RMB equivalent in'000	Original currency in'000	RMB equivalent in'000
Cash and bank balances:				
US$	826	6,033	525	4,097
JPY	12,615	808	683	45
HK$	215	201	696,744	699,998

The RMB is not freely convertible into other currencies, however, under the PRC Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.

Company

	2007 RMB'000	2006 RMB'000
Cash and bank balances	414,844	1,037,220
Less: Restricted deposits	-	653,035
Cash and cash equivalents	414,844	384,185

The restricted deposits can be analysed as follows:

	2007 RMB'000	2006 RMB'000
Restricted bank balances and time deposits not allowed to be withdrawn before maturity	-	653,035

The Company's cash and bank balances are denominated in RMB at each balance sheet date, except for an amount of RMB201,000 (2006: RMB699,998,000) which is denominated in HK$215,000 (2006: HK$696,744,000).

Cash at bank earns interest at floating rates based on daily bank deposit rates. Short-term time deposits are made for varying periods within six months depending on the immediate cash requirements of the Group, and earn interest at the respective short-term time deposit rates. The bank balances and pledged deposits are deposited with creditworthy banks with no recent history of default. The carrying amounts of the cash and cash equivalents and the restricted deposits approximates to their fair values.

31. TRADE PAYABLES

The trade payables are non-interest-bearing and are normally settled on 60-day terms. An ageing analysis of trade payables, based on the invoice date, is as follows:

Group

	2007 RMB'000	2006 RMB'000
Within 3 months	291,830	332,930
Over 3 months but within 6 months	54,089	55,656
Over 6 months but within 1 year	6,893	14,710
Over 1 year but within 2 years	1,436	2,371
Over 2 years	6,631	7,006
	360,879	412,673

The amounts due to associates and SEC group companies included in the above can be analysed as follows:

	2007 RMB'000	2006 RMB'000
Due to associates	-	39
Due to SEC group companies	7,400	6,045
	7,400	6,084

Company

	2007 RMB'000	2006 RMB'000
Within 3 months	106,820	109,512

The amount due to a subsidiary of RMB91,918,000 (2006: RMB99,201,000) is included in the Company's trade payables.

The Group's and Company's balances with related parties are unsecured, non-interest-bearing and payable on similar credit terms to those offered to the Group by its major suppliers.

32. BILLS PAYABLE

The maturity profiles of the bills payable are as follows:

	Group		Company	
	2007 RMB'000	2006 RMB'000	2007 RMB'000	2006 RMB'000
Within 3 months	25,500	11,800	-	10,000
Over 3 months but within 6 months	24,960	-	-	-
	50,460	11,800	-	10,000

33. OTHER PAYABLES AND ACCRUALS

Group

	2007 RMB'000	2006 RMB'000
Advance from customers	19,355	54,821
Other tax payables	25,525	21,348
Staff cost payables	19,431	40,993
Interest payables	4,743	4,768
Payables for purchases of non-trade assets	3,579	6,057
Accruals	9,150	13,151
Other payables	7,545	5,522
Due to ultimate holding company	557	2,536
Due to SEC group companies	22,643	39,526
	112,528	188,722

Company

	2007 RMB'000	2006 RMB'000
Advance from customers	10,053	8,375
Other payables	798	1,992
Accruals	1,810	5,658
Due to SEC group companies	1,517	-
Due to subsidiaries	301,328	194,093
	315,506	210,118

Other payables are non-interest-bearing and have average terms of one to three months. The Group's and Company's balances with related parties are unsecured and are repayable on demand or within one year.

34. INTEREST-BEARING BANK AND OTHER BORROWINGS

Group

	2007			2006		
	Effective interest rate (%)	Maturity	RMB'000	Effective interest rate (%)	Maturity	RMB'000
Current						
Bank loans						
- secured	-	-	-	5.0 - 5.3	2007	75,000
- unsecured	5.1 - 6.6	2008	75,000	5.4 - 6.1	2007	15,000
			75,000			90,000
Non-current						
Other loans						
- unsecured	-	Not fixed	17,000	-	Not fixed	17,000
			92,000			107,000
Analysed into:						
Bank loans repayable:						
Within one year or on demand			75,000			90,000
Other loans repayable:						
Beyond five years			17,000			17,000
			92,000			107,000

There were no secured bank loans as at 31 December 2007.

Certain of the Group's bank loans at 31 December 2006 were secured by:

(i) mortgages over certain of the Group's buildings, land use right and machineries with aggregate net book value of approximately RMB120,318,000 at 31 December 2006; and

(ii) pledge of certain of the Group's bank balances and time deposits as set out in note 30.

The Group's other loans were borrowed from non-banking financial institutions and are not expected to be repaid within one year.

The Group's bank and other borrowings are all denominated in RMB.

The carrying amounts of the Group's bank and other borrowings approximate to their fair values.

35. ISSUED CAPITAL

	2007		2006	
	Number of shares '000	Amount RMB'000	Number of shares '000	Amount RMB'000
Registered, issued and fully paid:				
Domestic shares of RMB1.00 each, currently not listed				
– State-owned shares	678,576	678,576	678,576	678,576
H Shares of RMB1.00 each	759,710	759,710	759,710	759,710
	1,438,286	1,438,286	1,438,286	1,438,286

The domestic shares are currently not listed on any stock exchange.

The holders of domestic shares and H shares are entitled to receive dividends as and when declared by the Company. All domestic shares and H shares carry one vote per share without restriction.

A summary of the transactions during the year with reference to the above movements in the Company's issued share capital is as follows:

	Number of shares in issue '000	Issued share capital RMB'000	Share premium account RMB'000	Total RMB'000
At 1 January 2006	747,640	747,640	-	747,640
Shares issued on 27 April 2006	690,646	690,646	809,834	1,500,480
	1,438,286	1,438,286	809,834	2,248,120
Share issue expenses	-	-	(118,617)	(118,617)
At 31 December 2006 and 31 December 2007	1,438,286	1,438,286	691,217	2,129,503

36. RESERVES

(a) Group

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity on page 41 of the financial statements.

36. RESERVES (continued)

(a) Group (continued)

Surplus reserves

In accordance with the PRC Company Law and the articles of association of the relevant companies, the Company, its subsidiaries and jointly-controlled entity are required to appropriate certain percentage of their net profits after tax to the surplus reserves comprising statutory common reserve and discretionary common reserve. Subject to certain restrictions set out in the relevant PRC regulations and in the Group companies' articles of association, the statutory common reserve may be used either to offset losses, or to be converted to increase share capital; and the discretionary common reserve is set aside to cover unexpected losses. These reserves cannot be used for purposes other than those for which they are created.

Contributed surplus

The Group's contributed surplus represents the difference between (i) the Company's cost of investments in the subsidiaries and an associate acquired from Shanghai Electric Corporation and Shanghai Electric Industrial Corporation ("Shiye") as part of the Group reorganisation, and (ii) the aggregate amount of the paid-up capital of those subsidiaries attributable to the Group and the then carrying value of the Group's investment in the associate upon the establishment of the Company.

Capital reserve

The capital reserve of the Group includes the Company's share premium of RMB691,217,000 and the non-distributable reserves of the Company and its subsidiaries created in accordance with accounting and financial regulations in the PRC.

Distributable reserves

The amount for which the Company can legally distribute by way of a dividend is determined based on the lower of the retained profits determined in accordance with the generally accepted accounting principles in the PRC and the HKFRSs. As at the balance sheet date, the Company has distributable reserve amounted to RMB55,812,000 (2006: RMB169,810,000), of which RMB55,806,000 (2006: RMB57,531,000) has been proposed as a final dividend for the year. The Company's share premium account in the amount of RMB691,217,000 (2006: RMB691,217,000) may be distributed in the form of fully paid bonus shares.

36. RESERVES (continued)

(b) Company

	Capital reserves RMB'000	Surplus reserves RMB'000	(Accumulated losses)/ retained profits RMB'000	Total RMB'000
At 1 January 2006	-	5,623	(6,316)	(693)
Issue of shares	809,834	-	-	809,834
Share issue expenses	(118,617)	-	-	(118,617)
Profit for the year	-	-	24,335	24,335
Transfer to capital reserve	28,604	-	(28,604)	-
Appropriation to surplus reserves	-	16,995	(16,995)	-
Proposed final 2006 dividends	-	-	(57,531)	(57,531)
At 31 December 2006 and 1 January 2007	719,821	22,618	(85,111)	657,328
Profit for the year	-	-	104,797	104,797
Transfer to capital reserve	(27,268)	-	27,268	-
Appropriation to surplus reserves	-	(9,454)	9,454	-
Proposed final 2007 dividends (note 13)	-	-	(55,806)	(55,806)
At 31 December 2007	692,553	13,164	602	706,319

The capital reserve account balance as at 31 December 2007 included the Company's share premium of RMB691,217,000 (2006: RMB691,217,000).

37. BUSINESS COMBINATIONS

During the year ended 31 December 2007, the Group acquired the following companies:

(a) On 1 March 2007, the Group completed its acquisition of an additional 40% interest in United Bearings from the foreign investor of United Bearings and thus increased its equity interest in United Bearings to 90%. Prior to the acquisition, United Bearings was a jointly-controlled entity of the Company and was accounted for in the Group's consolidated financial statements using proportionate consolidation method. United Bearings is engaged in the production and sale of bearings and related specific equipment. Other details of United Bearings are set out in note 19 to the financial statements. The purchase consideration of RMB30,000,000 for the acquisition was in the form of cash, which has been fully paid up to the balance sheet date.

(b) On 30 November 2007, the Group acquired the entire equity interest in Electric Bearings, a subsidiary of Shanghai Electric Corporation. Electric Bearings is engaged in the production and sale of bearing products. The purchase consideration of RMB32,486,000 for the acquisition was in the form of cash and was paid on 21 September 2007.

37. BUSINESS COMBINATIONS (continued)

The aggregated fair values of the identifiable assets and liabilities of United Bearings and Electric Bearings as at the date of acquisition and the corresponding aggregated carrying amounts immediately before the acquisition were as follows:

	Notes	Fair value recognised on acquisition RMB'000	Carrying amount RMB'000
Property, plant and equipment	15	70,190	64,070
Available-for-sale investments		200	200
Deferred tax assets	22	7,837	7,837
Inventories		53,384	53,384
Trade receivables		42,145	42,145
Bills receivable		10,481	10,481
Prepayments, deposits and other receivables		43,560	43,541
Cash and cash equivalents		10,610	10,610
Trade payables		(57,857)	(57,857)
Tax payable		(2,214)	(2,214)
Other payables and accruals		(33,363)	(33,363)
Interest-bearing bank and other borrowings		(58,000)	(58,000)
Deferred tax in relation to fair value adjustments	22	(1,530)	-
Minority interests		(5,296)	(4,837)
		80,147	75,997
Goodwill on acquisition	17	8,818	
Revaluation surplus relating to previously held interests		(2,295)	
		86,670	
Satisfied by:			
Cash		62,486	
Proportionate consolidation before business combination		24,184	
		86,670	

37. BUSINESS COMBINATION (continued)

An analysis of the net outflow of cash and cash equivalents in respect of the acquisition of subsidiaries was as follows:

	RMB'000
Cash consideration	62,486
Cash and cash equivalents acquired	(10,610)
Offset by cash and cash equivalents recognised by the proportionate consolidation before the business combination	5,139
Net outflow of cash and cash equivalents in respect of the acquisition of subsidiaries	57,015

Since its acquisition, United Bearings contributed RMB240,967,000 to the Group's turnover and RMB17,078,000 to the consolidated profit for the year ended 31 December 2007. These figures include the Group's share of United Bearings' turnover and profit of RMB120,483,000 and RMB8,539,000, respectively, under proportionate consolidation for the said year had the acquisition not taken place and United Bearings remained a jointly-controlled entity of the Group. Electric Bearings contributed RMB324,000 to the Group's consolidated profit for the year ended 31 December 2007 since its acquisition.

Had the combinations taken place at the beginning of the year, the revenue from continuing operations and profit of the Group for the year would have been RMB2,911,165,000 and RMB232,915,000 respectively.

38. DISPOSAL OF A SUBSIDIARY

On 30 November 2007, the Group disposed of its entire 60% interest in Nanyang Motor for a total consideration of RMB128,893,000. Total consideration consisted of sales consideration of RMB122,568,000 according to the share transfer agreement entered into between the Company and Shanghai Electric Corporation on 16 August 2007 and an additional consideration of RMB6,325,000 according to the supplementary share transfer agreement entered into between the Company and Shanghai Electric Corporation on 11 November 2007 (note 43(b)).

	Notes	2007 RMB'000
Net assets disposed of:		
Property, plant and equipment	15	144,709
Prepaid land premiums/land lease payments	16	31,322
Other intangible assets	18	15,771
Long-term prepayments		368
Deferred tax assets	22	845
Inventories		161,464
Trade receivables		54,798
Bills receivable		80,012
Prepayments, deposits and other receivables		9,205

38. DISPOSAL OF A SUBSIDIARY (continued)

	Notes	2007 RMB'000
Restricted deposits		348
Cash and cash equivalents		11,069
Trade payables		(196,115)
Tax payable		(1,614)
Other payables and accruals		(46,943)
Interest-bearing and other borrowings		(75,000)
Minority interests		(75,530)
Contributed surplus		666
		115,375
Gain on disposal of a subsidiary	5	13,518
		128,893
Satisfied by:		
Cash		122,568
Prepayments, deposits and other receivables		6,325
		128,893

An analysis of the net inflow of cash and cash equivalents in respect of the disposal of a subsidiary is as follows:

	2007 RMB'000
Cash consideration	122,568
Cash and cash equivalents disposed of	(11,069)
Net inflow of cash and cash equivalents in respect of the disposal of a subsidiary	111,499

39. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

Major non-cash transactions

(i) During the year, the Group disposed of its 60% interest in Nanyang Motor for a total consideration of RMB128,893,000, RMB6,325,000 of which has not been received as at year end; and

(ii) During the year, the Group acquired a 30% interest in Shanghai Morganite Electrical Carbon Co., Ltd ("Shanghai Morganite") for a total consideration of RMB19,988,000. As at 31 December 2007, an amount of RMB1,517,000 has not been paid.

40. OPERATING LEASE COMMITMENTS

(a) The Group

(i) As lessor

The Group leases out certain of its buildings and plant and machinery under operating lease arrangements, with leases negotiated for terms ranging from 3 to 5 years. The terms of the leases generally also require tenants to pay security deposits and provide for periodic rent adjustments according to the prevailing market conditions.

As at 31 December 2007, the Group had total future minimum lease receivables under non-cancellable operating leases with its tenants falling due as follows:

	2007 RMB'000	2006 RMB'000
Within one year	270	308
In the second to fifth years, inclusive	261	480
Total	531	788

(ii) As lessee

The Group leases certain land, buildings and motor vehicles under operating lease arrangements, with leases negotiated for terms ranging from 1 to 20 years.

As at 31 December 2007, the Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	2007 RMB'000	2006 RMB'000
Within one year	21,401	23,690
In the second to fifth years, inclusive	21,502	25,465
After five years	7,049	8,543
Total	49,952	57, 698

(b) The Company

The Company leases certain offices under operating lease arrangements with a lease term of one year. As at 31 December 2007, the Company had future minimum lease payments under non-cancellable operating leases of RMB2,033,000 (2006: RMB2,070,000).

41. COMMITMENTS

(a) The Group

In addition to the operating lease commitments detailed in note 40(a)(ii) above, the Group had the following capital commitments as at 31 December 2007:

	2007 RMB'000	2006 RMB'000
Contracted, but not provided for:		
Land and buildings	325	24,569
Plant and machinery	59,775	163,945
Intangible assets	900	1,891
Others	-	21,000
	61,000	211,405
Authorised, but not contracted for:		
Land and buildings	26,512	26,512
Plant and machinery	115,688	279,350
	142,200	305,862
Total	203,200	517,267

(b) The Company

The Company had the following capital commitments as at 31 December 2007:

	2007 RMB'000	2006 RMB'000
Contracted, but not provided for:		
Intangible assets	900	1,891
Others	-	21,000
Total	900	22,891

42. CONTINGENT LIABILITIES

(a) The Group

	2007 RMB'000	2006 RMB'000
Guarantees given to banks in connection with banking facilities granted to and utilised by:		
- Jointly-controlled entity	-	30,000
- Associates	1,800	25,500
	1,800	55,500

42. CONTINGENT LIABILITIES (continued)

(b) The Company

	2007 RMB'000	2006 RMB'000
Guarantees given to banks in connection with banking facilities granted to and utilised by:		
- Jointly-controlled entity	-	3,000
- Associates	-	24,000
	-	27,000

43. RELATED PARTY TRANSACTIONS

(a) In addition to the transactions detailed elsewhere in these financial statements, the Group had the following material transactions with related parties during the year:

	Notes	2007 RMB'000	2006 RMB'000
Purchase of materials from:	(i)		
Associates		341	-
SEC group companies		4,296	31,481
Other related companies		-	1,679
		4,637	33,160
Sales of goods to:	(i)		
Jointly-controlled entity *		4,615	23,407
Associates		670	-
SEC group companies		210,912	223,438
		216,197	246,845
Sales of scraps and spare parts to:	(i)		
SEC group companies		-	2,807
		-	2,807
Receiving of manpower services from:	(i)		
SEC group companies		12	3,494
		12	3,494

43. RELATED PARTY TRANSACTIONS (continued)

(a) (continued)

	Notes	2007 RMB'000	2006 RMB'000
Rendering of manpower services to:	(i)		
SEC group companies		555	6
Other related companies		-	16
		555	22
Purchase of property, plant and equipment from:	(i)		
SEC group companies		392	2,206
Other related companies		-	687
		392	2,893
Rental fee payable to:	(ii)		
Ultimate holding company		4,261	2,805
SEC group companies		18,956	20,132
		23,217	22,937
Interest income from:	(iii)		
Jointly-controlled entity *		126	717
		126	717
Dividend income from:			
SEC group companies		1,354	-
		1,354	-

Notes:

i. The sales and purchases were conducted in accordance with mutually agreed terms with reference to the market conditions.

ii. The rental fee was based on mutually agreed terms with reference to market rates.

43. RELATED PARTY TRANSACTIONS (continued)

(a) (continued)

Notes: (continued)

iii. The interest income and interest expenses were based on mutually agreed terms with reference to market rates.

* The amounts of transactions with the jointly-controlled entity disclosed in the tables above are arrived at after deducting the Group's share portion, which has been eliminated in the proportionate consolidation of the Group's investment in the jointly-controlled entity.

(b) Other transactions with related parties

(i) During the year, the ultimate holding company leased certain properties to United Bearings with no consideration. The directors are of the opinion that the prevailing rental on these properties with reference to market rate is RMB1,105,000 per annum.

(ii) During the year, one of the SEC group companies leased certain properties to Shanghai Tool Works Company Limited, a wholly-owned subsidiary of the Company, with no consideration. The directors are of the opinion that the prevailing rental on these properties with reference to market rate is RMB3,292,000 per annum.

(iii) During the year, two subsidiaries of Sweden Ruihua Group Corporation ("Ruihua"), who owns 40% equity interest in Nanyang Motor, leased certain properties to Nanyang Motor with no consideration. The directors are of the opinion that the prevailing rental on these properties with reference to market rate is RMB2,427,000 for the period from 1 January 2007 to 30 November 2007.

(iv) During the year, the Group acquired a 30% minority interest in Shanghai Morganite from Shiye for a consideration of RMB19,988,000 which was determined with reference to valuations carried out by independent professional qualified valuers in Mainland China.

(v) During the year, Biaowu Fasteners entered into a property purchase agreement with Shanghai Tongqiang Fastener Company Limited ("Tongqiang"), a subsidiary of Shanghai Electric Corporation, to acquire certain land use right and property, plant and equipment from Tongqiang for a consideration of RMB97,970,000, which was determined with reference to valuations carried out by independent professional qualified valuers in Mainland China.

(vi) During the year, the Group disposed of a 60% interest in a subsidiary, Nanyang Motor, to Shanghai Electric Corporation for a consideration of RMB128,893,000 (note 38).

43. RELATED PARTY TRANSACTIONS (continued)

(b) Other transactions with related parties (continued)

(vii) Biaowu Fasteners, disposed of 16% interest in Tongqiang to Shanghai Fasteners Import and Export Company Limited, a subsidiary of Shanghai Electric Corporation, for a consideration of RMB6,423,000, which was determined with reference to valuations carried out by independent professional qualified valuers in Mainland China.

(viii) During the year, the Group acquired 100% equity interest in Electric Bearings from Shanghai Electric Corporation for a consideration of RMB32,486,000 which was determined with reference to valuations carried out by independent professional qualified valuers in Mainland China.

(c) Guarantees provided to related companies of the Group

As disclosed in note 42, the Group provided corporate guarantees totalling RMB1,800,000 (2006: RMB55,500,000) to related companies. The expiry dates of such guarantees fall between 11 January 2008 and 26 February 2008.

(d) Balances due from/to related parties

The balances due from/to related parties during the year mainly result from trading transactions, bills receivable, deposits and miscellaneous amounts reimbursable by/to the related parties. Further details are set out in notes 24, 25, 26, 31, and 33.

(e) Compensation of the key management personnel of the Group

	2007 RMB'000	2006 RMB'000
Fees	587	457
Short-term employee benefits	2,387	2,394
Post-employment benefits	123	117
	3,097	2,968

Further details of directors' and supervisors' emoluments are included in note 8.

The related party transactions with the ultimate holding company, SEC group companies and subsidiaries of Ruihua also constitute connected transactions or continuing connected transactions as defined in Chapter 14A of the Listing Rules.

44. FINANCIAL INSTRUMENTS BY CATEGORY

The carrying amounts of each of the categories of financial instruments as at the balance sheet date are as follows:

Group

Financial assets

	2007				2006			
	Held-to-maturity investment RMB'000	Loans and receivables RMB'000	Available-for-sale investments RMB'000	Total RMB'000	FA RMB'000	Loans and receivables RMB'000	Available-for-sale investments RMB'000	Total RMB'000
Held-to-maturity investment	80,000	-	-	80,000	-	-	-	-
Available-for-sale investments	-	-	1,072	1,072	-	-	6,263	6,263
Trade and bills receivables	-	419,397	-	419,397	-	408,470	-	408,470
Financial assets included in prepayments, deposits and other receivables	-	23,625	-	23,625	-	45,686	-	45,686
Loan receivable	-	-	-	-	-	14,139	-	14,139
Derivative financial instruments	-	-	-	-	1,615	-	-	1,615
Restricted deposits	-	18,833	-	18,833	-	659,805	-	659,805
Cash and cash equivalents	-	863,303	-	863,303	-	527,318	-	527,318
	80,000	1,325,158	1,072	1,406,230	1,615	1,655,418	6,263	1,663,296

"FA" represents financial assets at fair value through profit or loss upon recognition.

Financial liabilities

	Financial liabilities at amortised cost	
	2007 RMB'000	2006 RMB'000
Trade and bills payables	411,339	424,473
Financial liabilities included in other payables and accruals	64,009	107,412
Interest-bearing bank and other borrowings	92,000	107,000
Other long-term payables	3,465	6,309
	570,813	645,194

44. FINANCIAL INSTRUMENTS BY CATEGORY (continued)

Company

Financial assets

	2007			2006		
	Held-to-maturity investment RMB'000	Loans and receivables RMB'000	Total RMB'000	FA RMB'000	Loans and receivables RMB'000	Total RMB'000
Held-to-maturity investment	80,000	-	80,000	-	-	-
Trade receivables	-	156,364	156,364	-	147,098	147,098
Financial assets included in prepayments, deposits and other receivables	-	271,493	271,493	-	61,188	61,188
Loan receivable	-	22,000	22,000	-	28,278	28,278
Derivative financial instruments	-	-	-	1,615	-	1,615
Restricted deposits	-	-	-	-	653,035	653,035
Cash and cash equivalents	-	414,844	414,844	-	384,185	384,185
	80,000	864,701	944,701	1,615	1,273,784	1,275,399

"FA" represents financial assets at fair value through profit or loss upon recognition.

Financial liabilities

	Financial liabilities at amortised cost	
	2007 RMB'000	2006 RMB'000
Trade and bills payables	106,820	119,512
Financial liabilities included in other payables and accruals	305,453	201,660
	412,273	321,172

45. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments comprise bank loans, other interest-bearing loans and cash and short-term deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as trade receivables and trade payables, which arise directly from its operations.

The Group also enters into derivative transactions, including principally forward currency contracts. The purpose is to manage the currency risks arising from the Group's operations and its cash and bank balances and restricted deposits.

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. The board of directors reviews and agrees policies for managing each of these risks and they are summarised below. The Group's accounting policies in relation to derivatives are set out in note 2.4 to the financial statements.

(i) Interest rate risk

The interest rates and the terms of repayment of the Group's bank and other borrowings are disclosed in note 34 above. The Group has no significant exposure to interest rate risk as all the current interest-bearing bank borrowings are subject to fixed interest rates and non-current loans are non-interest-bearing.

(ii) Foreign currency risk

The Group's exposure to market risk for changes in foreign currency exchange rates relates primarily to certain trade receivables and certain cash and cash equivalents in currencies other than the functional currency of RMB.

The following table demonstrates the sensitivity at the balance sheet date to a reasonably possible change in the United States dollar / Euro exchange rate, with all other variables held constant, of the Group's profit before tax (due to changes in the fair value of monetary assets and liabilities).

45. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(ii) Foreign currency risk (continued)

	Increase/ (decrease) in US$ or EUR rate %	Increase/ (decrease) in profit before tax attriutable to continuing operations RMB'000
2007		
If US$ weakens against RMB	5	(5,947)
If EUR weakens against RMB	5	(1,034)
If US$ strengthens against RMB	(5)	5,947
If EUR strengthens against RMB	(5)	1,034
2006		
If US$ weakens against RMB	5	(5,579)
If EUR weakens against RMB	5	(1,056)
If US$ strengthens against RMB	(5)	5,579
If EUR strengthens against RMB	(5)	1,056

(iii) Credit risk

The carrying amount of trade receivables included in the consolidated balance sheet represents the Group's maximum exposure to credit risk in relation to the Group's trade receivables. The Group does not have a significant concentration of credit risk in relation to trade receivables as the trade receivables due from the five largest customers accounted for only 14% of the Group's total trade receivables as at 31 December 2007.

The Group performs ongoing credit evaluations of its customers' financial conditions. The impairment of trade receivables is based upon a review of the expected collectibility of all trade receivables.

45. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(iii) Credit risk (continued)

The credit risk of the Group's other financial assets, which comprise cash and cash equivalents and other receivables, arises from default of the counterparty, with a maximum exposure being equal to the carrying amount of these instruments. There are no significant concentrations of credit risk within the Group in relation to the other financial assets.

Further quantitative data in respect of the Groups' exposure to credit risk arising from trade and other receivables are disclosed in notes 24 and 26 to the financial statements.

(iv) Liquidity risk

The Group monitors its risk to a shortage of funds using a recurring liquidity planning tool. This tool considers the maturity of both its financial instruments and financial assets (e.g. trade receivables) and projected cash flows from operations.

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank and other loans. In addition, banking facilities have been put in place for contingency purposes.

The maturity profile of the Group's and the Company's financial liabilities as at the balance sheet date, based on the contracted undiscounted payments, were as follows:

Group

	2007					
	On demand RMB'000	Less than 3 months RMB'000	3 to less than 12 months RMB'000	1 to 5 years RMB'000	Over 5 years RMB'000	Total RMB'000
Trade and bills payables	105,269	269,431	36,639	-	-	411,339
Financial liabilities included in other payables and accruals	28,061	34,444	1,504	-	-	64,009
Interest-bearing bank and other borrowings	-	9,000	66,000	-	17,000	92,000
Other long-term payables	-	-	-	3,465	-	3,465
	133,330	312,875	104,143	3,465	17,000	570,813

45. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(iv) Liquidity risk (continued)

Group (continued)

	2006					
	On demand RMB'000	Less than 3 months RMB'000	3 to less than 12 months RMB'000	1 to 5 years RMB'000	Over 5 years RMB'000	Total RMB'000
Trade and bills payables	28,070	234,794	161,609	-	-	424,473
Financial liabilites included in other payables and accruals	87,109	20,265	38	-	-	107,412
Interest-bearing bank and other borrowings	-	56,000	34,000	-	17,000	107,000
Other long-term payables	-	-	-	6,309	-	6,309
	115,179	311,059	195,647	6,309	17,000	645,194

Company

	2007					
	On demand RMB'000	Less than 3 months RMB'000	3 to less than 12 months RMB'000	1 to 5 years RMB'000	Over 5 years RMB'000	Total RMB'000
Trade payables	-	106,820	-	-	-	106,820
Financial liabilities included in other payables and accruals	269,329	34,511	1,613	-	-	305,453
	269,329	141,331	1,613	-	-	412,273

	2006					
	On demand RMB'000	Less than 3 months RMB'000	3 to less than 12 months RMB'000	1 to 5 years RMB'000	Over 5 years RMB'000	Total RMB'000
Trade and bills payables	-	119,512	-	-	-	119,512
Financial liabilities included in other payables and accruals	194,064	7,300	296	-	-	201,660
	194,064	126,812	296	-	-	321,172

45. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

Fair value

Fair value estimates are made at a specific point in time and are based on relevant market information and information about the financial instrument. These estimates are subjetive in nature and involve uncertainties and matters of significant judgement and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

The carrying amounts of financial instruments of the Group and of the Company approximated to their fair values due to the short term to maturity at each of the balance sheet dates.

Capital management

The primary objective of the Group's capital management is to safeguard the Group's ability to continue as a going concern and to maintain healthy capital ratios in order to support its business and maximise shareholder value.

The Group manages its capital structure and makes adjustments to it, in the light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. No changes were made in the objectives, policies or processes during the year ended 31 December 2007 and 31 December 2006.

The Group monitors capital using a gearing ratio, which represents the ratio of interest-bearing bank and other borrowings to equity attributable to equity holders of the Company.

The gearing ratios as at the balance sheet dates were as follows:

Group

	2007 RMB'000	2006 RMB'000
Interest-bearing bank and other borrowings	92,000	107,000
Equity attributable to equity holders of the Company	2,527,371	2,356,847
Gearing ratio	3.6%	4.5%

46. POST BALANCE SHEET EVENTS

On 17 January 2008, the board of directors has approved a project of building the manufacturing base for 1,000 MW extra large nuclear power generation turbine blades and technology upgrades for manufacturing aviation blade forgings for Wuxi Trubine Blade. Approved total project cost was RMB918.7 million, which includes RMB850 million for purchases of property, plant and equipment and RMB68.7 million as working capital for the project. At the date of this report, total authorised and contracted expenditure amounted to RMB65 million.

47. COMPARATIVE AMOUNTS

The comparative income statement has been represented as if the operation discontinued during the current year had been discontinued at the beginning of the comparative period (note 12).

48. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 28 March 2008.